

U.S. - EU Dialogue on Making Ventures Grow

Brussels, Belgium

May 5, 2015

Summary written by Karen E. Wilson, Senior Fellow, Bruegel

On May 5, 2015, the U.S. Mission to the European Union and the European Business Angels Network (EBAN) co-hosted a high-level dialogue among private sector investors and policy makers from Europe and the United States. The focus of the discussions was to identify what key players on both sides of the Atlantic can do to support the EU's efforts to unleash and attract venture capital and other forms of entrepreneurial finance to help ventures grow in Europe. Access to capital is critical for startups and young innovative firms, particularly in the context of the European Commission's efforts to promote private sector investment in Europe through President Juncker's Investment Plan and efforts to deepen capital markets in Europe through the proposed Capital Markets Union (CMU), among other efforts.

10 Recommended Action Points: In the course of the dialogue, participants in the high-level group proposed the following action points to the European Commission:

1) Pursue an integrated, diverse and resilient financial market approach to stimulate growth

The Capital Markets Union has the opportunity to drive longer term change in the financial markets in Europe. Bold action should be taken to implement the proposed CMU to broaden Europe's capital markets as well as to move towards a more integrated pan-European market for capital. More integrated and efficient capital markets will complement the banking sector and increase the flexibility and speed with which European start-ups and SMEs access finance.

2) Diversify funding sources by fostering an equity culture in Europe

Stimulate an investment risk culture in order to fund SMEs, particularly start-ups and young innovative firms with high growth potential. Early stage investors, including crowd funders, angel investors and venture capitalists, contribute to the creation and growth of companies, accepting a level of risk beyond the scope of banks. The CMU should aim to attract equity financing to Europe from pools of capital held by institutional investors, corporate ventures and international investors, as well as by families and individuals. This requires adjusting the current fiscal bias against equity. As long as equity capital is more "expensive" than debt, there will be little incentive for the broader capital markets to develop.

3) Address regulatory and legal barriers

Existing legislation should be reviewed to check for unintended negative consequences on entrepreneurs and/or investors in start-ups and growth firms. In addition, progress needs to be made on addressing regulatory fragmentation across Europe in areas such as insolvency law and taxation. In many European countries, there is inadequate scope for companies to declare bankruptcy, which would allow them to restructure or more effectively close their businesses without lasting penalties that prevent future start-ups. Also, tax levels and tax incentives vary dramatically across Europe making it difficult for entrepreneurs and investors to conduct business across borders.

4) Work towards a European Single Market

To move towards a European Single Market, there must be more convergence in framework conditions across Europe. Starting with particular sectors, such as is being done with the energy union and the digital single market, can be helpful in moving the broader single market agenda ahead. The creation of a special pan-European status or start-up regime to facilitate and speed the start-up and growth of innovative young firms would be helpful.

5) Provide appropriate incentives to attract private investors

While there is no shortage of money, European investors and large international pools of capital have a proportion of their assets invested in Europe that is lower than Europe's relative economic importance. There was a general perception in the group that Europe needs to "market" itself better to attract the appropriate level of funding. For start-ups, smart money is needed, not just more money.

Recommendations for increasing private investment include:

- Venture capital: create an EU level fund-of-funds, which is private sector led but with incentives provided by the EU (guarantees or asymmetric profit sharing which provides upside to investors) to reduce risks. This would help in creating needed critical mass, or larger funds, in the venture capital industry in Europe. Also, corporate venture capital could be further encouraged.
- Angel investors: encourage public co-investment with angel investors/groups, provide tax incentives for angel investors and potentially create a pan-European angel fund to encourage cross-border angel investment.
- Crowdfunding: leverage this new tool as a mechanism to help drive equity investments by working to harmonize regulations across Europe to enable cross-border investments.

6) Address regulatory barriers for institutional investors

Institutional investors such as pension funds, banks and insurance companies are key funders of venture capital. Lightening pension fund legislation can help to open up further investment in private equity/venture capital as was done in the U.S. a few decades ago which led to the growth of the industry. For banks and insurance companies, policy makers should make sure that Basel III and Insolvency II do not discourage investment in private equity and venture capital.

7) Develop the financial exit markets in Europe

Encourage private sector led initiatives to develop the IPO, M&A, secondary markets in Europe. In addition, changes to the prospectus directive should be made to speed up and ease the requirements for SMEs and high growth firms to raise capital throughout the EU.

8) Encourage high-growth entrepreneurship in Europe

Much effort has been made in the United States and Europe in recent years to encourage the creation of start-ups. Incubators, accelerators, seed funds and early-stage market players on both sides of the Atlantic have helped to catalyze a stronger entrepreneurial culture. With Europe's priority being jobs and growth, entrepreneurship is high on the agenda. Young, innovative firms are significant job creators, but ventures need to scale in order to be sustainable engines of growth. Today, many successful European entrepreneurs move to the U.S. to fund and grow their business.

Policies should be put in place to help lower the risk and increase the rewards for entrepreneurs in Europe. This can be achieved with educational programs to help build talent and skills, provide connections and networks, and facilitate investor readiness and financial literacy. It can also be achieved by providing tax and regulatory relief for start-ups and creating an attractive environment with connectivity and proximity to customers.

9) Facilitate entrepreneurial ecosystems in Europe

A growing variety of entrepreneurial ecosystems (hubs/clusters) are developing across Europe. These are emerging through a mix of bottom up (market driven) and top down (policy) initiatives. Europe does not need to, nor should it, replicate the Silicon Valley. However, greater collaboration is needed within these ecosystems between entrepreneurs, corporations, universities and the public sector. Large firms, in particular, play an important role in the ecosystem and more efforts are needed to effectively link them with entrepreneurs and young innovative firms. The development of other key actors and enablers in the innovation system including financial and legal advisors, incubators, accelerators, clusters, etc. should also be encouraged.

10) Increase awareness and interest in entrepreneurship across Europe

Exposure to entrepreneurship in the educational system, from an early age through university, can help encourage young people with entrepreneurial skills and interests to pursue these opportunities. Educational institutions provide a safe place for young people to experiment, learn to fail and start over. Young people are more entrepreneurial by nature and much more open to risk. They should be encouraged to pursue opportunities and also should have a voice in policy discussions. Activities to engage other underserved groups including women, minorities, etc. are also important to unleash greater entrepreneurial potential in Europe.

Entrepreneurship should be celebrated in Europe to help create a more entrepreneurial culture. A growing number of initiatives to promote entrepreneurship are being implemented across Europe. The EU and national governments can help to support those efforts. In particular, efforts should be made to engage local entrepreneurs to provide realistic role models for young people and also to mentor young entrepreneurs.