Investment readiness

Summary report of the workshop

Brussels, 28 November 2006
This summary is based on the work of experts attending a workshop in Brussels on 28 November 2006 on investment readiness. The workshop was designed to assess how the European Commission could support SMEs’ investment readiness in Europe. It identified key problems and possible solutions. A list of participants is provided in the appendices to this report¹. The workshop was organised by Directorate-General for Enterprise and Industry of the European Commission.

¹ The document does not contain the complete and verbatim text of all presentations and interventions during the workshop. Likewise, the contents do not necessarily reflect the opinion or position of the European Commission. Neither the Commission nor any person acting on behalf of the Commission is responsible for the use, which might be made of the information contained herein.
BACKGROUND

When looking at the financing of innovative SMEs, the supply of funds has been the main concern focus. Considerable work has been carried out to improve the supply of funds for investment in SMEs. Investors who seek to obtain a profit on their investment and unless they are convinced that an SME can grow and become profitable, they will not make a commitment. To ensure an effective market in the supply of finance for SMEs, it is therefore necessary to develop the demand side to help SMEs attract investors. In other words, SMEs should become “investment ready”.

Investment readiness may be defined as the capacity of an SME or entrepreneur – who is looking for external finance, in particular equity finance – to understand the specific needs of an investor and to be able to respond to these needs by providing an appropriate structure and relevant information, by being credible and by creating confidence.

Investment readiness programmes can help SMEs develop in a number of areas – for example, by helping in developing a business plan, explaining the sources of financing, understanding investors’ requirements, ensuring that the right management skills are available, and improving the quality of presentations to convince the investors.

There is a need to develop the awareness of the importance investment readiness among SMEs and policymakers. The workshop discussed the needs of SMEs and investors, the nature of investment readiness programmes and who should provide them and fund them. It discussed how they should be publicised and assessed. It also discussed what role public authorities, both the Member States and the European Commission, could play in promoting investment readiness. The particular needs of the new Member States were highlighted. Experts also provided a series of good practices to share (see Annex).

KEY OUTCOMES OF THE WORKSHOP

The rationale for investment readiness schemes lies in the importance of considering both the demand for capital as well as the supply side. Improving the demand for capital means helping SMEs understand and respond to investors’ concerns.

The rationale underlying investment readiness is the need to consider the demand side for capital by SMEs as well as the supply side. There has been much work by the European Commission, Member State governments, local bodies and others in trying to stimulate the development of a better supply of capital to SMEs. But stimulation of the supply side must also be matched by stimulation of the demand side for the market to be effective.

Improved investment readiness can stimulate the demand side by making SMEs more attractive for investors. The principal objective is to help place SMEs in a position where they can provide potential investors with a credible investment
opportunity, to the benefit of both the SME and the potential investor. A successful outcome would be an increase in the number of SMEs attracting investments.

It is important to raise awareness among policymakers to develop suitable policy frameworks to promote investment readiness among SMEs.

The workshop considered that it is important to raise awareness amongst policymakers on investment readiness promotion. Policymakers are taking decisions on how to help support SMEs, but may have no relevant experience and in particular no experience of investment readiness issues. Policymakers need to be aware both of the range of measures that are available, and the policy changes that can help stimulate a climate of entrepreneurship. Guidance on best practice and even an “Academy for Policymakers” could be considered to address the gap between policy advisers who have no business experience and the investors.

There is also a need to raise the awareness of SMEs on investment readiness, and the possible effect on their own businesses.

SMEs need to be aware of the potential benefits of investment readiness and ways to achieve it. The objective is to reach SMEs who could benefit from investment readiness programmes, and for the SMEs to realise the potential benefits of participation, in particular the increased possibility of raising finance. Demand for investment readiness programmes is usually high. However, high demand does not necessarily mean that all the companies who should utilise investment readiness programmes are aware of the services offered or the most appropriate schemes. In Ireland, for example, 400 companies had enquired about a scheme but only 75 could be accepted. Similar situations were reported in other Member States.

There are several ways of raising awareness or informing companies about the availability of investment readiness advice. Economic development agencies in the public sector provide investment readiness advice with the objective of growing the economy. Business angels and venture capitalists have an objective of obtaining good investments on which a return could be made. These and other sources of investment readiness support have differing aims and delivery models reflecting amongst other things their target markets.

Many public authorities and other investors run investment readiness programmes and a large number of organisations provide help in setting up businesses. Examples include banks and finance firms, who seek future clients. In the UK there are estimated to be many thousands of agencies providing some form of investment readiness advice. The quality of advice is excellent in many but not in all cases. SMEs need to be able to judge where the best advice can be found. There may be a role for some form of quality indicators – probably administered at national or regional level. It would be helpful to know more about any existing quality schemes and to consider best practice in this area.
Investment readiness programmes must meet the needs of individual SMEs – but what are the needs and what should programmes therefore contain?

A number of models of investment readiness programmes were presented at the workshop. Some are publicly backed programmes such as those in Ireland and Spain and others are private programmes such as in France and Austria. In the UK, both publicly backed and private programmes are available. Further information was received following the workshop, both from the presenters and from other programmes. A summary of the main presentations is contained in Appendix A.

All programmes have the ultimate objective of helping SMEs to raise finance. It is likely that this objective will be met through a process consisting of several stages. A first stage might be an initial assessment of the business and its plan. Other aspects will be an assessment of the most appropriate form of financing – whether to use loan finance, equity finance and the characteristics of each type of finance. There may then be a need to address potential barriers to attracting investment (for example, key skills or the ownership of IP assets). Finally, there may be some specific work on introducing investors and helping the company present its case.

A most important question is the quality of management and whether the right skills are available for the next stage of business development. Ensuring the right quality of management, through training or the introduction of new skills and new people, is a critical part of investment readiness. To propose the introduction of new people, or new skills, is not a task that can be undertaken without a good understanding of a business so it can be time consuming to provide help in this area.

The ownership of IP assets is another important issue. This is particularly so where a company has significant IP assets. There is a need to ensure that the assets are owned by the company into which investments are made. A company – and not an individual founder – should have control of IP assets if it is to attract finance. Legal and financial advice may be necessary to select the right corporate structure that gives security to potential investors and is tax efficient.

Finally, investment readiness schemes should provide specific advice on raising finance, including introductions. Where business angels are involved, a company will have to convince a ‘gatekeeper’ to allow it to make a presentation to a group of angels. It will have a limited time to make a good impression on the angels. In other cases, the investment readiness programme may make introductions to investors. Good quality presentations and convincing business plans are important and an investment readiness programme will help develop these.

Investment readiness programmes can be targeted at high growth SMEs, or could be aimed more widely to benefit more SMEs. Programmes targeted at a small number of companies can be more intensive, but the economy needs the contribution of the mass of SMEs.

Many investment readiness programmes concentrate on high growth SMEs. These companies are seen as giving the highest returns to the economy. The issue is how they are identified in the assessment process. But the needs of other SMEs, which will grow but perhaps not so quickly, should not be overlooked. An important issue discussed was whether investment
readiness programmes should just concentrate on high growth SMEs, or whether the programmes should include a much wider group of SMEs that would grow at a more moderate rate. It had to be recognised that much of the growth in the economy would come up from the larger number of SMEs that may not by themselves be a high growth SMEs. It is estimated that 91% of European enterprises are micro businesses with less than 10 employees. And only 1% of enterprises have more than 250 employees.

**There is a need for an assessment process to identify suitable firms among those applying for investment readiness support.** There is a need for a ‘gatekeeper’ or funnel to ensure that companies get the most appropriate advice. Many companies will first be given some general advice, which will enable a selection programme to take place for further modules. Some companies may just need written material, whilst others will benefit from one to one mentoring.

**Who is best placed to deliver investment readiness programmes, and should they be delivered locally?**

**Advice has to be provided locally at the first stage to be effective.** More technical advice can be given from other sources but the most effective initial contact is at local level. The involvement of people who have previously built up a business is seen as adding value to the programme. Clearly, the supply of good advisers is likely to be limited.

**The best general advisers are often people with entrepreneurial experience.** In Ireland, for example, retired or semi-retired entrepreneurs are paid a nominal retainer of €1,000 per year. In other cases advisers are drawn from the investor community. An interesting example in France is mentoring by senior graduates from a business school (Ecole Centrale Paris) of more recent graduates.

**What is the best framework to develop future investment readiness programmes - at a local or national level?**

The workshop discussed how new investment readiness programmes could be developed. There is a large number of such programmes and information on best practice would be helpful.

**Delivery of investment readiness programmes is likely to be local, so local involvement is essential.** But the framework for developing programmes, and the preparation of common materials or modules, can benefit from good practices elsewhere. The other key issues on development are an assessment of demand, the identification of the most appropriate SMEs and the selection of people to deliver the programmes.

**Some investment readiness programmes are run without public support. Examples include schemes led by investors but many are best run in the context of SME support provided by local or national authorities.**
What approach should be adopted to the pricing of investment readiness support – for example, should investment readiness programmes be free or should fees be charged if (e.g. only if linked to investment)?

Funding for investment readiness programmes can come from investors, SMEs and/or from public bodies. Investors have an interest in identifying the right sort of opportunity and the workshop heard of examples where advice had been given to SMEs free by business angel groups. In practice, it is likely that a significant screening process will take place to identify a few suitable SMEs who could benefit from such free help, and that the process will be closely linked to the likelihood of there being a good investment opportunity.

Another model is where SMEs pay directly for some advice, in particular advice on specific issues relating to their business. The advantage is that SMEs are likely to value advice they pay for, and can choose the areas in which they consider they need advice. The disadvantage is that SMEs may not be fully aware of all the issues they need to cover, or of the value of the advice provided.

Public bodies are likely to subsidise investment readiness schemes at a more general level, through overall SME support programmes. As with the provision of advice by investors, there is likely to be a screening programme to identify the most suitable companies.

Overall there appears to be a role for each source of funding and in practice some programmes will be funded from more than one single source.

How can investment readiness programmes be evaluated and what measures could be applied to help SMEs ensure that the programme will be effective for their needs?

In some countries, SMEs may be faced with a variety of programmes, not all of which will be suitable for their needs. In part of the UK, for example, there is an attempt to try to reduce the number of advisory programmes supported by public funds from the thousands to the hundreds. The objective is to concentrate support on the most effective programmes. There is therefore a need to have a means of identifying good programmes. More work needs to be done on the criteria to be used and how programmes could be monitored.

It would be helpful to have more comparative information on the way that investment readiness is delivered and on best practices. There is a project under way by London Business Angels, mentioned in Appendix A, which will address some of these issues. Depending on the outcome of this project there may be scope for further work to be carried out to share best practice or carry out demonstration projects.

In the new Member States, where there is less of a record of helping entrepreneurs, additional measures such as exchange schemes could be developed to help investment readiness programmes.
Many investment readiness programmes rely on identifying the right mentors or teachers, who may be recently retired entrepreneurs. In the new Member States there may be difficulty in identifying such people because most entrepreneurs are highly active in their own businesses. One possibility would be to have exchange schemes between the older Member States and the new Member States. An exchange scheme would not only allow for the movement of experienced people, but would also enable good practice to be exchanged between established schemes and newer schemes.

The importance of the development of a culture of entrepreneurship should not be overlooked in promoting investment readiness.

An interesting issue discussed at the workshop is that of cultural change and entrepreneurial teaching at school and university level. An example was provided by the UK programme of funding for business awareness at schools. Many UK schools operate a young entrepreneur scheme under which students form themselves into small businesses to carry out some entrepreneurial activity. The objective of these schemes is to teach students the basics of business. A further driver of cultural change is the use of media, in particular TV. There is an increasing number of programmes in which potential entrepreneurs present ideas to be possible investors with the objective of seeking finance.

**Role of the EU and the National Authorities**

Participants in the workshop developed a series of recommendations for the EU and national authorities which are summarised below. There are separate sets of recommendations for the Commission and for national authorities.

**There is a need to promote the sharing of best practice in the development of investment readiness programmes.** The workshop heard from investment readiness programmes across Europe with different approaches to helping SMEs. Some studies are under way to compare practice so that investment readiness programmes can learn from what has been developed in other countries and regions. But there may be a wider role for the Commission to support studies of investment readiness programmes to encourage the sharing of good practice. Clearly, a starting point would be the work that is already being carried out. Examples of areas where practice could be compared include many of the issues referred to earlier – who should provide help, whether help should be charged for, what modules of practice could be shared and what quality measurement schemes are available, as well as alternative delivery mechanisms such as comparing self assessment tool kits now used by some programmes. A particular issue could be the targeting of such programmes, at high-growth companies or at a wider body of growing SMEs.

**There is a need to raise the issue of investment readiness on the agenda of policymakers, at a national and at local level.** It is not only SMEs and those providing support to them that need to be aware of the issues involved in investment readiness. There is a particular need to ensure that policymakers think of stimulating the demand for capital by SMEs, as well as the demand side. There are important policy issues which need to be decided – often at local level. These issues include the need for a programme, its scale, the method of delivery, whether there should be charges for advice and the types of SME to be targeted (for example fast growing SMEs, or a wider group of SMEs). A further consideration is the relationship of any
investment readiness to the local finance community including business angels and other capital providers. If public funds are involved, policymakers need to decide what quality standards to use to select schemes for support. Following up the proposed best practice study referred to above, the Commission could prepare a guide aimed at policymakers with examples of the development of investment readiness programmes and their effect. The guide could be used in specific training – one possibility is an “academy” for policymakers which could cover various aspects of risk capital finance for SMEs.

**Support should be provided for training - including pilot programmes - on setting up investment readiness programmes.** A follow on to the sharing of good practice could be assistance in training those providing investment readiness programmes. It is possible that training could be funded on a pilot basis with the objective of bringing together programme managers and mentors from different member states.

**Broad array of incentives could be provided including taxation incentives to organisations helping raise investment readiness** (in practice, this is likely to be aimed at any tax incentives for business angels and similar providers). This is likely to be a task that is carried out by Member States but the Commission may have a role in providing comparable data on the tax incentives currently available. The European Private Equity & Venture Capital Association (EVCA) has already examined this issue and any further work should take account of their proposals and information. Some research on the comparable effect of different tax incentives in different member states might stimulate debate amongst policymakers on the most appropriate approach.

**The special needs of the new Member States should be taken into account by providing mobility grants.** The new EU Member States have particular problems in setting up investment readiness programmes. The workshop heard that in Member States with a longer history of such programmes, it is often recently retired entrepreneurs who make good mentors. But in new Member States there is a limited supply of such people. One possibility would be to organise links between organisations providing investment readiness in older and newer Member States so that experience can be shared. Funding mobility grants could also be considered to enable people working in investment readiness organisations in an old member state to work for a period of time helping develop similar organisations elsewhere.

**Better information could be provided to SMEs about investment readiness programmes and their value** – Whilst most information on investment readiness programmes is provided to SMEs at a local or national level, there may be a role for European organisations which have contact with SMEs – including IRCs and Euro Info Centres - to disseminate information on how to access investment readiness programmes and the value of such programmes. A series of success stories – with examples of how investment readiness programmes have helped SMEs - could be prepared to help promote awareness through such organisations.
APPENDIX A – EXAMPLES DISCUSSED DURING THE WORKSHOP

Irish Development Agency – Ireland

In Ireland an investment readiness scheme is run by the Irish Development Agency. SMEs are assigned a dedicated ‘Development Adviser’ who works with the company until their strategic objectives are reached. Other in-house specialists are drafted in to assist with issues such as business planning, team building, and recruitment and employment law. Training programmes are planned for 2007 and it is envisaged that the companies will pay a fee.

Coaching has been in place for over 5 years and involves a panel of 4 experienced mentors screening the venture and providing feedback to businesses. Mentors are involved in the assessment of business plans. Usually they are retired professionals that are paid a nominal €1,000 per annum. Enterprise Ireland (who run this scheme) are subsidised to Euro 300-500 per company/promoter. From some 400 enquiries per year there are 75 companies who go on the programme.

Key aspects of the scheme include the involvement of mentors on a 1-1 basis which provide high quality business advice to the entrepreneurs. The involvement of retired professionals is seen as important and it is preferable to have people who have been personally involved in running a business. Inevitably, and the constraint is the availability of good mentors to match the likely good prospects and to a careful sifting of prospects is needed.

UK - Greater London Enterprise

GLE (London Business Angels) do not charge for their services but are selective on those organisations to help. A ‘gatekeeper’ assesses possible projects. They see a clear need for good integration and interface with the finance community. They have in-house training models including “Ready for Growth” and the “Creative Business Accelerator”. Continual refinement of the model has led to a sectoral focus, with a particular emphasis on the creative sector which is important to London’s economy. An e-learning model has been developed. The financial & legal advisers are all investors.

They are underwriting a project “EASY” dealing with early stage investment across Europe in conjunction with 17 partners including: (Banks, VCs and Government) including Poland, Czech Republic and Romania. The project is looking at harmonisation issues such as: cross-border investments, taxation and legal issues. GLE will host a workshop in February 2007 on investment readiness to explore different models. A series of further workshops will ensue across the EU over a two year period.

GLE claim that 70% of their clients have raised finance, 60% have created new products, Promoters time is saved and investors have confidence in the quality of the proposals.

Germany, BANDacademy (Business Angels Netzwerk Deutschland)

In Germany, BANDacademy (Business Angels Netzwerk Deutschland) the investment readiness philosophy (still in development) is built around 3 key areas, creating, coaching and financing. The envisaged process will involve idea generation, writing a business plan, support/coaching the entrepreneur in starting up and financing, informal study, stakeholder brainstorming, tools for business angels.

Investment Readiness is embodied in the process and cannot be disaggregated. Plans are underway to train the stakeholder groups – angels, investors and entrepreneurs. The intention is also to integrate other programmes, other groups on a regional and
wider geographical base. Plans exist to work with the companies/promoters through 2nd round financing and beyond.

They have elicited feedback from companies that do not receive funding but they have not tracked the numbers that have undergone training. The BANDacademy do not believe in being overly protective of their companies/promoters.

**Hungary and the Czech Republic**

Hungary is in need of an angel network to kindle the entrepreneurial flames and business interventions need to be introduced. In the Czech Republic there are cultural issues that render the promoters reluctant to be seen to be in need of finance. Reluctance also to be seen as an investor for fear of being perceived as wealthy.

**UK - England**

In England there are multiple agencies and products providing investment readiness services. Government policy is to consolidate the offering and reduce the number of agencies to hundreds by 2010, from the present thousands. The offering has to be provided locally, with generic services tailored to the needs of individual sectors. The focus on the present is quick wins and Investment readiness is integral to the overall product/service offerings. The government small business service ‘SBS’ has an online ‘health-check’ to increase self-awareness of possible deficiencies in their presentation. At a policy level it should be recognised that investors’ objectives are a return on their investment.

**Spain - Catalonia**

In Catalonia, the investment readiness programme is emerging as a key component of the angel network, supported by the Catalonia Development Agency although the business angel network is at an early stage with seven networks. Catalonia has been successful in attracting inward investment and is now looking to mechanisms to develop locally grown businesses.

**France – Ecole Centrale de Paris**

**Partnership between stakeholders** may be another interesting approach to investment readiness. In France, there is an association of the Ecole Centrale Paris which provides business mentoring (and some business angel activity) between former members of the school. The association provides an opportunity for networking between graduates with the same technical background.

Many of the issues covered by the approach are similar to other approaches, but delivered in a different manner. For example, training is available (some is paid for), and will include business analysis, a review of funding opportunities and investor expectations. There is a helpful self assessment tool.
APPENDIX B – LIST OF WORKSHOP PARTICIPANTS

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