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International Conference on Ways and Means
of Attracting External Finance for New Innovative Enterprises

Astana, Republic of Kazakhstan, 21-22 May 2009

**REPORT ON THE INTERNATIONAL CONFERENCE ON
WAYS AND MEANS OF ATTRACTING EXTERNAL FINANCE FOR
NEW INNOVATIVE ENTERPRISES**

I. ATTENDANCE

1. The International Conference brought together about 100 representatives of governments, private companies, business associations from 13 member States of the United Nations Economic Commission for Europe (UNECE) as well as representatives of the Secretariat of the Commonwealth of Independent States, Eurasian Economic Community, Eurasian Patent Office and the World Intellectual Property Organization.

II. OPENING OF THE INTERNATIONAL CONFERENCE

2. The International Conference was welcomed by the Minister of Economic Affairs and Budget Planning of the Republic of Kazakhstan and the Deputy Secretary General, Eurasian Economic Community. They emphasized the need for a growing innovative enterprise sector as a means of alleviating the consequences of the current economic crisis and enhancing the competitiveness of countries with economies in transition. They encouraged the participants to actively exchange country experiences and good practices to facilitate the establishment of an enabling environment for innovative enterprises.

III. SUMMARY OF DISCUSSION

3. The International Conference discussed various sources of financing innovation enterprises and role of specialized financial providers, including public grant programmes, business angels and venture capital firms. In addition to factors that influence the availability of finance, it also examined the criteria used by financial intermediaries to assess the attractiveness of potential investments as well as linkages between operations of financiers and the general business environment conducive to the emergence and operation of new innovation-based companies. The issues of protecting and commercializing a company's intangible assets through acquiring intellectual property rights (IPR) were at the centre of the debate. The Conference discussed the topics of strategic management of intellectual property, including its use as part of a business model to raise external finance. It also explored ways and means of strengthening the innovative potential of companies at various stages of their life cycle. Finally, the meeting considered a variety of instruments and strategies that could be adopted to promote the financing of innovation, including, among others, grants, business incubators, networking services and hybrid public-private venture capital funds. The concluding session of the Conference focused on the corrective actions required from governments to improve the financing opportunities of innovative enterprises.

4. The discussion at the first session focused on the identification of financing options available to innovative enterprises at early stages of their development and the role of various types of intermediaries.

5. The participants noted that the major challenges faced by innovative entrepreneurs when trying to raise finance included unclear prospects for the commercialization of developed technologies, inadequate business plans and vague profitability perspectives, as well as the lack of qualified and motivated managers. In many countries of the region, both scientists and managers dramatically lack training and experience in implementing the innovation projects.

6. Of 280 project proposals, which Kazakhstan technoparks received during 2004-2008, only four were found investment-ready and financed externally. The participants noted that in countries of the region technoparks often lack the financial basis and pilot manufacturing facilities to ensure the commercialization of new technologies. The effective operation of technoparks in developed market economies attests to the important role of public-private cooperation in early-stage financing of innovative undertakings. In Japan, for example, as much as 60 per cent of financing for technoparks and similar undertakings comes from central and local government. In the context of transition countries, public co-financing is of particular importance at the pilot and trial stages of innovative production.

7. The participants noted that in the absence of alternative sources of finance, the amounts of state-sponsored financing available to scientific institutions and start-ups were often insufficient to encourage the commercialization. In addition, government priorities in this area often were not clearly defined.

8. Despite a certain progress, in many countries of the region, the existing laws and regulations do not define unambiguously the property rights of the authors of innovations. Combined with high risks and uncertain marketing prospects for innovation-based products this

hinders the innovative activities of both research institutions and enterprises. It was argued that innovative companies also suffered from burdensome tax administration, excessive reporting requirements, as well as protracted procedures in the course of enterprises registration, patenting, certification of products and customs administration of imports.

9. Recently, some of the larger transition economies of the region have witnessed a growth in the numbers of early-stage investors, including business angels and venture capitalists. During the 2000s, the cumulative capitalization of private equity and venture funds in the Russian Federation almost doubled reaching more than \$ 4 billion. At the same time, the role of business angels, instrumental at the earliest stages of innovative entrepreneurship remains modest. For example, in the Russian Federation, there are about 200 operational business angels as compared to 225 thousand in the United States. The former invest about \$ 20 million a year as compared with \$ 23 billion worth of similar investment in the United States. According to estimates, the Russian Federation could have as many as 10 thousand business angels investing about \$ 1 billion a year.

10. In Western Europe, the total number of deals involving business angels has grown. However, under the influence of the financial crisis, the size of individual investments has tended to decrease, and angels are increasingly seeking investment opportunities abroad. The Conference noted that at early stages of development, in addition to financing the business angel networks could render advisory services to innovative companies, for example, providing investment/investee readiness support and facilitating the syndication.

11. In transition countries, the activity of business angels and venture funds is hindered by attractive alternatives for investment characterized by low risks, high profitability and short payback, e.g. trade, real estate, etc. Insufficient legal security of minority stock holders, high cost and risks of entry, operation and exit from the innovative business, the lack of tradition for business angel operation, as well as the lack of understanding of their function and potential within government bodies also impede the development of early-stage financing institutions.

12. The participants noted that in the conditions of the current crisis the profitable exit from innovative business became increasingly difficult for both business angels and venture capitalists. The successful initial public offering has ceased to be a realistic option for investment exit and the only viable strategy has become an acquisition or merger.

13. During the second session, international and national intellectual property experts discussed the ways and means of translating the results of research and development into intangible assets and using these assets to generate revenues and financing for innovative firms.

14. Participants stressed the important role of IPR in creating exclusive market niches for innovative enterprises and differentiating them from competitors. Strong IPR and a sound IPR management strategy were therefore seen as key factors for innovative companies to attract outside financing. A sound IPR management strategy should include the strategic licensing out of selected IPR to carefully chosen partners. Licensing out enables an innovative company to save human and financial resources needed to continue research and development (R&D), and to profit from markets it would not be able to penetrate on its own. Similarly, participants stressed the importance of IPR management in the transfer of new technologies from universities and

academic research institutes to industry, be it through spin-off or start-up companies, or through licensing deals.

15. The Conference paid particular attention to the issue of a realistic valuation. Putting a value on IPR is necessary when a new company is trying to raise money from external investors, when two companies are negotiating a licensing agreement, and when a research organization is trying to commercialize research results. Arriving at a realistic valuation is hindered by the uncertainty, risks and important investment involved in turning an unproven new technology into a successful product; and disagreements on this issue can derail commercialization efforts. It was argued in this context that the valuation market needs rules and methods of valuation mutually acceptable for buyers and sellers of technology. The efforts of stakeholders including patent offices and valuation and auditing companies should focus in the future on creating a framework for the valuation market which would help innovative enterprises commercialize their R&D outputs.

16. Other challenges for IPR management in both small and medium-sized enterprises (SME) and public research organizations include a lack of awareness about the importance of IPR, the often high cost and complexity of obtaining IPR, and a lack of human and financial resources for enforcing IPR once obtained. As a case in point, a recent survey of the Ukrainian research community found that a lack of experience and knowledge was the most significant barrier to the commercialization of R&D results in that country. The major factor behind this was found to be a lack of awareness of key government officials, leaders of scientific organizations and industrial enterprises about the important role of IPR in economic development.

17. The third session provided an opportunity for representatives of public financial institutions, government agencies and private investors to present their views on public initiatives that may have a positive impact on the financing of innovative enterprises.

18. The participants emphasized the need to raise the awareness of enterprises and government officials of the crucial role of intellectual property and its commercialization in enterprise development. This brings to the forefront the need for training of both managers and government bodies in charge of enterprise development. Governments and university centres should hire successful entrepreneurs who could exercise the mentoring function and train the operational and would-be entrepreneurs in designing the realistic business plans, choosing appropriate legal form, assessing market prospects and preparing financial projections for their companies. The international organizations could provide a platform for such capacity-building exercise.

19. The Conference thought that the government investment programmes should make more emphasis and allocate more resources to the “seed stage” of financing. When implementing such programmes, government bodies should cooperate and coordinate their activities with the private sector, including large companies. The government regulation should also facilitate the spill over of investment resources to the early-stage financing sector through favourable taxation rules, financing of business angel networks and public-private co-financing of innovative companies.

20. At the same time, governments should set priorities to foster the development of innovative activities concentrating scarce resources and providing guidance to the private sector and academia. In particular, enterprise development agencies should advise research institutions and enterprises on alternative forms of commercialization of R&D results and co-finance patenting

of the latter. Stakeholders should have opportunity to share information on good practices of selecting investment projects to be financed by public institutions. Here, again international organizations could provide a forum for such a dialogue.

21. To strengthen the capacity of innovative enterprises to harness IPR for financing, governments may want to consider integrating IPR promotion into wider SME support policies and to strengthen the coordination and cooperation between IP offices and enterprise support agencies. Additional services to enterprises could include IP audits, clearing-house services matching inventors and investors, as well as development of model licensing agreements. Campaigns aimed at raising the awareness of entrepreneurs and research managers of the importance of IPR protection and management were also considered vital. Policy options to reduce the costs of IPR protection could include tax breaks and public subsidies to lower the cost of patenting.

22. The outcome of the International Conference will be reported to the UNECE Committee on Economic Cooperation and Integration at its fourth session in September 2009.

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