Government’s Venture Capital Policy in Finland

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Brief pre-history of VC-policy in Finland

• 1986
  • Fact-finding mission to Silicon Valley,
  • Sitra (Finnish Foundation of Technology and Innovations) starts direct VC-investments.

• 1988
  • EVCA Business Seminar organised in Finland,
  • Capital Management Ltd, the first private VC-fund was established (KOP - the biggest commercial bank in Finland).

• 1990
  • Finnish Venturing Association was established,
  • Start Fund of Kera was established (Regional Development Fund in Finland).

• 1993
  • Government’s Committee recommended guidelines for VC-policy (broadening of investment rules of Pension Funds, Subsidizing management fees of VC-funds, etc.).
The growth of venture capital and private equity in Finland

Early stage investments down from 50 % to 20 % in 2001-2004

Source: Finnish Venture Capital Association
Innovation environment in Finland, resources and funding

The figures represent the total extent of each organisation in million euros in 2004. In parenthesis the share that is funded from the State budget. The funds of Tekes, the Academy of Finland and Innofin are funded entirely from the State budget.
European Innovation Scoreboeard 2007
Finland is investing heavily in innovation…

![Graph showing R&D/GNP % for Finland, USA, and EU from 1992 to 2004. The graph indicates an increase in R&D/GNP % for Finland over time, while USA and EU show relatively stable trends.](image)
Private equity investment as % of GDP in 2006 by country of destination

- Sweden: 1.437%
- United Kingdom: 1.256%
- The Netherlands: 1.048%
- France: 0.607%
- Hungary: 0.596%
- Europe: 0.569%
- Czech Republic: 0.453%
- Belgium: 0.441%
- Ireland: 0.394%
- Spain: 0.367%
- Denmark: 0.339%
- Italy: 0.333%
- Germany: 0.313%
- Switzerland: 0.282%
- Norway: 0.258%
- Finland: 0.233%
- Poland: 0.205%
- Portugal: 0.115%
- Romania: 0.112%
- Austria: 0.103%
- Greece: 0.033%
Average size of P/E investments – Year 2004 Europe (MEUR)
Classic VC and informal VC investments as % of GDP in 2001
Entrepreneurial activity

Willingness for self-employment

- Portugal
- USA
- Ireland
- Spain
- Italy
- Greece
- EU15
- France
- Great Britain
- Germany
- Denmark
- Austria
- Sweden
- Belgium
- Netherlands
- Finland

The survey is based on approx. 21,000 telephone interviews.

Source: Flash Eurobarometer 160, 2004

DM 36054
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The Nordic countries are high in R&D, but not so high in the financing of growth.

Sources: OECD, EVCA, 3i/PwC, Worldbank, Tekes
BENCHMARKING EUROPEAN TAX & LEGAL ENVIRONMENTS FOR VENTURE CAPITAL

Tax and legal environment in the European Union Member States

<table>
<thead>
<tr>
<th>Rank</th>
<th>Country</th>
<th>Total score</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>United Kingdom</td>
<td>1.26</td>
</tr>
<tr>
<td>2</td>
<td>Luxembourg</td>
<td>1.49</td>
</tr>
<tr>
<td>3</td>
<td>Ireland</td>
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<td>8</td>
<td>Hungary</td>
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<td>10</td>
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<td>11</td>
<td>Switzerland</td>
<td>1.95</td>
</tr>
<tr>
<td>12</td>
<td>Spain</td>
<td>1.96</td>
</tr>
</tbody>
</table>

The Total average is 1.97

13 Norway    2.04
14 Sweden    2.05
15 Czech Republic  2.12
16 Poland    2.13
17 Finland   2.30
18 Germany   2.37
19 Austria   2.42
20 Denmark   2.46
21 Slovak Republic  2.49

Scale: 1=more favorable, 3=less favorable

There is still a lot to do in improving the conditions for growth-oriented entrepreneurship and venture capital in Nordic countries.

Several widely shared problems in the Nordic countries, e.g.

- Permanent establishment for foreign investors in venture capital funds
- Limitations of pension funds and insurance companies to invest in venture capital funds
- High tax rates
- Lack of tax incentives for individuals to invest in new ventures
- Taxation of stock options

Source: EVCA 2004 Benchmarking European Tax & Legal Environments
Benchmarking European Legal and Tax Environment (EVCA)

Figure 1: Current European situation

Source: EVCA
The level of foreign commitments in private equity funds varies extremely across Europe. The chart illustrates the percentage of funds raised as a percentage of GDP from 1994-2002, with the following countries and their respective figures:

- **Austria**: 20.8%
- **Belgium**: 11.1%
- **Denmark**: 11.1%
- **Finland**: 11.1%
- **France**: 10.3%
- **Germany**: 33.9%
- **Greece**: 23.3%
- **Iceland**: 27.6%
- **Ireland**: 0.0%
- **Italy**: 32.0%
- **Netherlands**: 24.2%
- **Norway**: 3.9%
- **Portugal**: 1.4%
- **Spain**: 47.7%
- **Sweden**: 61.1%
- **Switzerland**: 27.3%
- **UK**: 60.1%

Percentages above columns refer to the share of foreign commitments in new funds.

Source: Analysis based on data from EVCA, Eurostat, and EIF.

Note: Investments of EIF and EIB have been deducted from other European figures.

Lack of professional Venture Capital for post seed

Problem Area

Lack of professional support for early growth investments from 0,5 to 3,0 MEUR

<0,5 MEUR - Strong Government support

>3,0 MEUR - Most private VC’s looking for later stage and lower risk investments
SUMMARY OF THE CHALLENGES

• =>Finland is investing strongly in innovation and education producing great technology but limited amount of commercial success.

• The success is limited by
  1) Lack of entrepreneurship and especially experienced serial entrepreneurs
  2) Very limited pool of internationally operating, professional start-up and early growth VC activity
  3) The poor local exit market (M&A and IPO)
What has the Government done?

- To improve the supply of capital:
  - Opened the VC-market for foreign fund-investors (taxation)
    - Needs still some corrections.
  - Incentivized the corporate venture investments (taxation).
  - Permitted pension funds to invest more in stocks, in non-listed companies and in VC-markets.
    - A problem still exists that pension funds do not want to invest in Venture Capital, only in buy out markets.
      - A joint Fund of Funds by the Government and pension funds to be build.
  - Increased the supply of seed-capital (a new state-owned seed fund - Start Fund of Finnvera co-invests with business angels).

- To improve the demand side (competence gap):
  - Competence building of start-ups (an investment readiness programme) by Technology and Innovation Development Center (Tekes) for Young Innovative Companies (YIC).
  - Tax incentive for business angels’ investments to be designed.
Government’s policy to turn innovations into high growth SME’s

Sources of innovations
- Universities
- Research institutes
- Technology Programmes
- Corporations

Deal flow generators for new ventures
- Technology Development Center’s grants to business sector R&D (the programme for Young Innovative Companies).

New generation of business incubators

New seed and early stage VC-funds

Regional Funds

Increased number of new growth SME’s

More investments for start-ups

Veraventure co-invests with business angels

Imorovement of Legal Framwork:
- incentives to business angels
- removing obstacles from foreign investors and institutional investments

Strategy of the government coordinates the process

FII-Finnish Industry Investment – Government’s VC-fund investor

Venture Capital Funds, foreign investments

Corporations
Why business angels are needed?

- Industry structure is based on big corporations and tiny family enterprises in Finland.
- Innovation infrastructure is excellent, but, does not generate new hi-growth companies to the global market.
- Innovative start-ups lack business experience to go global – and risk capital for their early growth.
- Institutional investors and professional Venture Capital companies are risk avoidant and do not invest in innovative start-ups.
- Proper incentives can attract experienced business people to invest their time and money to start-ups.
- Business angels can create value for start-ups and improve their investment readiness for professional VC’s.
- Business Angels are key players in increasing the number of new hi-growth firms.
How to design an incentive to Business Angels

• Incentive for value creation (tax relief on capital gains after 3 years hold time) not for investment as itself (upfront).
  • Fiscal argument: incentive brings tax incomes before tax relief.
• Eligible enterprise shall fulfil certain criterias, outside independent statement is obligatory.
• Eligible investor is a natural person or an investment company established by natural persons for this purpose.
• Size of the investment is regulated by the investor’s share of the ownership of the target company (min. 10 %, max. 49 %).
• The Government will decide exact limits for the variables above within in a few months’ time.
• The incentive is assumed to multiply the number of active business angels, to double the size of the investment as well as to contribute the intensity of business angel’s work for the value creation of the target company.
Thank you for your attention!

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