



# Boosting the innovation and competitiveness in the industrial clusters: an EIB perspective

Brussels 26 March 2013

Eramiat workshop

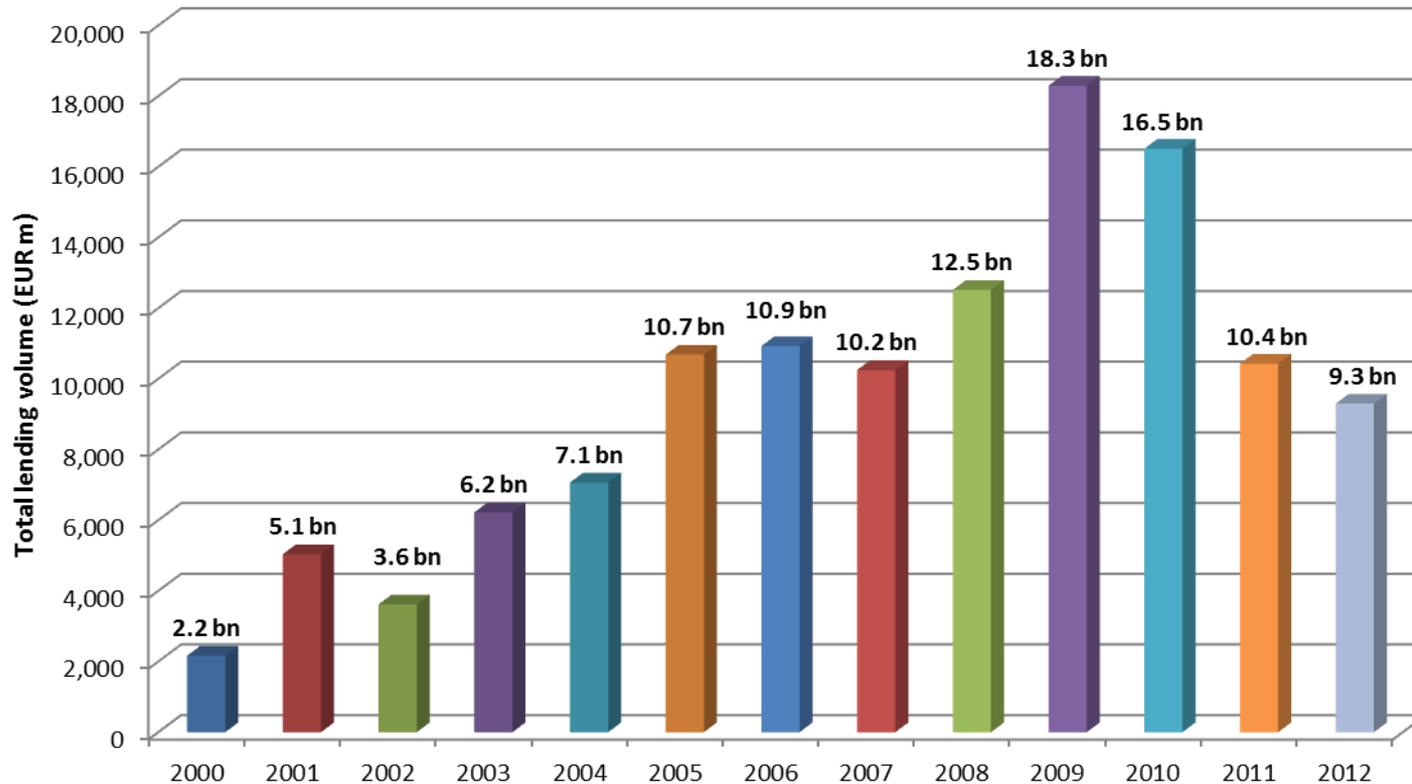


## Innovative and competitive industrial clusters

- Average corporate R&D spending as % of GDP in US & Japan is around 3%, in Europe it lags significantly at levels around 1.7%
- Innovative companies investing much in RDI (Capex + Opex) have more difficulties securing stable financing at acceptable financial terms
- Continuing market gaps and deficiencies in debt and equity markets for financing of innovative enterprises, and especially SMEs
  - 75% of SMEs dependent on external financing
  - 'access to finance' the second most pressing problem for Eurozone SMEs, right after getting customers
  - Venture capital fundraising and investment levels at one quarter of 2006 levels
- Leveraging on innovative and integrated clusters: mix of companies with different funding needs and access to banks and capital markets



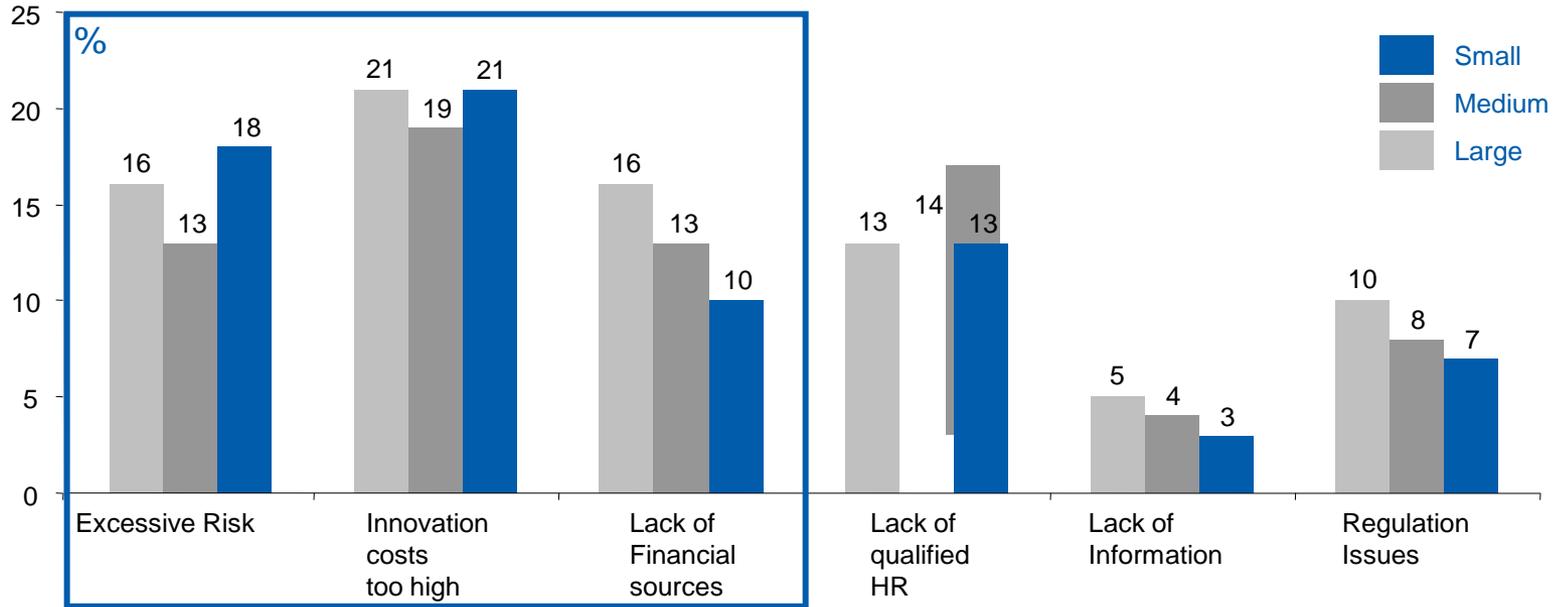
### Total Lending 2000-2012 : EUR 123 bn



- Transaction sizes have ranged from EUR 8m to EUR 600m
- Approximately 50% of the transactions were pure private sector investments



Proportion of EU enterprises that regarded selected hampering factors as highly important



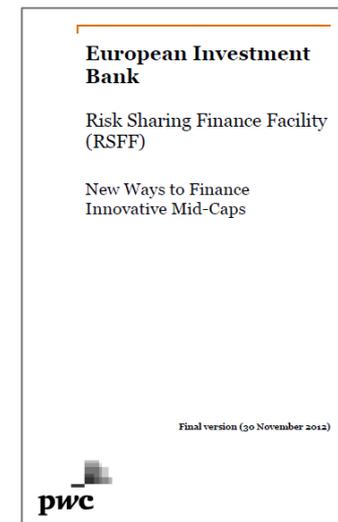
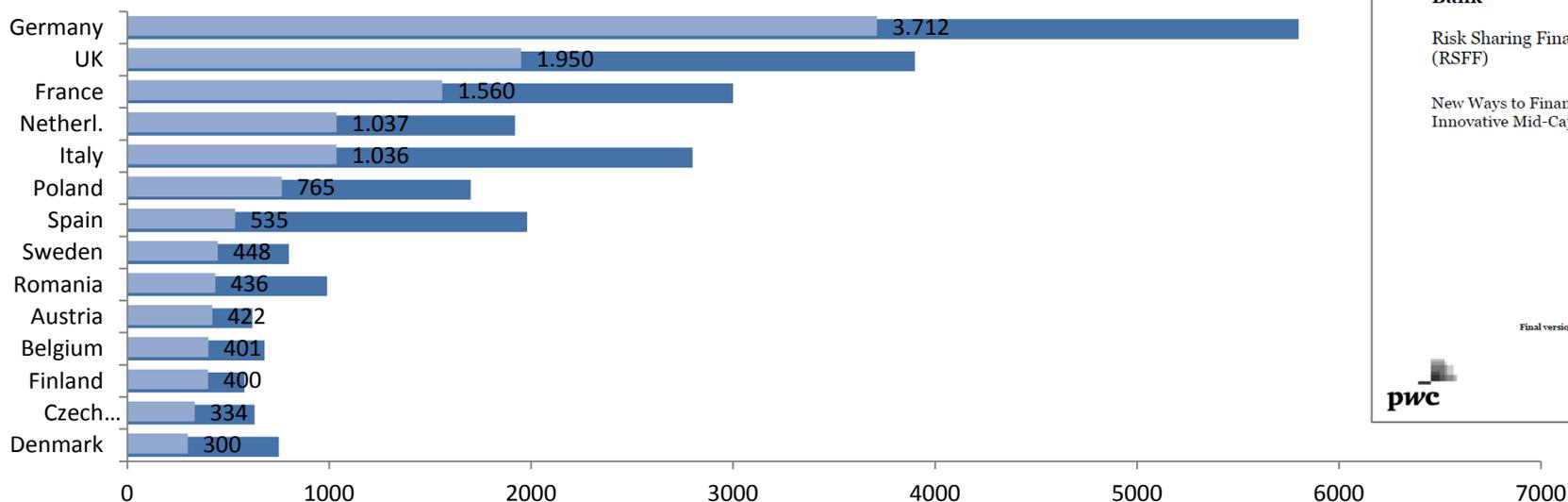
- ❖ Appropriate financial resources, excessive risk and high innovation costs are the most critical limiting factors quoted by EU corporations. The provision of EIB risk sharing financing aims to address the 3 key obstacles.
- ❖ This is mainly due to the nature of RDI: intangible assets, unproven markets, highly complex products and technologies, and high risks.
- ❖ Asymmetric Information: Commercial capital providers have difficulties to evaluate the RDI risks and hence to provide sufficient appropriate financing.

# Mid-Caps and their Role in Innovation

## What is the economic role of Innovative Mid-Caps in the EU?



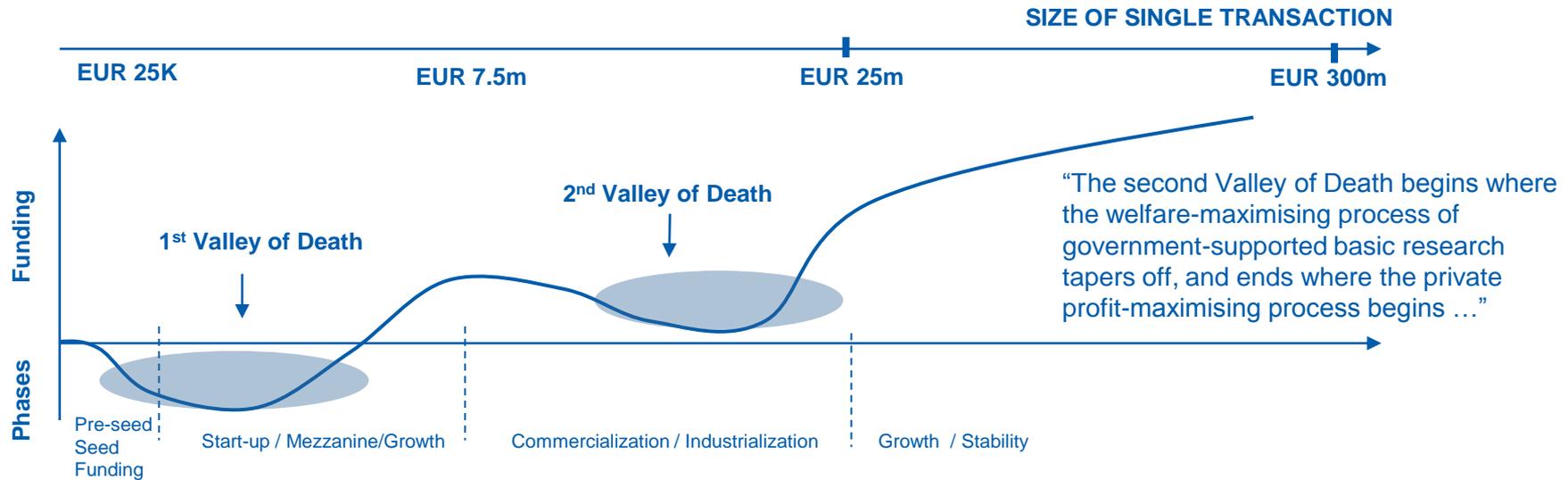
**Number of Innovative Mid-Caps by Country (Source: PWC 11/21012)**



- ❖ The total number of Mid-Caps is estimated at c. 28,000. Innovative mid-cap companies investing in RDI projects and undergoing a period of commercialization (stable cash-flows) in the EU is estimated at just over 14,000 (ca. 50% of all Mid-Caps) and employ c. 9.1m people.
- ❖ The total RDI project investments for all SMEs, Mid-Caps and large companies in the EU 27 in 2008 was EUR 279.5 billion. Mid-caps and larger entities accounted for EUR 194.9 billion or 70% of the total innovation expenditure.
- ❖ Although the general economic outlook has worsened, the majority of Mid-Cap companies have been maintaining (66%) or increasing (17%) their investments in RDI.



# Innovation lifecycle and funding needs of SMEs and Midcaps



- ❖ Policy papers and research studies identify two troughs in the supply of capital to innovative SMEs and mid-caps. The **first Valley of Death**, whose existence is attributed to a lack of early stage risk capital for start-ups, is currently addressed by the EIB Group via the EIF products (Seed, TT, VC).
- ❖ The **second Valley of Death** inhibits innovation's transition from technical and economic feasibility to commercial production. The occurrence of the second Valley of Death at the intersection of these two stages in the innovation sequence is due to the dearth of financing available to RDI projects during the post-creation venture capital stage. This results in businesses being financially ill-equipped for the creation of new value chains, upscaling, demonstrations, testing and co-developing with end-users.

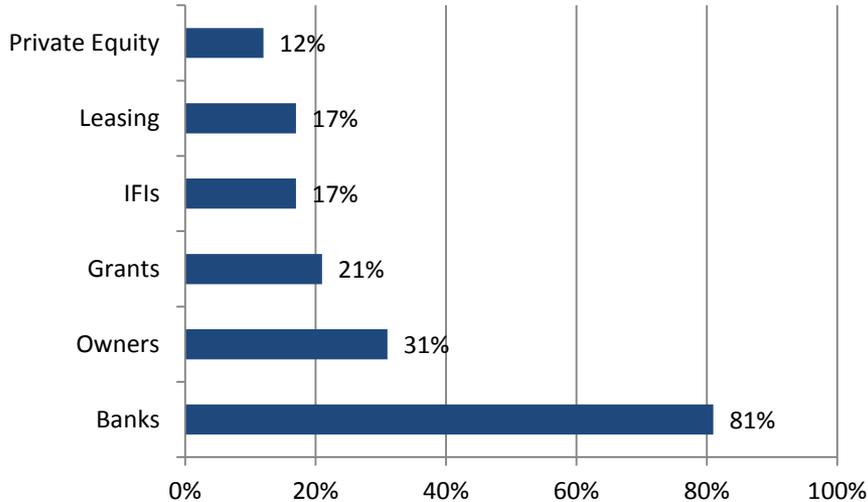


# Mid-Caps and their Role in Innovation

## What are the key debt financing trends in the EU for Innovative Mid-Caps?



### Sources of Funding for Mid-Caps by Importance in 2011 (PWC)



- ❖ Banks are by far the most widely used source of debt funding (see chart beside).
- ❖ The loans that are currently available by commercial banks are primarily short-term loans.
- ❖ Basel II/III requires high capital charges for large tickets and long tenors explaining partly the shortfall in the availability of long-term loans for many Mid-Caps.
- ❖ 50% of Mid-Caps are unsatisfied with the security and guarantee requirements as well as the tenor of financing options currently available.
- ❖ The majority of Mid-Caps feel that the availability of financing targeted specifically at RDI had worsened in the recent months.
- ❖ **For mid-sized and larger mid-caps, 75% of surveyed companies will be seeking up to EUR 30.0m and 40.4m of debt financing respectively. The average annual loan size for all mid-caps that expect to raise funds is EUR 40.1m.**

### Average Ticket Sizes of Mid-Caps seeking debt financing

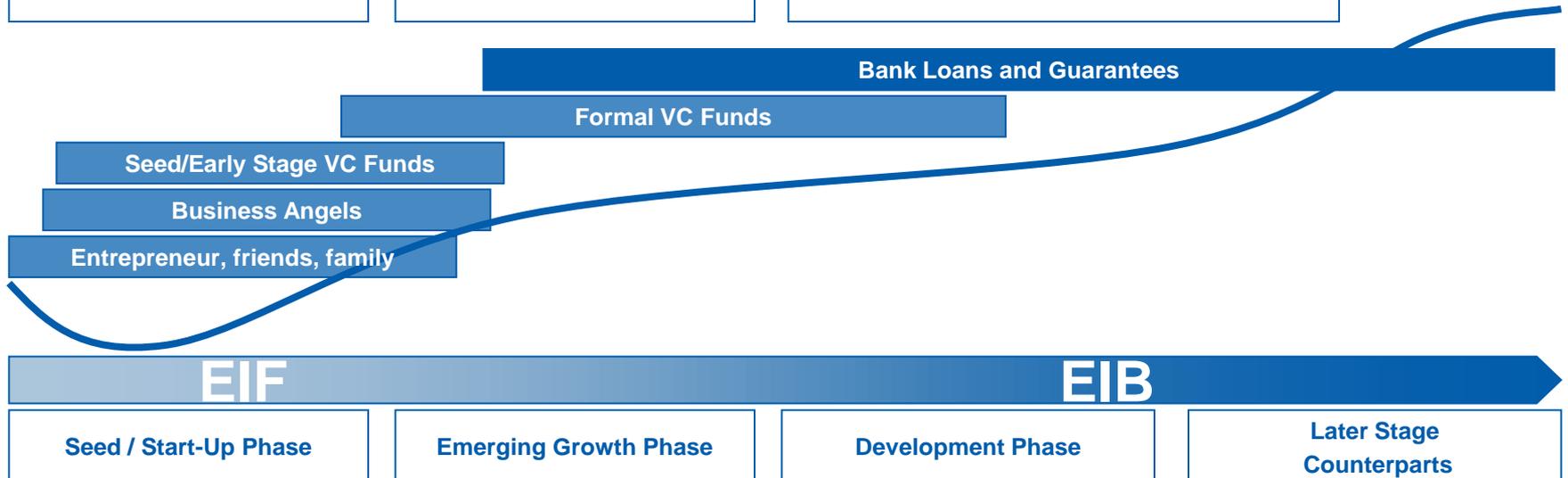
Copmany Size	Average Ticket Size	Min	Median	Max
250-499	EUR 11.0m	EUR 0.4m	EUR 2.0m	EUR 50.0m
500-999	EUR 52.5m	EUR 0.5m	EUR 25.0m	EUR 225.0m
1000-2999	EUR 63.7m	EUR 5.0m	EUR 10.8m	EUR 300.0m
All Mid-Caps	EUR 40.9m	EUR 0.4m	EUR 10.0m	EUR 300.0m

# The European Investment Bank Group

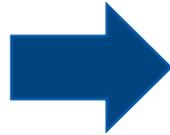
## EIB Group Product Offer – RDI and Growth



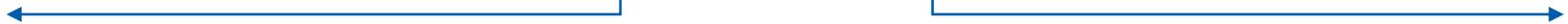
Knowledge transfer, Early-stage	Equity for Venture Capital, Mezzanine Funds	Debt
<ul style="list-style-type: none"> <li>Facility: Competitiveness and Innovation Programme (CIP), Ecotech, EIB Risk Capital Mandate</li> <li>Purpose: IP financing, technology transfer, seed financing, investment readiness, early-stage VC</li> <li>Target Group: VC Funds, Business Angels, Universities</li> </ul>	<ul style="list-style-type: none"> <li>Competitiveness and Innovation Programme (CIP), EIB Risk Capital Mandate, Fund of funds mandates</li> <li>Growth financing for SMEs, mid-caps</li> <li>Formal VC Funds, Mezz funds</li> </ul>	<ul style="list-style-type: none"> <li>RSFF, RSI (RSFF for SMEs; new product in development) EIB loans, CIP</li> <li>RDI financing, growth financing</li> <li>SMEs/MidCaps, Banks, PE Investors (sub-investment grade), Corporates, Public Sector entities</li> <li>Loans (incl. Mezzanine), Funded Risk Sharing Facilities with Banks</li> </ul>



# Risk Sharing Finance Facility principles



**RSFF**  
[up to EUR 10bn  
assuming  
leverage of 5.0x ]



## Direct Lending

- Corporate / Project Financing
  - Senior Loans (*pari passu*)
  - Subordinated Debt

## Indirect Lending / Financing

- Financial Intermediaries  
(extend lending capacity)
  - Risk Sharing
  - Co-financing



## RSFF Value Added Proposition

- Complementary stable funding source
- Long Maturities of up to 10 years
- Large single loan sizes (< EUR 300m)

- Strong technology/industry expertise
- No cross selling / Take and hold strategy
- Signaling Effect: EIB as quality stamp

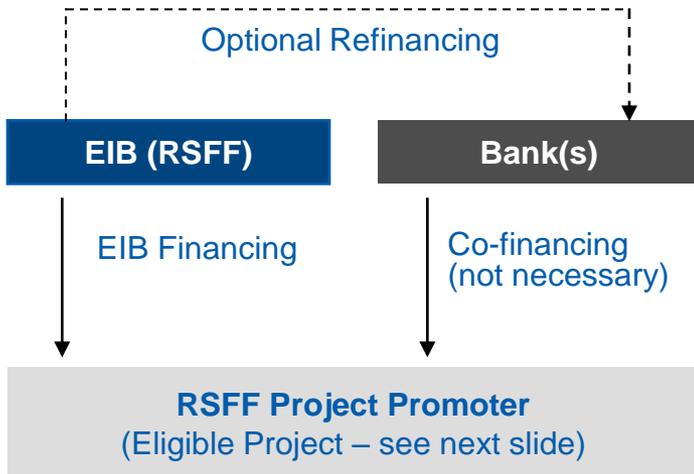


# RSFF Direct Financing

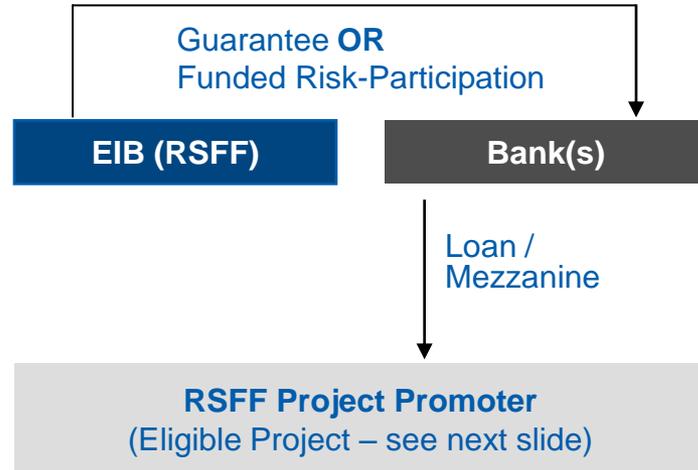
## Typical Transaction Structures



### OPTION 1: Parallel Financing Approach



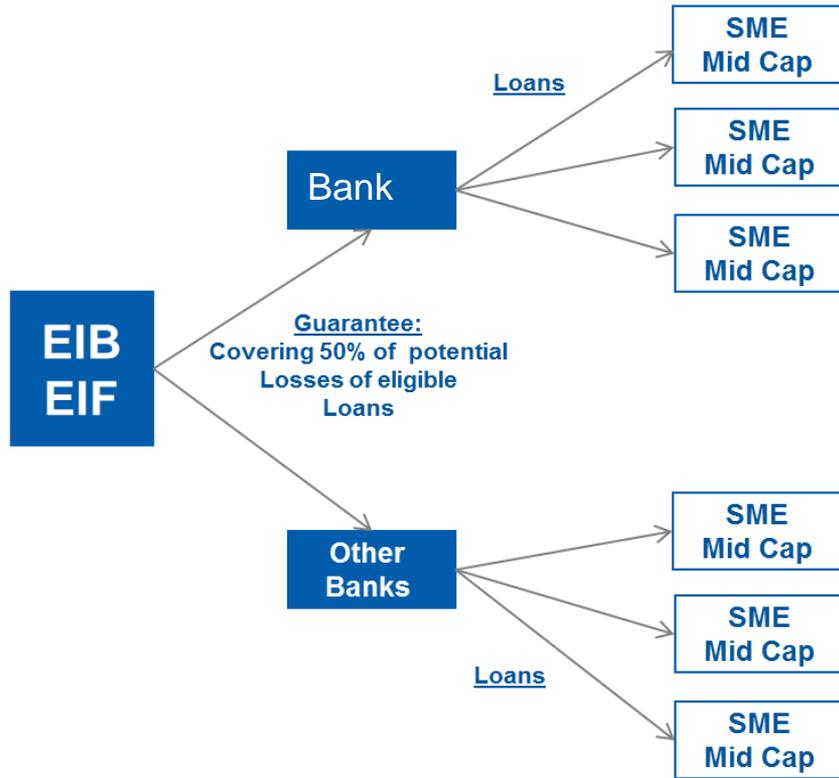
### OPTION 2: Back-to-Back Financing Approach



- To finance individual projects, EIB can either act as the sole financing provider or as a co-financing partner to other bank(s).
- In the case of co-financing, EIB could provide a direct financing agreement in parallel to other financing(s) from financing partner(s) or provides back-to-back to the financing partner(s).
- EIB financing contracts normally are in line with market standards (protective clauses, covenants, etc.) but will always be structured according to the needs of the borrower.
- EIB financing can also be junior to co-financing banks (e.g. Mezzanine financing)



Product Structure Chart



**Product Rationale: Improve senior debt lending capacity in the field of RDI financing.**

**RSI/MCI Facilities under RSFF:**

- ❖ Under the indirect financing approach, the EIB Group shares risk of up to 50% of loans from house-banks to innovative SMEs and small Mid Caps (up to 500 employees) under RSI. A new product (MCI; under development) could cover companies from 500 to 3,000 employees.
- ❖ Loan amounts can range from:  
 RSI: EUR 25,000 to EUR 7.5m  
**MCI: EUR 7.5m to EUR 50m**
- ❖ Loan maturities range from 2 years to 7 years;
- ❖ The key operational handling of the product is designed to be straight forward to operate and manage (simplicity is key);
- ❖ The product provides capital relief for the financial intermediary.



## Future developments

- EIB priority for knowledge economy will be on:
  - ❑ New and breakthrough technologies with long lead time
  - ❑ Innovation activities for the market launch of new products, processes and services
  - ❑ Integrated private sector projects strengthening competitiveness and enhancing Europe's position as a major provider
  - ❑ Without neglecting public sector R&D programmes
  
- Reinforce the expertise to identify and deliver robust projects
  
- Develop a portfolio of financial instruments:
  - ❑ RSI and MCI through RSFF
  - ❑ Leveraging on structural funds
  - ❑ Deepening of the EU VC market
  - ❑ Corporate innovation platform
  - ❑ Non-banking instruments