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INFORMAL MEETING OF MINISTERS FOR INDUSTRY (COMPETITIVENESS COUNCIL)

PANEL DISCUSSION: 'BE INNOVATIVE - GO INTERNATIONAL'

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Ministers,

I would like to look successively at two elements of the theme "Be Innovative – Go International".

1. Innovation

Starting with innovation, we support the broad definition taken by the Commission in its SME policy. We indeed believe that innovation should be encouraged in all its forms, be it innovation in technology, in design, in services or in business models.

Hi-tech start-ups

The first type of innovation activity that I would like to touch on is high-tech start-ups.

This activity involves very high risks, and generally involves recourse to venture capital as a source of finance.

The discussion paper that we received ahead of this Council discusses the health of the European venture capital industry. I must say that for me, the situation of the European venture capital industry is not as reassuring as is suggested by the document.

The document underlines that the European venture capital industry is more integrated than has been generally supposed. This is certainly good news. But the fundamental problem remains that the volumes of venture capital invested by European operators are much smaller than those invested by their American counterparts. Let me give you an example. In 2007, Europe filed two to three times more patents for clean technologies in 2007 than the US. However, for the same year, corresponding venture capital investments were little more than one third of American investments in these technologies.



How can we inject fresh dynamism into venture capital activities in Europe?

I see four policy lines:

- First, introduction of national tax incentives for creation of innovative businesses. France has taken a major step by introducing, in 2004, the “Young Innovative Company” status. This status confers tax exemptions on SMEs (with fewer than 250 employees) that spend at least 15% of their total annual expenditures on R&D. These companies are exempt from all corporation tax and all capital gains tax for 8 years after their creation. The measure provides incentives for both companies and investors. It should inspire similar initiatives in other countries through the new SBA governance process or application of article 173 of the Lisbon treaty on the competitiveness of industry.
- Second, reinforcing the long-term financial base of European venture capital operators, which is chronically fragile. It would be worthwhile to explore, for example, scenarios for steering a larger portion of pension funds’ resources towards venture capital companies, to take but one example.
- Third, removal of obstacles to operators’ cross-border activities. We await with interest the Commission’s proposals in this area.
- Last, the EU and EIB Group should continue to deploy venture capital instruments such as the GIF, the High Growth and Innovative SME Facility. The amounts allocated under this facility to risk capital operators encourage them to finance SME projects which would normally escape their attention for a number of reasons. One reason can be, for example, that projects offer a good return over the long term rather than over the near term.

Other high-growth SMEs

Let’s now consider innovative businesses in a lower risk class than high-tech start-ups. These can be for example high-tech enterprises that are in their second phase of expansion. Or it can be companies based on other forms of innovation, which are starting up or growing.

The challenge here is to ensure that these SMEs have access to the wider spectrum of finance justified by their different risk profile.

Indeed, these SMEs do not necessarily want to be financed massively by venture capital operators. Rather, these SMEs are looking for bank loans. However, banks may be reluctant to grant classical loans to these SMEs, for instance because they do not have sufficient collateral.

It is therefore important that the public authorities enable the offer of tailor-made financial products occupying the middle ground between venture capital and classical bank loans.



Three types of such financing products are particularly useful:

- Loans with attractive conditions, facilitated by the fact that a public authority puts up guarantees against the risk of default of payment;
- Mezzanine finance products, like subordinated or convertible loans. Once again, guarantees provided by public authorities can play a key role in making these products more attractive;
- Financial guarantees granted to SMEs under favourable conditions, thanks to special public counter-guarantees.

BUSINESSEUROPE notes that the offer of these financing products suffers from some limitations in many member states. These can be limitations in terms of volume, or in terms of economic attractiveness of the products on offer.

We are therefore very pleased with the broad spectrum of EU financial instruments developed by the Commission and the EIB Group over recent years. It was right to focus on supporting both technological innovation-based companies and other growth based-companies.

We are in particular happy that the 7th Research Framework Programme (FP7) and the Competitiveness and Innovation Programme (CIP) contain instruments to address market failures in covering the specific needs of:

- Small firms in the first expansion phase, having insufficient collateral;
- High growth SMEs in further expansion stages.

BUSINESSEUROPE appreciates very much the growth impulse that has been given by the Risk-Sharing Financial Facility (RSFF), the High Growth and Innovative SME Finance Facility (GIF), and the SME Guarantee Facility (SMEG). The fact that these instruments have a revolving effect is also very positive.

These instruments should be further enhanced and continue to occupy a prominent place in the future EU budget. I would like to draw your attention to this particular point in the context of the preparation of the EU Multiannual Financial Framework.

The key importance of equity finance

As an SME moves along its growth path, the consideration that should have precedence is constitution of a solid equity base. A balance sheet with strong equity reduces the enterprise's vulnerability to the ups and downs of business life.

It is therefore essential to adjust the tax systems which penalise equity financing over debt financing. As you know, Belgium has done this by introducing the "Notional Interest Deduction" system.

We recommend that the Commission and the Member States consider including this system in the list of best practices to be discussed in view of broader dissemination.



2. Going international

I would like to turn now to SME internationalisation, stressing five points.

First of all, I would like to underline companies' strong preference for market access rules developed at WTO level. By promulgating a single set of rules for all WTO countries, WTO considerably facilitates companies' internationalisation operations.

The largest problem faced by European SMEs is formed by non-tariff barriers to trade. For instance, in many commercial sectors, exporting to or opening an establishment in Japan is virtually impossible given the difficulties posed by non-tariff barriers present in that country. It is vital to solve this problem.

Regarding EU trade policy instruments, SMEs expect them to be transparent and easy to use, without having to call for the help of specialised lawyers.

Another issue is improvement of information to SMEs on the regulatory environment in third countries. A number of public or private information services exist at national or European level. However, these initiatives are fairly disparate and there are gaps in the provision of information services. The Commission should explore what synergies might be developed between the existing services.

Lastly, I would like to underline the great usefulness, in some sectors, of clusters and networks which support SME internationalisation.

In Italy, more than one hundred export consortia have been created, providing a whole range of services to affiliated SMEs. National and transnational export consortia should be promoted through the EU SME policy and through the SBA governance process.

There is also an Italian law encouraging the creation of business networks, based on "network contracts" between companies. In these networks, companies put together some parts of their operational activities, for example in relation to international trade. Tax incentives are granted for investments in networked activities. Dissemination of this network model should be encouraged through EU initiatives, looking also at how to foster the creation of transnational networks.

In conclusion, I would like to thank the Hungarian Presidency for its initiative which has enabled today's debate with the main stakeholders concerned on how to strengthen the innovation capacities and internationalisation of SMEs. BUSINESSEUROPE very much hopes that, with the momentum generated by the Hungarian Presidency and then the Polish Presidency, every effort will be made to maximise the new impetus that the Commission has given to SBA policy.
