

Theory vs. Reality: Venture Capital in Europe

A Verve Capital Partners Analysis of Europe's Annual Venture Capital Spent

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Introduction

Most investors understand how venture capital (VC) promotes economic growth. The flow of equity into innovative start-ups can fuel job creation and drive industry development. It lays a foundation for a breeding ground for innovation and inventions. Therefore, the amount of VC money spent in a country is a telling metric to grasp the growth potential and sustainability of this country's economy. Indices exist to compare the VC climate in various countries. We at Verve Capital Partners were curious, what is the VC spent per capita in European countries; and subsequently, does the actual VC spent per capita correlate with attractiveness rankings?

Expecting that the "most attractive" countries would yield the highest VC per capita, some of our findings were surprising.

Analysis

The analyzed European countries fell within five distinct groupings according to the actual amount of VC spent per capita.

GROUP ONE Switzerland (\$69) and the Netherlands (\$62) had the highest VC spent per capita in Europe. As a benchmark, the U.S. was calculated at \$67. Switzerland's leadership regarding actual VC invested is clearly reflected in its high attractiveness rank (#6) according to the Global IESE Venture Capital Attractiveness index. According to IESE, Switzerland scores well across all "VC attractiveness" dimensions analyzed - among those the quality of deal opportunities (i.e. a flow of technology spin-offs from its world-leading research universities) as well as its attractive taxation. But Switzerland's top position is also made possible due to the help of foreign investors (Switzerland is a net importer of VC) and the expansive

\$70-\$60



Figure 1: Venture capital spent per capita

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wealth of Swiss citizens. The Netherlands' top position has to do with a similarly high VC attractiveness index (#9) and - very much like Switzerland - with a high GDP per capita.

GROUP TWO Some Scandinavian countries - Sweden, Finland (both \$59) and Denmark (\$53) - also performed well above the \$35 European average. Like group one, these countries' excellent ranks regarding their actual VC spent are well founded by their VC attractiveness indices: #8, #12 and Denmark ranking #11. And again not surprisingly, their attractive VC environments are complemented by above-average GDP per capita.

\$60-\$50

GROUP THREE The European average (\$35) is exemplified by the U.K. and Ireland (around \$39), Belgium (\$33) as well as France (\$31), whose actual VC spent already positions these countries well behind the second group. This group is the first to deviate from our expectations as most of these countries' actual VC spent per capita is notably lower than their attractiveness rating would suggest. Especially the U.K. is commonly perceived

to be one of the leading VC spots in Europe and its VC attractiveness ranking (#3) suggests the same. Much like France (#15 of the globally most attractive), this counter-intuitive finding might have to do with their centralistic economies focused on its large capitals. While especially London remains a leading VC breeding ground, peripheral regions and populations deflate the actual figures of VC spent per capita. There have been

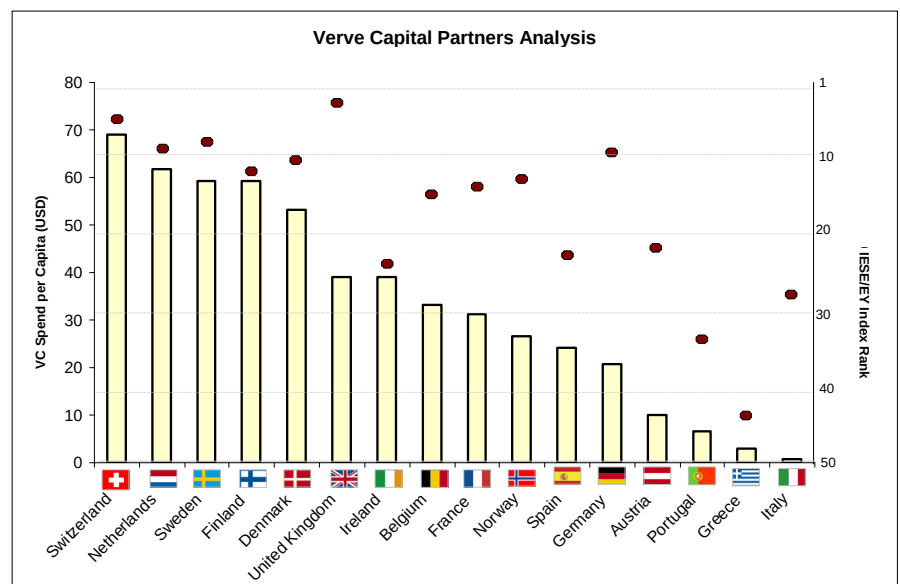


Figure 2: Illustration comparing the VC spent per capita to the VC index rank

attempts to artificially create start-up hubs in the periphery, but more time might be needed for these initiatives to bear fruit.

GROUP FOUR The next group of Norway (\$27), Spain (\$24) and Germany (\$21) spends less VC per capita than the European average. In theory, the economic powerhouse of the European Union, Germany, with a population approaching 82 million is ranked #10 according to IESE's VC attractiveness ranking and should thus be doing fine. However, actual VC spent is little more than \$20. Norway (#14) is even more surprising, as one of the world's richest countries with a GDP per capita of almost \$55'000. The gap between a high VC attractiveness but a low rate of actual VC investments in countries like Germany and Norway

\$30-\$20

- but also France and the UK - might be due to economies traditionally relying on heavy industry, manufacturing or wealth derived from natural resources. This heritage does not force entrepreneurs to constantly innovate and create new markets, while resource-scarce and smaller countries like Switzerland traditionally had to rely on high-tech innovation to stay competitive. Germany is known for being a financially conservative country with a rigid regulatory environment and a strong sense of investor protection. While these qualities are seen as positive for some attractiveness indices, start-ups require flexibility, rely on angel investments and can get bogged down with legal costs or bureaucratic constraints in their early stages. IESE's index does not seem to attribute sufficient weight to these factors. Besides, a high corporate R&D activity (as IESE attests Germany for instance) might result in lots of patents but is not necessarily a good indicator for the innovativeness of a start-up ecosystem.

GROUP FIVE The red lantern is carried by small countries such as Austria (\$10), Portugal (\$7) and Greece (\$3) as well as one of Europe's biggest countries: Italy (\$1).
\$10-\$00 This finding is consistent with low attractiveness rankings of Portugal (#34) and Greece (#44). Italy should be doing better according to the index (#28), however, Italy - like Portugal and Greece - has a GDP per capita figure below \$31'000, so it simply lacks the financial potential of the north. Austria (#22), to the contrary, should think about ways to unleash the potential of its wealth: \$40'400 GDP per capita.

Conclusion

Looking back at our results, we conclude that theory (in this case: the IESE index) and reality only match in countries with a strong VC activity. But the differences in other countries are very specific and depend on a mixture of cultural and economic influences - thus, they are very difficult to map in a comprehensive index.

While a relatively high investment interest in start-ups does exist in some European countries (groups one and two), this should not be seen by politicians and investors as a call to rest on their laurels. Many recent political initiatives to promote a thriving start-up ecosystem across Europe proved to be of limited success. Especially in wealthy countries such as high-spending Switzerland or low-spending Austria, enabling private investments outside of traditional investment vehicles such as VC funds has more potential to boost these economies. In this context, innovative concepts to channel the wealth of private investors to capital-seeking entrepreneurs with sustainable and innovative business models promise to be more effective in achieving this goal.

While indices such as the IESE VC attractiveness index provide a helpful framework for assessing the relative venture capital potential of different countries, they tend to obscure our view when it comes to finding solutions for fostering a vibrant start-up ecosystem. Understanding the needs of start-ups and VC investors goes beyond analyzing the political, social and economic macro-dimensions. Only if capital-seeking innovators and innovation-seeking investors are efficiently brought together, theory and reality will go hand in hand.

About *investiere* and Verve Capital Partners

Verve Capital Partners, a Swiss AG based in Zug, Switzerland was founded in 2007. With the goal to develop and implement innovative financing concepts, in February 2010, the team at Verve Capital Partners launched *investiere* (www.investiere.ch) and opened a previously insulated and elusive market of innovative Swiss start-ups to the general public via an online platform.

In contrast to crowdfunding companies, *investiere* is a hybrid model that combines the established practices of traditional venture capital with elements of e-finance and social media. All start-ups featured on the site go through a rigorous due diligence process and investors are able to choose the start-up that sparks their unique interest.

investiere delivers its services together with its strong cultivated global network of entrepreneurs, investors, subject matter experts and partners.

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Appendix

Table 1: Verve Capital analysis of venture capital spent per capita in comparison to the 2011 IESE and Ernst & Young Venture Capital and Private Equity Attractiveness Index

Country	Verve Capital Partners Analysis: average VC spent per capita	IESE VC attractiveness index rank	GDP per capita
Switzerland	\$68,99	6	\$42.600
U.S	\$66,54	1	\$34.800
Netherlands	\$61,77	9	\$40.300
Sweden	\$59,30	8	\$39.100
Finland	\$59,23	12	\$35.400
Denmark	\$53,09	11	\$36.600
United Kingdom	\$39,08	3	\$47.200
Ireland	\$38,91	24	\$37.300
Belgium	\$33,15	16	\$37.800
France	\$31,12	15	\$33.100
Norway	\$26,54	14	\$54.600
Spain	\$24,10	23	\$29.400
Germany	\$20,63	10	\$35.700
Austria	\$10,00	22	\$40.400
Portugal	\$6,57	34	\$23.000
Greece	\$2,92	44	\$29.600
Italy	\$0,82	28	\$30.500

Method

Venture capital (VC) spent per capita was calculated in the following manner: research from each country's individual venture capital association was evaluated to understand the total venture capital spent. For the purpose of this analysis, venture capital is defined as the sum of seed/start-up stages and early development and expansion stages. The country's venture capital spent was then divided by the population to get a per capita estimate. This estimate was averaged with the OECD Venture Capital Indicator (often OECD uses a percentage of GDP to express venture capital). GDP for each country was taken from World Bank 2010 Current Indicators as well as the CIA World Factbook. The average of Verve Capital's research and OECD's indicators is referred to in this document as the "venture capital per capita spent". The European average of VC spent per capita was calculated at \$35.46.

Sources

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