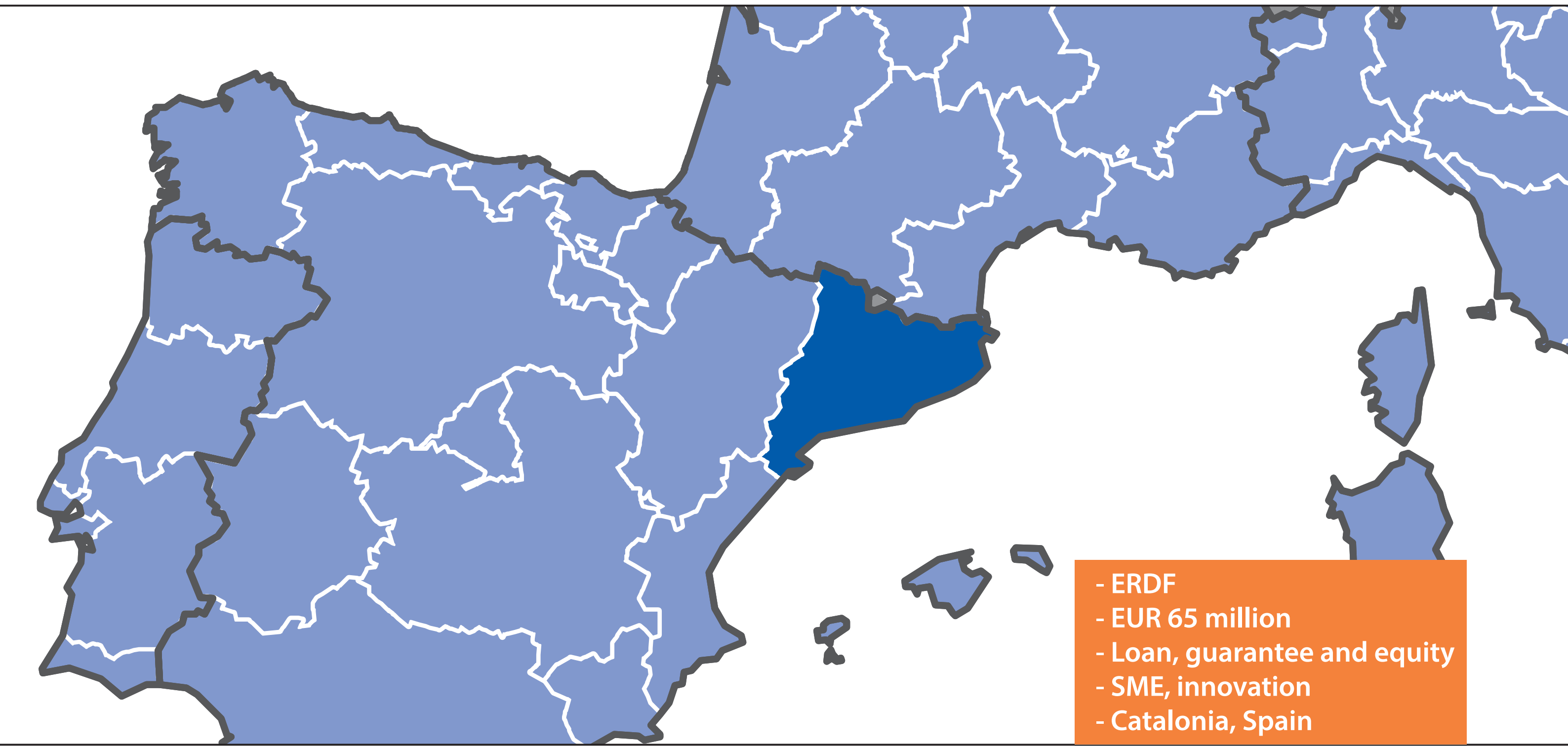

- ERDF
- EUR 65 million
- Loan, guarantee and equity
- SME, innovation
- Catalonia, Spain

*… supporting SMEs and the development of the private investment market …*

# Financial instruments for innovative firms

## Case Study

European Commission

European Investment Bank The EU bank

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The case projects can in no way be taken to reflect projects that will actually be financed using Financial Instruments. Neither the European Investment Bank nor the European Commission gives any undertaking to provide any additional information on this document or correct any inaccuracies contained therein.

The authors of this study are a consortium of three companies: t33 (lead), University of Strathclyde – EPRC and Spatial Foresight.

# Abbreviations

| | |
|---|---|
| ACC1Ó | Catalan Agency for Competitiveness |
| ERDF | European Regional Development Fund |
| ESIF | European Structural &Investment Funds |
| ICF | Instituto Catalán de Finanzas (Catalan Institute of Finance) |
| IFEM | Instrumentos Financieros para Empresas Innovadoras (Financial Instruments for Innovative Enterprises) |
| MA | Managing Authority |
| OP | Operational Programme |
| R&D | Research & Development |
| SME | Small and Medium-sized Enterprise |
| VC | Venture Capital |

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# 1 Summary

The Fund was set up in 2007 under the Catalan ERDF Operational Programme 2007-13, initially with a total allocation of EUR 50 million split equally between the ERDF (EUR 25 million) and regional government co-funding (EUR 25 million). The Fund comprises four schemes: a guarantee scheme supporting SME development and growth; a risk capital scheme supporting the development and consolidation of risk capital funds for SME start-ups and expansion; a micro credit scheme providing small loans to micro-enterprises; and a co-investment scheme offering joint loans with business angels to innovative SME in their start-up and expansion phases. The regional government's financial institution (ICF – Catalan Institute of Finance) designed the schemes and set up a subsidiary Limited Company (IFEM – Financial Instruments for Innovative Firms) as fund manager.

This Fund has contributed to regional economic development by supporting the creation and growth of SMEs and the development of the private investment market in Catalonia. By the end of 2013, 1209 guarantees were granted, venture capital (VC) investments were made in 7 VC firms to support 36 projects, loans were made to 18 projects jointly with accredited business angel networks and 50 projects were supported with microloans. The attraction of private sector investment varies significantly across the schemes: from 10 times the public contribution under guarantees, to 5 times for joint loans with business angels and for venture capital instruments and 2 times for microloans. Despite the lower rates under the co-investment scheme loans and venture capital schemes (compared to guarantees), such instruments are considered to play a critical role in supporting systemic change in the financing environment and long-term economic development.

A key lesson for promoting effective financial instruments is the need for critical mass to ensure effective participation from local banks, guarantee companies, venture capital firms and business angel networks, while minimising the administrative burden of management. Other success factors include the need for sound analysis of financing gaps, careful management of public and private tensions and flexiblility to adapt the strategy to changes in the socio-economic context. The positive experiences and lessons learned have provided a solid basis for continuing the delivery of the programme's objectives through financial instruments in 2014-2020, depending on the results of the ex ante assessment.

**Name**

JEREMIE Catalonia

**Funding source**

ERDF

**Type of FI**

Guarantees, loans, equity

**Financial size**

EUR 50 million Total = EUR 25 million from ERDF + EUR 25 million public regional funding. Increased to EUR 65 million (of which EUR 28.3 million ERDF) at end of 2014.

**Absorption rate[1]**

42% (at the end of 2013)

**EU leverage[2]**

11.9 (leverage effect of ERDF funds)

**Leverage of public resources**

5.2 (leverage effect of ERDF and other public funds)

**Re-investment**

Most repayments will be made from 2016 onwards

**Thematic focus**

SME support

**Partners involved**

Financial intermediaries (local banks/guarantee companies, venture capital firms and business angel networks)

**Timing**

From 2007 to 2015

**Main results**

By end of 2013, 1209 guarantees were granted; venture capital investments were made in 7 venture capital firms to support 36 projects; loans to 18 projects made jointly with business angel networks and 50 projects supported with microloans.

[1] *This refers to the absorption rate of all OP allocations for this financial instrument. It is calculated as funds disbursed to final recipients divided by funds available through the OP.*

[2] *This refers to the leverage effect of EU funds, in this case of ERDF. It is calculated as total funds available to final recipients divided by the amount of ERDF financing.*

# 2 Objectives

Catalonia is one of Spain's most economically advanced regions. As highlighted in the socio-economic analysis of the ERDF OP 2007-2013, Catalonia witnessed strong economic growth and performance in the 1990s and 2000s prior to the onset of the crisis. Despite a high employment rate, key labour market challenges are the seasonal, precarious and low-productivity nature of many jobs along with a strong dependence on the construction sector. Industry has a relatively stronger weight in the Catalan economy than in the rest of Spain and the EU as a whole and there is a vibrant business sector based on SMEs (notably in the textiles, automotive and consumer electronics sectors), albeit facing difficulties in accessing external finance and subject to strong competitive pressures from other EU and emerging economies. The key challenge identified in the ERDF OP is a decline in competitiveness in the early 2000s. Expenditure on R&D and innovation in Catalonia is relatively low compared to the EU15 average, although it is above the national average and has a relatively strong private sector share.

Set against this background, the Catalan ERDF OP 2007-2013 focuses on four objectives: (1) Improving the conditions for competitiveness and supporting the information society (2) sustainable development (3) improving accessibility and mobility and (4) local/urban development and social and territorial cohesion. The programme has a total budget of EUR 1.4 billion (ERDF EUR 679 million) and is structured according to four Priority Axes (plus technical assistance) corresponding to the above objectives. The business development objective of the first priority axis (P1 Innovation, business development and knowledge-based economy) has three strands: SME support, business innovation and competitiveness and access to finance. Financial instruments contribute to the access to finance strand with the overarching objective of addressing financing gaps for SMEs to support growth across the different phases of SME development and increase the global orientation of Catalan firms.

The majority of the interventions under the access to finance objective are supported through the instruments set up under the JEREMIE initiative. The specific objectives are: to increase the number of new companies with high growth potential; to involve financial market actors in the development of high quality financial instruments to boost growth and competitiveness; and to increase investment in R&D and encourage private investment. The Fund includes four main types of instrument: guarantees (capital to mutual guarantees and convertible debt) in favour of technology-based SMEs and SMEs with high growth potential; micro loans for start-ups; venture capital for early stage start-ups; and loans made jointly with networks of business angels through a co-investment scheme.

The JEREMIE Fund was introduced following the recommendations of an EIF study on how to address gaps in the finance available to firms in Catalonia. The instrument is managed by the Institut Català de Finances (ICF), a financial institution owned by the regional government that facilitates business access to finance. The other main body with responsibility for SME support is the Catalan government's regional development agency for business development, innovation and internationalisation (ACC1Ó, previously CIDEM), which primarily provides business support services but also manages some aid schemes and financial instruments.

# 3 Set up of the financial instrument

The Fund was set up in 2007 under the Catalan ERDF OP 2007-13, initially with a total allocation of EUR 50 million split equally between the ERDF (EUR 25 million) and regional government co-funding (EUR 25 million). The ICF was responsible for designing the package of schemes supported by the Fund and setting up 'Financial Instruments for Innovative Firms' (IFEM - Instruments Financers per a Empreses Innovadores) as a subsidiary Limited Company to act as fund manager in 2008. Following the appointment of IFEM's Board of Directors in April 2009, the financial intermediaries were selected for the different schemes - specialists in venture capital, loans, micro loans and guarantees - allowing implementation to proceed.

## 3.1 Preceding events

The ERDF OP Catalonia 2007-2013, approved by the European Commission in November 2007, included the option of setting up a fund under the access to finance objective of the business development priority. Preparations for setting up a fund for SME support took place during 2006/2007, in parallel to the development of the OP. This included a joint study with the EIF on financing gaps in Catalonia, including an assessment of a package of schemes proposed for inclusion under the JEREMIE framework by ICF. The planned instruments were considered to address key market gaps in access to finance, although some general and scheme-specific recommendations were made by the EIF to improve their effectiveness.

The main gaps in the market identified were:

- Loans and guarantees: Gaps in the availability of guarantees for SMEs in terms of volume, type and integration with the private sector.
- Microfinance: Gaps in the availability of microcredits for social enterprise and particularly for SMEs. There is also a shortage of qualified financial intermediaries which limits the possibility of satisfying potential demand.
- Mezzanine: Gaps in volume of equity loans.
- Venture Capital: Low investment volume and average level of investments.
- Networks of private investors: Low investment volume due to high perceived risk linked to an unfavourable environment and insufficient complementary instruments (guarantees, loans).

The package of schemes proposed by the ICF within the JEREMIE framework was assessed as addressing the key market gaps identified and several general recommendations were made by the EIF. First, to focus available resources on a limited number of schemes to maximise the market reach. Second, to exploit scale opportunities through inter-regional/cross-border initiatives and by seeking additional financing resources. Third, to consider the "whole offering" of connected financial instruments and services to SMEs. Fourth, the financial instruments should be adequately communicated to the market. Fifth, delegation to financial intermediaries should be well thought-out and precisely implemented and monitored avoiding interference in decision-making.

Specific recommendations were made for several of the proposed schemes. First, an increase in the funding to the guarantee scheme was recommended. Second, a reduction in the allocation to the venture capital scheme was proposed to avoid risks of low take-up or reduced competition. Third, the microfinance scheme for start-ups could use a portfolio of guarantees to incentivise the uptake of the facility and agile procedures should be ensured, i.e. all loans granted by a given financial institution that complies with the established set of eligibility criteria are automatically covered by the guarantee.

*Source: EIF (2007) Estudio de evaluación del acceso a la financiación de la PYME en CATALUÑA, Diciembre de 2007.*

The formal decision to designate the ICF as the Fund Manager was confirmed on 21 December 2007 through the Act on Fiscal and Financial Measures approved by the Catalan Parliament. At the first Monitoring Committee of the OP in March 2008, the project selection criteria for all interventions in the programme were discussed – subsequently approved and published in June 2008 - and the committee members were informed of the next steps for setting up the Fund. The Funding Agreement between the Fund Manager (ICF) and the Directorate General for Economic Affairs of the regional government's Ministry of Economy and Knowledge (the intermediate body with overall management responsibility for the OPs regional interventions) was subsequently signed on 25 June 2008, setting out the key financing arrangements and contractual obligations.

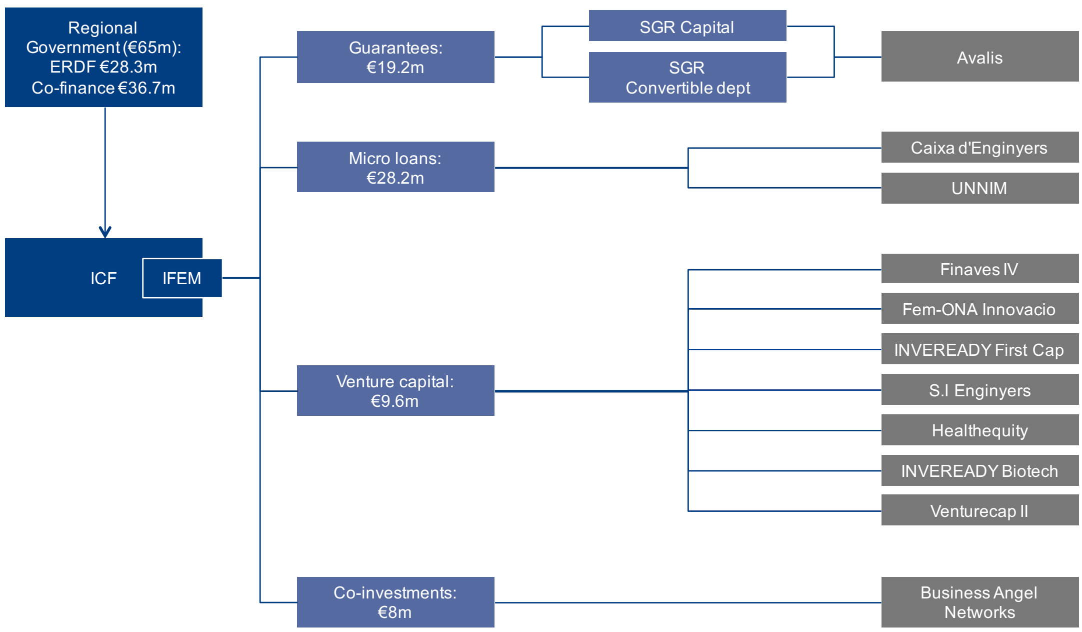
The ICF then created a subsidiary body 'Financial Instruments for Innovative Firms' (IFEM - Instruments Financers per a Empreses Innovadores) on 12 December 2008 as the Fund Manager. The IFEM Board of Directors was established on 1 April 2009, with overall responsibility for key decisions relating to the development and implementation of the schemes, notably the approval of funding conditions and the selection of financial intermediaries. A common approach was used for selecting the financial intermediaries for the different schemes. This involved launching competitive processes for each scheme, a pre-selection of applicants, evaluation of business plans, formal selection of successful applicants and adoption of bilateral contracts setting out the obligations to the Fund Manager and final recipients. For the guarantee schemes, competitive processes were launched in 2009 (for the capital strand) and in 2010 (convertible debt guarantees), both of which were awarded to the same guarantee company (Avalis de Catalunya). The micro-credit scheme competitive processe was launched in 2009 and awarded to three intermediaries in 2010, although one of these intermediaries subsequently pulled out. The first competitive processe for the risk capital scheme was opened in 2010, followed by two further competitive processes in 2012 and 2013, leading to the selection of a total of eight financial intermediaries (risk capital funds/firms) by the end of 2013.

Following the selection of financial intermediaries, it was the responsibility of each intermediary to assess and select project applications in line with the requirements set out in the bilateral contracts between the intermediaries and the IFEM.

## 3.2 Funding and partners

The ICF was responsible for designing the package of schemes supported by the Fund and setting up IFEM as a subsidiary Limited Company to act as fund manager. The financial intermediaries selected by IFEM are specialists in venture capital, loans, micro loans and guarantees. IFEM is represented on the governing boards of the financial intermediaries responsible for the venture capital and co-investment schemes. The ICF also has a stake in the guarantee company (Avalis de Catalunya) that acts as the intermediary for the guarantee scheme, which was set up as a public-private venture by the Catalan government in 2003 to provide access to credit for SMEs.

*Figure 1: Scheme of funding relationships*




The overall budget of the JEREMIE Fund is EUR 65 million, of which EUR 28.3 million is from the ERDF and EUR 36.7 million is co-funding from the regional government (Table 1). The most recent estimates of private sector investment attracted is EUR 336.8 million (Table 2). In terms of specific instruments, guarantees are expected to attract 10 times the public investment, while participative loans and venture capital instruments are expected to attract 5 times the public investment. The equivalent rate for micro loans is lower at 2 times the public investment.

*Table 1: Funding sources at Fund level*

| Funding sources | EUR |
|---|---|
| ESIF (ERDF) | EUR 28.3 million |
| Public (regional) | EUR 36.7 million |

*Source: JEREMIE Catalonia Funding Agreement, Revised Version of 19 November 2014*

| Instrument | Regional Govern-ment | EU (ERDF) | Total | EU Leverage | Multiplier or Leverage of public resources | Investment attracted |
|---|---|---|---|---|---|---|
| Guarantees | 10.1 m | 9.2 m | 19.2 m | 21 times | 10 times | 192.2 m |
| Venture Capital | 7.1 m | 2.5 m | 9.6 m | 19 times | 5 times | 48.0 m |
| Micro loans | 15.0 m | 13.3 m | 28.2 m | 4 times | 2 times | 56.5 m |
| Co-invest-ment loans | 4.6 m | 3.4 m | 8.0 m | 12 times | 5 times | 40.0 m |
| Total Fund | 36.7 m | 28.3 m | 65.0 m | 11.9 times | 5.2 times | 336.8 m |

*Table 2: Funding sources and investments attracted at Fund and instrument level (EUR million)*

## 3.3 Implementation

The fund manager (IFEM) was specifically established to manage the financial instruments and is responsible for key functions relating to the Fund, notably the selection of financial intermediaries, compliance with selection criteria, control, monitoring, reporting and publicity requirements for the financial instruments.

The IFEM receives annual ERDF payments from the regional OP as agreed in the Funding Agreement. Following an initial transfer of EUR 15 million in 2008, the remaining allocation (EUR 35 million) was distributed in equal tranches of EUR 7 million annually between 2009 and 2013. Payments to financial intermediaries are undertaken following the relevant checks required by EU Regulations.

## 3.4 Governance

The governance arrangements between the fund manager (IFEM) and the regional OP managing body and between IFEM and the financial intermediaries are established in the Funding Agreement in accordance with EU regulatory requirements. As noted, IFEM has the lead management role in terms of setting up the schemes, selecting the financial intermediaries, monitoring implementation, complying with control requirements and reporting to the regional programme management secretariat. It is staffed by a director, two analysts (responsible for management and control/audit respectively) and a lawyer. Key decisions within the IFEM are taken by a board of directors. These include approving the terms and conditions of the different schemes, selecting the financial intermediaries and agreeing revisions to the investment strategy, if necessary. The board is composed of 4-8 members, initially including representatives from the Ministry of Economy and Finance of the regional government, the regional development agency (CIDEM), the ICF and, as an observer, a representative of the European Investment Fund (EIF).

The financial intermediaries are in turn responsible for implementing the schemes, subject to the contractual conditions and requirements agreed with IFEM. The monitoring, reporting, control and other compliance arrangements are formally agreed in contracts with each financial intermediary and set out in the IFEM management and control manual to comply with EU regulatory requirements.

# 4 Strategy

The investment strategy aims to support the objectives of the OP through a guarantee scheme supporting SME growth; a risk capital scheme supporting risk capital funds for SME start-ups and expansion; a micro credit scheme providing small loans; and a co-investment scheme of participative loans with business angels accredited by IFEM. Revisions to the strategy were made to facilitate absorption involving internal reallocations across the schemes and, more recently, an increase in the Fund's budget and changes to product terms.

## 4.1 Investment strategy

The investment strategy is set out in the Funding Agreement with the MA, comprising a description of the different schemes characteristics and objectives within the framework of the OP objectives on business development and access to finance: a guarantee scheme for SMEs to facilitate access to financial products that support growth and the strengthening of the general activity of the firms; a risk capital scheme that aims to develop and professionalise the risk capital market by supporting the creation and consolidation of new risk capital funds for the start-up and expansion phases; a micro credit scheme for SMEs providing small loans for the creation, development and expansion of business; and a co-investment scheme of participative loans with business angels accredited by IFEM.

**Loan to tech-based start-up Bibulu (Barcelona)**

Bibulu is an online platform (bibulu.com) that connects dog owners with sitters to host their dog while they are unable to or are away, charging a commission per transaction. The tech-based start-up was founded in Barcelona in March 2013 by Enrico Sargiacomo with advisory support from an engineering manager on the technological aspects. Following the launch of the website, the company sought finance from investors with the ambition of developing the concept and expanding to other geographical markets across Europe. Financial support was obtained under the co-investment scheme of the Fund, in the form of a participative loan by IFEM.

## 4.2 State Aid

The guarantee scheme (convertible debt strand) and micro loan scheme fall under the de minimis Regulation. The contracts between IFEM and the financial intermediaries include a clause with the formula for calculating the gross grant equivalent of aid and a requirement for the intermediaries to calculate this for funded projects. Project contracts with recipients must specify the gross grant equivalent of aid and include a declaration by the recipient identifying any de minimis support received in the last three years to verify that the de minimis limits are not exceeded.

The venture capital, co-investment and guarantee schemes (mutual guarantee strand) fall under  the General Block Exemption Regulation. IFEM is responsible for sending to the Commission the form with summary information under the reporting obligations required under the Regulation (Annex III, Regulation 800/2008).

## 4.3 Financial products and terms

The financial instrument for SME support provides guarantees (capital to mutual guarantees and convertible debt), venture capital, loans (offered jointly with business angel networks) and microloans, under the following product terms and project selection criteria.

*Table 3: Product terms and selection criteria*

| Product description and conditions | Project selection criteria |
|---|---|
| **Guarantees** | |
| Split in two strands:<br><br>1. Capital to mutual guarantee companies (MGC) through a permanent capital investment in the MGC to reinforce their capacity to provide guarantees to SMEs. The outstanding risk must be maintained above 90% of the total funds disbursed times 10 and the maximum amount per operation is EUR 625,000 (estimated average is EUR 150,000)<br><br>2. Convertible debt. Acquisition of convertible debt issued by mutual guarantee companies aimed to partially pay the company's capital contribution to the MGC, and provide extra treasury to it. When the MGC gives a guarantee, 2.5% of the amount is converted from debt to mutual capital on behalf of firms (which contribute 1.5% instead of 4%)<br>Applications by beneficiary firms are made directly to the mutual gurantee companies. | 1. Innovative background and level of activity supported by the business model<br><br>2. Coherence between resources (technical, human, financial) and planned growth targets<br><br>3. Capacity of the management team<br><br>4. Degree of preparation and maturation of the proposal as well as technical and economic feasibility<br><br>5. Consistency of the proposed size with reality and needs of the sector, suppliers and clients |

| Loans | |
|---|---|
| IFEM provides participative loans jointly with business angels that are members of business angel networks accredited by IFEM, up to the same value of the loan made by the business angels. The projects are proposed and selected by the business angel networks. IFEM formalises the loan contract directly with the firm. Special consideration is given to projects based on R&D and new technologies.<br><br>The conditions of the IFEM part of the loan are: value range of EUR 50,000-200,000, with a term of 5 years and maximum grace period of 2 years; interest rate has a fixed component (Euribor+5.5%) and a variable component which depends on the implementation of the business plan (up to 15% in total, including the fixed rate); default interest at 10%; and management fee is 0.5% per annum. | 1. Quality and viability of the projects<br><br>2. Professionalism of management: corporate experience in the sector, technical competences, and coverage of all business management areas<br><br>3. Adequate return on risk |
| **Micro loans** | |
| Loans aimed at financing investments and working capital for the establishment, consolidation or expansion of micro enterprises through projects that contribute to development, job creation and social objectives. IFEM provides 50% of the funds to the financial intermediaries, and also shares 50% of the risk on an individual loan basis. This guarantee is capped at 10% of the funds provided by IFEM.The maximum value is EUR 25,000 per final recipient and 100% of the project. The loan term is up to 7 years with a grace period of 2 years. The interest rate can be fixed or variable linked to Euribor. Management fees in line with market conditions. | 1. Quality and economic viability of the projects<br><br>2. Coherence between the resources (technical, human, financial) and planned targets |

| Venture capital | |
|---|---|
| Minority stockholding in capital finance for early stages focusing on start-up projects in R&D and new technologies. Most are "classic" VC (capital and convertible loans), but IFEM have invested in a Venture Finance Fund (loans with interest + free shares of the investee company). Distribution among entities with a professional team and independent investment committee. | 1. Quality and viability of the projects<br><br>2. Professionalism of management: corporate experience in the sector, technical competences, and coverage of all business management areas<br><br>3. Competitive advantages: the firm's product/s will develop an advantageous position against the competition on the market<br><br>4. The business is geared towards markets with significant growth and growth potential in the long-term |

*Source: Based on OP selection criteria and Funding Agreement.*

Final recipients can obtain soft support (e.g. advice, coaching, mentoring) from some of the financial intermediaries managing the schemes, notably the venture capital fund managers and business angel networks. The participative loans with business angels in start-ups can also prepare the recipients for subsequent rounds of financing in their growth phases, some of which is supported through the ICFs subsidiary ICF Holding. The micro loans scheme aims to facilitate subsequent access of final recipient firms to other financial instruments and programmes appropriate to their needs, but there is an absence of consolidated soft support measures for this scheme or as part of the guarantee scheme.

Most of the funding from the schemes will be repaid from 2016 onwards for further investments in projects. A small share of funding has been disinvested form the venture capital fund. The guarantee scheme allows a revolving effect within the financial intermediary.

**Loan to tech-based start-up Bibulu (Barcelona)**

The participative loan obtained by the tech start-up BIBULU from IFEM provided a top-up to the loan from business angels. IFEM initially provided a loan of EUR 60,000 which was renegotiated and extended a year later to a total loan of EUR 110,000. The repayment of the principal will begin in May 2015. The founder of the firm did not consider alternative options and chose the loan because the conditions were considered to be flexible, notably the two year grace period for the start of repayments. The recipient also appreciated the flexibility to extend the loan and obtain financing quickly, which provided the necessary liquidity to gain traction and grow the business.

## 4.4 Final recipients targeted

The schemes managed by the IFEM are designed to target SMEs because of the challenges faced by this group of firms in acquiring external funds, especially for innovative projects with considerable risk.

The communication of the Venture Capital Fund to recipients is presented as good practice example in the 2012 Annual Implementation Report of Catalonia's ERDF OP in terms of the wide dissemination to potential recipients and the public through presentations to businesses and publications. It also notes that the coverage of eligible recipients as a share of the population is relatively large given the varied and complementary nature of the different schemes.

**Co-investment in the tech-based start-up Bibulu (Barcelona)**

The founder of the company was aware of the ICF (and IFEM subsidiary) as a source of financing because it is a well-known institution among entrepreneurs in the region of Catalonia. The entrepreneur also appreciated the availability of a contact point at IFEM and considered that the institution was acting as a genuine co-investor through the provision of a participative loan with an interest in the company's growth.

## 4.5 Project types

The guarantee scheme targets SMEs in their start-up phases, firms with growth potential, firms that are developing and expanding as well as general business activity.  The micro credit scheme offers small loans to micro-sized firms for the establishment, consolidation or expansion of micro enterprises through projects that contribute to development, job creation and social objectives. By contrast, the venture capital and co-investment loan schemes target more innovative SMEs that invest in R&D, start-ups, expansion and technology-based ICT companies.

## 4.5 Changes in strategy

The main changes to the strategy involved internal reallocations in funds across instruments. The performance of the micro loan scheme was below expectations and one of the financial intermediaries pulled out of the scheme. This led to a transfer of funds at the end of 2012 from the micro loan scheme (- EUR 10.9 million) to the venture capital (+ EUR 1.9 million) and co-investment (EUR + 9 million) schemes. Within the guarantee scheme, there was also an internal transfer from the capital strand to the convertible debt strand of EUR 4 million. These changes led to a revision of the Funding Agreement in May 2013 including a more detailed description of the funding schemes and eligibility criteria.

Following a reprogramming of the ERDF OP to address absorption challenges in other interventions, an increase in the overall budget of the financial instrument for SME support was agreed including reallocations across the schemes and changes to the product conditions with a view to keeping the programme on track to meet its objectives. The main change was a significant increase in the budget of the microcredit scheme and in the threshold of the maximum value of the loans. New types of loans are also planned to address current market failures relating to access to finance for investments in start-ups in the cooperative sector as well as investments in early stage spin-offs from universities and research centres.

# 5 Achievements

This Fund has contributed to regional economic development by supporting the creation and growth of SMEs and developing the private investment market in Catalonia. By the end of 2013, 1209 guarantees were granted, venture capital investments were made in 7 venture capital firms supporting 36 projects, loans were granted to 18 projects jointly with accredited business angel networks, and 50 projects were supported with microloans.

## 5.1 Output

By 31 December 2013, the following outputs were reported for each scheme in the 2013 Annual Implementation Report:

- Guarantees – capital to guarantee companies: 356 guarantees were granted for a total investment of EUR 49 million in micro (79%), small (16%) and medium (5%) enterprises.
- Guarantees – convertible debt: 854 guarantees were granted for a total investment of EUR 106 million in micro (64%), small (25%) and medium-sized (11%) enterprises.
- Venture capital: Investments made in 7 venture capital firms to support 36 projects.
- Co-investments: Participative loans approved by IFEM (as co-investments with private investors in business angel networks accredited by IFEM) supporting 18 projects (EUR 2 million) of which 12 (EUR 1.2 million) had been contractually agreed by the end of 2013.
- Micro loans: 50 projects supported by two banks acting as financial intermediaries (Caixa d'Enginyers and Grupo BBVA).

**Loan to the tech-based start-up Bibulu (Barcelona)**

Bibulu is a successful start-up. Since the company was created in February 2013 in Barcelona, it has grown rapidly expanding to employ 14 staff. Towards the end of 2014, Bibulu merged with a UK competitor (DogBuddy) and is now operating in 5 countries across Europe (Spain, Italy, France, Germany and the UK). The participative loan from IFEM was regarded as very important by the company's founder to get exposure, gain traction and grow the business to this stage.

# 6 Lessons learned

EU funding has provided a positive stimulus for developing and reinforcing SME financing schemes in Catalonia. A key lesson for promoting effective instruments is the need for critical mass to ensure effective participation from financial intermediaries while minimising the administrative burden of management. Additional success factors include the need for sound analysis of financing gaps, for careful management of public and private tensions and for flexiblility to adapt to changes in the socio-economic context. The positive experience provides a solid basis for setting up similar instruments under Catalonia's new regional ERDF programme for 2014-2020.

## 6.1 Main success factors

From the perspective of the Fund Manager, the key success factor for setting up effective financial instruments is **critical mass**. Without sufficient critical mass the administrative set-up and implementation costs associated with the financial instrument can be too high to ensure effective participation and buy-in from financial intermediaries. Additionally, it is important to consider the different roles of different instruments in supporting policy objectives and avoiding an exclusive focus on simplistic performance indicators such as financial leverage. For instance, while venture capital support and participative loans may attract lower levels of private investment, they can be more effective instruments for promoting systemic change in the financing environment and supporting long-term economic development.

The ex-ante evaluation of the OP highlights the additionality of the ERDF as a key source of added value, noting that EU co-funding was critical for the viability and development of the financial instrument schemes in Catalonia (OP ex-ante evaluation 2007: p52).

More generally, a study of ERDF-funded financial instruments in Spain has highlighted several lessons from the experience in three regions (including Catalonia) and at the national level (Red2Red 2012: 87-88). The first is the need to **begin the planning process early** because of the long lead-in time needed to set up the instruments and to draw on relevant experience to avoid design and set-up difficulties associated with limited knowledge or experiences in working with financial instruments, financial institutions or ERDF requirements. A related recommendation is to draw on the knowledge and the experiences with financial instruments of other public authorities in Spain (both ERDF and domestically funded) and managers of financial instruments.

Second, the need to **find niche markets based on sound analysis** is an important lesson. As the number and type of financial instruments for business development are increasing across Spain, ex-ante assessments will be critical to identify the financing needs of businesses in different regions.

Third, **the relationship between the public and private sector** raises several tensions that need to be carefully managed. For example, to manage the schemes in the best interests of final recipients and maintaining high standards in selection criteria in an environment of restrictive bank lending.

Fourth, **fund managers need to be flexible** to adapt the supply of financial instrument to demand especially in a period of financial instability. The experience of the micro-finance scheme in Catalonia is pertinent here. As performance and take-up was below expectations, it was necessary to transfer part of the allocation to other financial instruments with stronger investment capacity. However, following absorption challenges in other parts of the ERDF programme, the budget of the micro scheme was increased along with changes to the product conditions to facilitate take-up.

Fifth, it is necessary to **create incentives to introduce some competition** (beyond the flexibility at the Holding Fund level to transfer funds across schemes) between financial intermediaries to ensure take-up and minimise the pressures of decommitment at the end of the funding period.

## 6.2 Main challenges

The main challenges faced are two-fold. First, there are **administrative challenges in the design of adequate monitoring and reporting tools so to adress (regulatory) requests for information from EU and national/regional entities**. For instance, increasing the professionalization, market orientation and critical mass of effective financial instruments (especially venture capital funds) requires operating in national and international markets outside of the region. This presents a challenge in demonstrating the precise volume of funding that is invested in final recipients established within the eligible region but which may also operate at a wider scale, even though investment clauses in the contracts between IFEM and the risk capital fund intermediaries do guarantee that the overall funds are invested within the region with a local multiplier effect.

Second, the **market conditions** following the fallout of the crisis were not the most suitable to promote the different financial products. In particular, saving banks in Spain were in a process of structural change of their governance arrangements or even dissolution and liquidation. However, following absorption challenges in other parts of the ERDF programme outside of the financial instruments framework, the budget for the micro loans scheme was increased significantly along with changes to the product conditions to increase their attractiveness and contribute to the achievement of the programme's objectives.

## 6.3 Outlook

The draft ERDF OP for 2014-2020 refers to the positive experience and results with financial instruments in 2007-2013, which provide a solid basis for continuing the delivery of the programme's objectives through financial instruments in 2014-2020, depending on the results of the ex ante assessment.

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