



## Challenges in financing start-ups and potential solutions

4<sup>th</sup> of October 2017

Challenges and opportunities of financing start-ups have been at the core of the 50<sup>th</sup> session of the *INSMEAcademy* that took advantage of the high level expertise of Mr. Jean-Louis Leloir, Special Adviser to the Board of Directors at the European Association of Guarantee Institutions.

Financing is a challenging issue both from the start-ups and the banks' point of view. Lenders need to have a clear understanding of a company's past situation, to know its performance and viability in order to accept the risk of granting a credit. It goes without saying that given the nature of start-ups this kind of information cannot be provided. The speaker stated that there is an 'asymmetry' of information between the borrower and the lender: the borrower is perfectly aware of what the business is and how it is going to evolve, but this is something the lender can understand only through written documents and explanations. This imbalance of information leads to hesitation that is sometime translated in the refusal to grant the credit.

Mr. Leloir referred that banks meet diverse challenges in financing startups given the fact that:

- the rate of startups default is 30% to 50% in a five year horizon;
- SMEs have a weak financial structure and in many cases entrepreneurs do not have additional financial capabilities, at least in the proportion needed, to guarantee equity in their companies in case of difficulty;
- entrepreneurs are often in charge of every aspect of the company and it is hard to manage several issues at the same time. In addition it is statistically proven that entrepreneurs usually have a single main knowledge and often miss financial culture.

Nevertheless financing startups also offers a number of opportunities since:

- they renew the SMEs population;
- they allow banks to enlarge their portfolio of clients and develop new activities that can contribute to the banks' future growth;
- they are a driver of job creation, unleash initiatives, bring enthusiasm and motivation which are essential factors for the dynamism of the business ecosystem.

By taken this positive impact into account, diverse measures to support startups have been established, both on a public and a private level. By referring to the public sector's measures, Mr. Leloir highlighted that among the instruments developed, it is worth mentioning specific guarantee funds offering a significant coverage in case of default, grants or small loans programmes.

The Speaker also stated that guarantee programmes are recognized as the main instrument of access to finance for startups.

As mentioned, the private sector too plays a significant role in this frame. Professional bodies such as chambers of commerce propose information centres, offer trainings and advisory teams dedicated to start-ups and provide them with simplified information on administrative processes and access to the different elements of support. They also act as facilitator providing assistance and instruments for matching the investors in research of potential targets with young enterprises in need of equity. These matching instruments can be developed both on a national and an international level and also be specialized on macroareas of interest which make the access to this instrument easier. A crucial role is played by associations of entrepreneurs: they involve experienced people that can share competences and knowledge, offer tutorship to young entrepreneurs and sometimes they provide financial support such as personal loans. Additionally these associations have a good reputation, according to statistics they increase the survival rate of the companies they assist by 50%. Worth to be mentioned are seeds and venture capitals which represent a very relevant support to start-ups. Equity investors are active partners, meaning that they tend to actively participate in the project, but this phenomenon is still limited representing a small percentage in the start-ups population.

Mr. Leloir also presented emerging opportunities related to the new economy or 'e-economy'. Given the fact that changes occur very quickly, the new economy offers new chances and large potential markets. Talking about alternative forms of financing the speaker referred to crowdfunding that in the last five years has become one of the key to access finance for SMEs, but he also mentioned other forms of financing such as leasing and factoring.

By concluding his presentation the Speaker stressed that many actors work together in this field but they adopt different strategies and methodologies that do not match the needs of other partners involved. In order to solve the difficulties in accessing finance it is crucial to create a kind of 'confidence sharing' process and exploit the high potential of digitalization to match competences and opportunities.