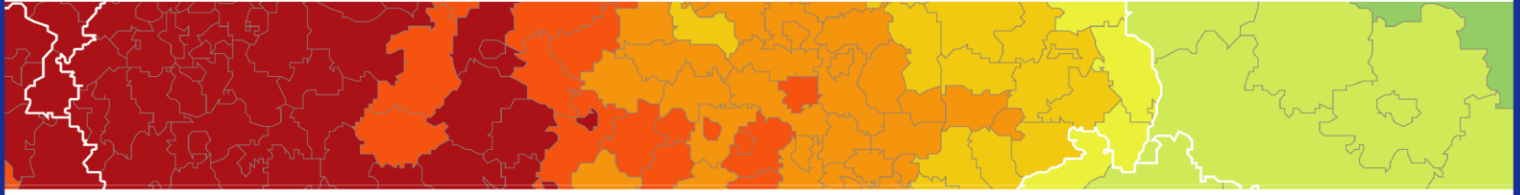


Inspire policy making by territorial evidence



Financial Instruments and Territorial Cohesion

Mellersta Norrland/Sweden

Case Study Report

30/08/2019

This applied research activity is conducted within the framework of the ESPON 2020 Cooperation Programme, partly financed by the European Regional Development Fund.

The ESPON EGTC is the Single Beneficiary of the ESPON 2020 Cooperation Programme. The Single Operation within the programme is implemented by the ESPON EGTC and co-financed by the European Regional Development Fund, the EU Member States and Partner States, Iceland, Liechtenstein, Norway and Switzerland.

This delivery does not necessarily reflect the opinion of the members of the ESPON 2020 Monitoring Committee.

Authors

Viktor Salenius, Nordregio (Sweden)
John Moodie, Nordregio (Sweden)
Kaisa Granqvist, Aalto University (Finland)

Advisory Group

Project Support Team: Cristina Wallez Cuevas, General Commission for Territorial Equality, France; Adriana May, Lombardia Region, Italy; Joerg Lackenbauer, European Commission

ESPON EGTC: Zintis Hermansons (Project expert) and Akos Szabo (Financial expert).

Acknowledgements

We would like to thank Jörgen Larsson, CEO of Inlandsinnovation (formerly Mittkapital); Eva Nordlander, CEO of Almi Invest in Mellersta Norrland; Lars Karbin, Chairman of the Board of Startkapital I Norr AB; Mattias Lööv, CEO of H1 Communication AB; Tobias Sjölander, CEO of Loxysoft AB, for taking the time to offer their useful thoughts, ideas and insights on the Swedish financial instruments ecosystem.

Information on ESPON and its projects can be found on www.espon.eu.

The website provides the possibility to download and examine the most recent documents produced by finalised and ongoing ESPON projects.

This delivery exists only in an electronic version.

© ESPON, 2019

Printing, reproduction or quotation is authorised provided the source is acknowledged and a copy is forwarded to the ESPON EGTC in Luxembourg.

Contact: info@espon.eu

ISBN 978-99959-55-97-7

Financial Instruments and Territorial Cohesion

Table of Contents

List of Tables	i
Abbreviations	ii
Abstract.....	1
1 Background	2
1.1 Economic and regional context.....	2
1.2 Summary background to the FI.....	2
1.3 Scope and objectives of the FI.....	2
1.4 Operational issues	3
1.5 Implementation issues	3
1.6 Scale and budget	4
1.7 Existing evaluation results.....	4
2 Main results and findings.....	6
2.1 Impact of the Financial Instrument.....	6
2.2 Value added of the Financial Instrument	10
2.3 Territorial dimensions of the Financial Instrument	12
2.4 Governance dimensions of the Financial Instrument.....	13
2.5 Strengths, weaknesses, opportunities and threats (SWOT).....	14
2.6 Typical or flagship projects.....	16
2.7 Overall assessment.....	16
References	17
List of Annexes	1
Annex 1: CS elaboration process.....	2
Annex 2: Flagship projects	3

List of Tables

Table 2-1: Table: Output and result indicator data for the two co-investment funds active in Mellersta Norrland. Programme period 2007-2013, situation at fund closure on 31.3.2017.....	7
Table 2-2: Comprehensive FI Assessment Matrix	9

Abbreviations

ERDF	European Regional Development Fund
FI	Finacial Instruments
GVA	Gross Value Added
ICT	Information and Communication Technology
IT	Information Technology
NUTS	Nomenclature of Territorial Units for Statistics
SEK	Swedish Kronor
SME	Small and medium-sized enterprises
SWOT	Strengths, Weaknesses, Opportunities, Threats

Abstract

The regional venture capital funds were first implemented under the ERDF programmes in Sweden during the 2000-06 programme period, and the Mellersta Norrland region was the location of one of the first of the regional funds to be launched. The main reason for the establishment of the co-investment funds, operating *pari passu* to strengthen the availability of private capital, was to reduce the capital-equity gap in the region caused by an imbalance between the private financial resources available and the demand by SMEs for funding and support. Twelve regional venture capital funds, managed by public sector agencies, now cover the entire country. In Mellersta Norrland, there are two venture capital funds co-financed by ERDF. The combined assets of the two public co-investment funds are €33 million, and of the €73 million invested in SMEs in the region, €45 million have been attracted from private co-investors.

The funds set up in Mellersta Norrland have had diverse and substantive impact on Mellersta Norrland – a remote region where the availability and utilisation of private risk capital have traditionally been sparse. The co-investment funds contribute to a more diversified economy by **supporting sectors that have few alternative sources of funding**, and to strengthening the local supply of private capital by **attracting private-sector partners that would not otherwise have invested**. Final evaluations have reported that there are positive signs that the funds' interventions have led to **increased number of employees among portfolio businesses** and have **improved the regional infrastructure for entrepreneurial financing**. The co-investment funds have also promoted **increased awareness and understanding about risk capital investment** in the region, informing both investors and businesses previously unaware of the opportunities associated with risk finance. Thereby the funds have contributed significantly to the regional economic ecosystem, both on the demand side by increasing the awareness and interest for risk capital among early-stage businesses in a range of sectors, and on the supply side by supporting local private investors with guidance and networking support as well as providing them with a co-financing platform that opens up previously unattainable investment opportunities.

1 Background

1.1 Economic and regional context

Mellersta Norrland (Middle Norrland) is one of the most sparsely populated regions in Sweden and the EU, with 4.8 inhabitants/km² and a 2016 population of only 374,245 (Regional Innovation Scoreboard, 2017). Regional unemployment stood at 6.8 percent in 2016, slightly below the national average and below the EU 28 average. The region's GDP per capita in 2015 (€30,600 PPS) was below the national average but above the EU 28 average. Mellersta Norrland is a NUTS 2 region made up of two relatively independent NUTS 3 regions, the county of Västernorrland and the county of Jämtland. The region is predominantly rural (forests cover about 67 percent of the area and the percentage of GVA from agriculture, forestry and energy is well above the national average) but the economy is dominated by heavy process industries.

1.2 Summary background to the FI

The regional venture capital funds in Sweden, built around equity financial instruments co-funded with the ERDF, are well-established, having been in operation over several programme periods. Mellersta Norrland was the location of one of the first of the regional funds to be launched. The regional venture capital funds were first implemented under the ERDF programmes in Sweden during the 2000-06 programme period. Three pilot partnership funds inspired by the Scottish Co-Investment Fund were launched in 2005, in the then Objective 2 programme areas of Västsverige, Gotland and Mellersta Norrland (Michie and Wishlade 2011).

1.3 Scope and objectives of the FI

The main reason for establishing the funds was to reduce the capital-equity gap in the region caused by an imbalance between the financial resources available in the market and demand for funding from SMEs. In addition, as a tool for regional development FIs are considered to be more cost-efficient than grants and there is a need to increase the flow of private capital in the region to promote the growth of SMEs (Nilsson 2012). The funds aim to invest in profitable companies, owned by committed entrepreneurs, which are in the early establishment stage but have a long-term business model which is attractive to investors (Nilsson 2012). The Swedish government does not require a return on investment from each fund; instead, the funds are designed to promote regional business growth, improve the regional infrastructure for entrepreneurial financing, and impact horizontal issues including gender equality, social integration and environmental issues (Nilsson 2012).

1.4 Operational issues

The co-investment funds operate with private commercial partners on equal terms: the ERDF/national agency contributes 50 percent and private investors contribute 50 percent, but each fund can only invest in their own region (Nilsson 2012). The funds' co-investment approach seeks to engage the private sector more proactively by investing *pari passu* in projects selected by private investors, which increases the incentive for and volume of investment. This approach specifically aims to take advantage of private sector expertise in the identification of appropriate investments. Although there was some initial uncertainty as to whether there would be private co-financiers willing to co-invest, results were considered positive – by July 2013 each SEK of fund investment had attracted an average of SEK 1.9 in private funding . The target group for funds include micro enterprises/SMEs and investment must supplement the market and not crowd out existing private investment (Growth Analysis 2016).

1.5 Implementation issues

From a territorial point of view, the Swedish approach to FI implementation is interesting, as 12 regional venture capital funds managed by public sector agencies cover the entire country. All 12 funds are managed by five different fund managers, and each fund is only allowed to invest in its own region. In Mellersta Norrland there are two venture capital funds co-financed by ERDF – Saminvest, belonging to the Almi Invest group, and Mittkapital (now Inlandsinnovation), a venture capital firm owned by a Swedish state pension fund (Nilsson 2012). Each fund employs a team of investment managers with a background in business management and solid knowledge of the local business community. Investments by the public funds are made on commercial grounds in long-term sustainable growth companies in areas such as forestry, energy, tourism, and the food industry (Nilsson 2012). The firms report annually on how many new firms and new jobs have been created through the funds.

In most cases, the co-investors attracted to the funds are private individuals, private companies, and organised capital (Tillväxtverket 2016). However, the region as a whole does not have a well-developed infrastructure for capital investment, which poses challenges for the development and implementation of FIs (Tillväxtverket 2011). In the first programme period, Almi Invest provided the majority of its funds to micro-enterprises in the IT and trade sectors at the start-up and early development stages, as the geographical area is largely dominated by capital intensive industries. In comparison, Mittkapital invested the majority of the funds in large, well-established companies in the industry and trade sectors, which seems to reflect the region's lack of entrepreneurial activity and limited venture capital finance availability. Most of the selected portfolio companies have used the funds primarily for market development, product development, and skills acquisition (Tillväxtverket 2011).

1.6 Scale and budget

Overall, SEK 3.4 billion¹ (c€367 million) has been invested in 320 companies across Sweden since 2009 (Growth Analysis 2016). In Mellersta Norrland, the combined assets of the two public co-investment funds is €33 million, and of the €73 million invested in SMEs in the region, €45 million has been from private co-investors (Tillväxtverket 2016).

1.7 Existing evaluation results

The mid-term evaluation of the funds found that demand varied between regions and had decreased in some parts of Sweden (particularly in the peripheral north) because of the economic downturn; there were also several problems with finding private co-funding. Given these issues, SEK 10-15 million² (€1.0-1.5 million) from one fund (located in northern Sweden) was transferred to funds in other regions. Most funds were still in the start-up phase at the time of the evaluation. However, the study noted that it was challenging for many of the funds to ensure a sufficient flow of solid deals and suitable investment partners, particularly in those regions dominated by large companies and industrial environments which historically have not had a culture of venture capital financing (Tillväxtverket 2011). The mid-term evaluation was generally positive, noting that the funds had helped increase the volume of capital to SMEs and the role of private investors in the region; however, the high levels of EU bureaucracy was regarded as a challenge by fund managers, with delays to setting up funds caused by difficulties in arranging co-financing agreements (Nilsson 2012).

The final evaluation report by the Swedish Agency for Economic and Regional Growth, which coordinates and evaluates all the co-investment funds at the national level, expresses that there are positive signs that the funds have increased the number of employees in businesses and improved the regional infrastructure for entrepreneurial financing. However, some of the impact goals set for the 2007-2013 programme period in terms of new jobs created and increased labour market equality have not quite been reached (Tillväxtverket 2016). The final report by Growth Analysis, another agency, notes that challenges persist in developing and implementing FIs (Growth Analysis 2016). These include unfavourable economic conditions, such as a lack of skilled companies and private capital, a fragmented entrepreneurial ecosystem, and inadequate regional leadership. There was also a significantly smaller number of investments within IT/telecommunications and life sciences businesses, with the greater proportion of money going to companies involved in transport and trade.

¹ Exchange rate Infoeuro (average of the corresponding time period (2009-2016): 1 SEK= €0.107808): http://ec.europa.eu/budget/contracts_grants/info_contracts/infoeuro/index_en.cfm

² Exchange rate Infoeuro (average of the corresponding time period (2009-2011): 1 SEK= €0.102981)

This final evaluation raises the question as to whether FIs are the right tool for promoting regional development and growth, noting that venture capital is vital for growth regions but cannot necessarily turn around economic development in underperforming regions that lack the required capital and have weak business infrastructure. In this regard, FIs are not considered a good substitute to existing grants and loans schemes. However, an overall analysis of the available capital and funding in Mellersta Norrland suggests that the region does not suffer from a worse investment gap than Sweden overall, but some actors in the regional economy are in a position which makes it difficult to get funding, and the public co-investment funds are seen as particularly helpful in this regard (Tillväxtverket 2017).

2 Main results and findings

2.1 Impact of the Financial Instrument

An understanding of the specific regional context in Mellersta Norrland is paramount in capturing the overall impact of the two co-investment funds based in the area. The regional economy in question, until the inception of the co-investment funds, was extremely unfamiliar with the processes and methods involved with financing enterprises with venture capital. This is partly due to the nature of industry in Mellersta Norrland, traditionally driven by sectors such as forest, mining and metal, where short-term risk capital into scalable innovations remains a secondary concern to the need to provide finance in support of long-term, incremental development. Consequently, an assessment of the impact of the co-investment funds ought to be approached from a perspective and with expectations substantively different from that of a similar analysis conducted in city-dominated and capital-rich regions.

The funds in Mellersta Norrland have clearly had significant impact in introducing and empowering a form of financing that was previously little-known in the region and which benefits otherwise underrepresented or disadvantaged sectors. Thus, the co-investment funds contribute to a more diversified economy and to strengthening the local supply of private capital by attracting stakeholders that would not otherwise have been available. On the one hand, the impact of the two co-investment funds in Mellersta Norrland has not swept across all sectors nor spread evenly in the region, as emphasised in the previous section with reference to the final evaluation report of the first programme period (Tillväxtverket 2016). On the other hand, however, the final report emphasises that this does not imply that the funds have failed to deliver but rather that the specific and regional nature of the impact is difficult to predict. Based on interviews conducted for this case study with fund managers and private-sector stakeholders, two kinds of specific impact stand out in particular.

First, the arrival of the co-investment funds has substantially strengthened local entrepreneurship and growth potential, particularly among early-stage firms, in a number of sectors where equity investment is a suitable but regionally scarce source of capital. These are predominantly enterprises that adopt scalable business-models for their growth and for whom the early-stage need for capital is much easier to raise through equity than by other means such as loans, for example. As innovation processes in some traditional local industries like forestry or metal work with different and more long-term financing strategies, the two co-investment funds have invested in a diverse range of other sectors, for which their presence in the region has become crucial. One interviewee recounts that interventions by the co-investment funds into ICT firms has in several cases contributed to keeping these employers in the region instead of relocating to capital-rich ICT clusters. The interviewees also emphasise that the relative impact of the co-investment funds has been much larger in Mellersta Norrland than it would be in capital-rich areas where risk finance is already available

by way of an established network of private investors. Moreover, because the expected returns are much lower by default in Mellersta Norrland than in metropolitan areas, the co-investment funds here have kept an open mind and invested more diversely in, for example, the tourism sector, which has clear growth potential in many regions but which often gets outcompeted by high-technology startups with faster growth predictions in larger finance hubs. Additionally, the risk threshold for the co-investment funds' operations is lower than for fully private investments as the former have no formal profit requirement, thus the intervention has contributed to the growth of new ventures at an earlier stage than private investors commonly fund emerging start-ups.

Between them, the Mellersta Norrland funds had made 30 exits in the region by 2015. As demonstrated by reporting on the output and result indicator data collected by the Managing Authority for the programme, the public funds have made venture capital investments in 56 recipient firms, predominantly SMEs and micro-enterprises, and these investments have given rise to over 200 new jobs in the region (by 2017, see table). Considering the sparse local conditions for achieving a critical mass in Mellersta Norrland, the effects of these direct impacts have, moreover, clearly also had indirect impacts in strengthening and diversifying the regional economy.

Table 2-1: Table: Output and result indicator data for the two co-investment funds active in Mellersta Norrland. Programme period 2007-2013, situation at fund closure on 31.3.2017.

Instrument	Expenditure	Final recipients supported							Result indicators		
		Clean tech	Retail/ tourism	Industry	ICT	Life Science	Other	Total	Jobs created women	Jobs created men	Jobs created total
Mittkapital i Jämtland och Västernorrland (Inlandsinnovation)	Total programme resources (€m): 15.9 of which ERDF: 8.0	1	4	5	n/a	n/a	7	17	20	19	39
Partnerskapsfond Mittsverige (Saminvest/Ami Mitt)	Total programme resources (€m): 11.5 of which ERDF: 5.8	2	11	10	10	1	5	39	45	147	192

Source: Managing Authority (Swedish Agency for Economic and Regional Growth).

Second, the co-investment funds have had a significant educative role in the region about processes related to risk finance, which has led to maturing of the local private investment supply and the establishment of several new private investment stakeholders. According to the interviewees, the initial plan when the co-investment funds were introduced was for these to be a supporting tool but for private investors to retain the lead and proactive initiative for seeking out and deciding on risk investments in the region. In Mellersta Norrland, however, it turned out that the supply of private risk finance by private stakeholders was very underdeveloped. The impact of the Mellersta Norrland funds has thus included the additional and partly unforeseen activity of raising awareness and spreading knowledge about risk finance.

Companies have become better at identifying the benefits of different finance alternatives, as the co-investment funds have provided information and networking opportunities to make sure that different funding instruments in the region find beneficiaries for which that specific kind of finance is most suitable.

Through the engagement of the regionally-focused public funds and their experienced personnel, many entrepreneurs who used to be suspicious of risk finance have been encouraged to make use of equity capital as a tool for growth, and many private stakeholders have been encouraged by the regional involvement of knowledgeable public instruments to embark on equity investments that they would not otherwise have made. In fact, the total amount of investments made by private co-investors over the programme period has been almost double the volume invested by the public funds, and this excludes the volume that private stakeholders invested on their own. An example from the flagship cases provided in the annex below is that the emergence in 2010 of Startkapital I Norr, a consortium of private investors spread around northern Sweden, was crucially inspired by its founders' observation of the opportunities created by the increase in public risk finance in the region. Inlandsinnovation, one of the two co-investment funds in Mellersta Norrland, has joined forces with the private consortium on several occasions and the two stakeholders collaborate actively in pooling their networks.

There are naturally similar ways in which the co-investment funds have impacts on society other than the main indicators measured by programme authorities and the financial output of the investments made. Capturing the full societal impact of the financial instruments is, however, very complex and multi-faceted. The following matrix aims to present a visualisation of the ways in which the Mellersta Norrland co-investment fund instruments contribute to the wider indicators and objectives of the Europe 2020 strategy, comparing what effects can be captured that relate to the three Europe 2020 sub-pillars of smart, sustainable and inclusive growth.

Table 2-2: Comprehensive FI Assessment Matrix

FI / Non-financial externalities	Smart growth			Sustainable growth			Inclusive growth			Urban/Regional development	Stakeholder involvement	
	Innovation	Education, training and lifelong learning	Digital society	Competitiveness	Climate change	Clean energy	Employment	Skills	Poverty		Efficiency and effectiveness in cohesion policy	PPP & knowledge-sharing
	Impact of FI on R&D investment intensity	Impact of FI on all levels of education and training	Impact of FI on uptake of ICT and development of digital economy	Impact of FI on regional competitiveness, with special emphasis on industry	Impact of FI on climate change adaptation and mitigation	Impact of FI on reduction of GHGs and uptake of renewable energies	Impact of FI on employment growth	Impact on FI on skills which are market oriented	Impact of FI on number of citizens living below poverty rate			
Mittkapital i Jämtland och Västernorrland (Inlandsinnovation)												
Partnerskapsfond Mittsverige (Saminvest/Almi Mitt)												

Source: own elaboration

	Significant non-financial externality
	Possible non-financial externality
	No non-financial externality

To summarise this sub-section, the impact of the public risk investment funds in Mellersta Norrland spans several dimensions of the regional economy and is visible as improved regional conditions as measured on a number of financial indicators. The co-investment funds have increased and supported the supply of local private capital by lowering the threshold of investments into, in particular, SMEs in sectors that have had difficulty finding other funding sources in the previously scarce and undeveloped regional private finance ecosystem. This is partly due to the higher risk tolerance of the co-investment funds, which operate with an aim to strengthening the regional economy, than of fully private venture capital investments, which commonly prioritise maximum expected return on investments. The SME-focus of investments by the co-investment funds has strengthened the growth potential of early-stage firms in the region and the wide range of supported sectors testifies that the co-investment funds have concretely contributed to diversifying the regional economy. Moreover, the understanding among regional actors of the rationale and benefits of risk capital finance has increased substantially since the inception of the co-investment funds. Overall, the maturing of the regional risk investment ecosystem and the raised awareness and experience among local stakeholders have gradually increased the impact of the co-investment funds' operations. There continues to be a steady demand for risk capital co-investments and neither of the public funds have had difficulty in finding enough portfolio companies in the region.

2.2 Value added of the Financial Instrument

This sub-section discusses what specific added value is generated by the structure and operation of the Mellersta Norrland co-investment funds in the assessment of the interviewed professionals. The first paragraph outlines the potential benefits of equity finance vis-à-vis other types of public funding and the latter part of the sub-section discusses the value added by the *pari passu* co-financing approach applied by the funds to the risk finance ecosystem of Mellersta Norrland.

As emphasised by the interviewed stakeholders, the specific value of channelling public structural funding as risk capital instead of as grants or loans is that this is an 'active' form of capital investment, which, for startups and early-stage companies in particular, adds many useful support structures to enhance their growth. The public and private equity investors bring considerable competence and experience to the board of directors of aspiring businesses and can thereby bring crucial insight to development and expansion processes. The co-investment funds also have an extensive business network both within and outside the region and can help portfolio companies connect with other investors and businesses for potential future collaboration. A further distinction between public risk capital and other kinds of public funding is that the former capital strengthens the balance sheet of the portfolio company while loans, recorded as company debt, weaken it. Thus, risk capital investment improves the chances of the portfolio company to get further funding from sources like banks,

for example, due to the strengthened liquidity added by the risk capital and the reassurance given to potential financiers by the fact that a stable co-investment fund and other risk investors are involved in the enterprise. A loan has the adverse effect of increasing the burden of debt placed on the company and making further funding costlier. It must be stressed, however, that the benefits described here are partly conditional on the characteristics of the sector and company in question – risk capital is not the optimal form of finance for all enterprises regardless of business strategy or stage of development (as explained in the previous sub-section on impact).

There are also several ways in which the specific design of the funds' operations as *pari passu* public-private co-investments more generally bring added value that is different from risk capital. Firstly, because the public co-investment funds have no formal profit requirement, they are more willing to invest in early-stage companies for which the growth prospects are naturally much more uncertain than for established firms. As already mentioned in the sub-section on impact, the public investment funds thereby also have a better starting point for spreading investments across sectors even if the expected rate of return for some of these would be lower than for others, while private investors operating without a public co-financing component naturally would centre all their attention on the narrow range of sectors in which the expected rate of return tends to be the highest and in which Mellersta Norrland hosts relatively few enterprises. Thus, the engagement of the public co-investment funds adds value to the private risk capital supply by extending its reach to riskier early-stage investment opportunities, on the one hand, and to a more diverse range of sectors, on the other.

Secondly, the collaborative operation of public-private co-investors provides added value compared to either of the parties investing alone because of the symbiotic combination of the experience and benefits of the different stakeholders. The private, local venture capital firms and investors have extensive insight and understanding of the region and its economic activities as well as personal networks with key stakeholders at the regional level. The public co-investment fund has a nationwide network and expertise in structural matters relating to risk finance and equity investments, but at the same time they are regionally oriented, and their investment plans – not beyond the reach or financial capacity of the local investors – means that the two are able to collaborate. Pooling these sets of competences enhances the operating-prospects of both private and public risk capital. Moreover, the attractiveness and trustworthiness of risk capital in the eyes of beneficiaries may increase by the involvement, alongside the private, return-oriented investors, of the public funds whose only economic objectives are for investment returns to cover administrative costs and for additional profits to revolve in the regional economy in the form of new investments.

Finally, channelling public funding through co-investment funds has the added value of enhancing and developing the regional risk finance ecosystem, thus providing opportunities for self-enforcing regional growth beyond the monetary and temporal scope of the public intervention. As outlined in the sub-section on impact, interviewees recount various ways in

which the engagement of the public funds has matured the formerly very underdeveloped risk capital ecosystem in Mellersta Norrland, transferring knowledge and competence to local investors and other stakeholders and encouraging new entrants to the private risk capital supply. These impacts have long-lasting effects in the regional economy that would not have been equally strong if the public funding would have been channelled to other instruments than risk finance based on equal participation of public and private investors.

2.3 Territorial dimensions of the Financial Instrument

This sub-section discusses the territorial reach and spread of the co-investment funds in Mellersta Norrland. As the regional economy and population is relatively sparse, their *ex-ante* expectation when setting up the funds was that critical-mass formation would present a considerable challenge. Based on the research and interviews for this case study, the geographical sparsity seems indeed to be a persistent feature of risk finance activity in Mellersta Norrland. That being said, this has not significantly inhibited the operation of the funds.

The territorial spread of the co-investment activities in Mellersta Norrland has followed the patterns of intra-regional divergence in economic agglomeration and start-up activity. The focus of investments, measured both in the number of beneficiaries and in the volume of the invested capital, is centred in the main urban areas (for example Sundsvall and Östersund) more than in rural municipalities, and also along the Western Baltic coast more than in sparsely-populated inland areas. A particular territorial feature highlighted by interviewed co-investment fund managers is the supply of private co-investors: in some cases there may be promising entrepreneurial activity with high growth potential but few private co-investors available in the respective part of the programme area, which, due to the *pari passu* operating requirement of the co-investment funds, means that some investment opportunities may be lost.

That being said, the inhibiting effect of the intraregional disparities should not be exaggerated. Out of the two funds active in Mellersta Norrland, the one focusing its investments on startups and more early-stage enterprises has invested in enterprises from 13 out of the 15 municipalities in its programme area, and the other, focusing more on funding growth-stage enterprises, has also been engaged very widely across the region. It appears that the variation in demand for risk capital – the formation of local-level critical mass to create new startups – is the more decisive territorial driver of co-investment activities, while the supply-side territorial constraints by the funds to provide investments is not an insurmountable challenge. Part of the regional variation in demand can, for example, be explained by the variation in interest and need for risk capital between different sectors: despite the difficulties in critical-mass formation and the long geographical distances, co-investment funds and

private investors seem to increasingly find their way to the those places where new businesses in ICT and other risk-capital favouring sectors are located.

The way in which the territorial challenges are overcome seems to depend crucially on extensive personal and professional networks among local authorities, investors, and entrepreneurs in Mellersta Norrland. The challenges with reaching a critical mass in small communities are outweighed by the benefit of naturally formed social networks spanning across sectors and between towns and localities in the entire region. This underlines the importance of the co-investment funds to be physically present in the different areas of the region, and the Mellersta Norrland funds have succeeded in this quite well by hosting different kinds of networking events and raising awareness among industry networks about their presence in the region. Private co-financers, for example Startkapital i Norr AB described in the flagship cases in the annex, have played an important role in overcoming territorial challenges by creating pan-regional consortia and collaborations between private investors, thus tackling the critical-mass challenge by 'pooling' both the supply of and demand for risk finance capital from the entire region.

In conclusion, while geographical distance and sparsity does continue to be a specific challenge in Mellersta Norrland, this has not prevented local stakeholders from finding ways to nonetheless operate successfully in promoting entrepreneurship and risk capital supply in the region.

2.4 Governance dimensions of the Financial Instrument

This sub-section discusses how the governance structure of the co-investment funds affects their operation in Mellersta Norrland. Both existing evaluation reports of the co-investment funds and the interviews conducted for this case study testify that finding the right balance between the main objectives of the FI intervention has caused confusion. As described by the intervention logics for the programme, the public funds, on the one hand, should work towards the objective of company growth and new job creation, but on the other hand, they should also aim at more long-term regional growth and on enhancing the establishment of a lasting private venture capital presence.

While admitting that this two-part objective has prompted questions about how the two ambitions should be prioritised, both co-investment funds in Mellersta Norrland emphasise that this has not caused hindrance to their day-to-day operation or investment decisions. The assessment of which companies to invest in is made on a purely economic basis and without considering regional policy implications or external factors, in the same way that private venture capital investors operate. The dimension of long-term regional stability and growth, in turn, is understood by the managers of the public funds to already be inherent in the market-complementing intervention itself: as described above, the public funds make market-based decisions but are then able to invest in riskier enterprises and a wide range of sectors, which

serves as an incentive for private investors to become more engaged in opportunities they would otherwise overlook or be unable to invest in. To that end, the structure of the public funds – in addition to the educative dimension of the public funds in spreading their competence, raising awareness, and enhancing networking between stakeholders in the region – covers the long-term regional-level objective so that there need not be any conflicting objectives confusing the actual investment processes. The returns on investments were, moreover, all reinvested in the region until recently, thus promoting both short-term growth and the long-term stability objective at the same time.

In contrast, the interviewees also highlight some ways in which the structure of the public risk capital funds may become a hurdle for operating in the private market. For example, the operating mandate of the public funds prohibits them from buying existing shares, which has proved to be a limitation in a few cases where the co-investment funds have been offered to invest in equity in conjunction with buying up shares from previous owners. From the perspective of beneficiaries it may thus be viewed as unreliable that the public funds do not always operate on a purely market-based logic.

The interviews conducted also revealed how the governance structure and planning of future co-investment activities in sparsely populated regions may facilitate their operation by accounting more specifically for the regional context. For example, as described in the earlier sub-section, the funds entered an underdeveloped risk capital ecosystem and an unanticipated amount of resources had therefore to be focused on building the knowledge and competence of local stakeholders and raise awareness among enterprises. This characteristic in the territorial context can hereafter be better anticipated and factored in when assessing the required operating capacity of the funds. Similarly, remote regions with a lower supply of private co-investor capital could be better serviced by public funds if limited exceptions to the *pari passu* operating requirements were allowed, so that public funds in rare cases would have the mandate to take on a larger share of an investment on their own.

2.5 Strengths, weaknesses, opportunities and threats (SWOT)

The following strengths, weaknesses, opportunities and threats to financial instruments in the Mellersta Norrland Region have been identified:

Strengths

- Experience from the previous programme period (e.g. the ecosystem and management structure have been developed).
- Substantial capacity and experience of the fund manager supports FI design and implementation.

- Even a relatively small-scaled intervention already helps to promote a positive economic cycle in the region.
- Co-investment model attracts private financing from the region. Risk sharing occurs between the public and private sectors.
- There are robust evaluations available from the previous programme period.

Weaknesses

- Difficulties in pinpointing the size and form of the regional financing gap, which puts the effectiveness of the intervention at risk.
- There are still information asymmetries among companies in the region's economy about the differences between and availability of different funding opportunities.
- Lack of initial preparedness and capacity for the educative, knowledge-sharing role in introducing risk finance to many stakeholders for the first time.
- Lack of robust exit strategies among early-stage firms, lack of tax-incentives for private actors to co-invest.
- Intraregional socioeconomic and industrial differences continue to make the finance environment more challenging.

Opportunities

- Commercialisation of university spin-offs operating in the region presents considerable regional growth opportunities.
- The co-investment model helps to leverage private capital from regional investors and business angels who may otherwise have been reluctant.
- Potential to develop a close-knit network of private investors in the region, which in the long term could even operate independently of the presence of the public co-investment fund.

Threats

- Finding enough innovative and growth-oriented companies to receive equity support in different parts of the region.
- Finding private co-financers in order to fulfil the *pari passu* criterion in different parts of the region.
- Threat to the continuity of the regional risk finance ecosystem if the public funds cease their activities (for example, for the present programme period, one of the two

active funds has been directed by its national-level parent company not to make any new investments in Mellersta Norrland but simply to oversee the investments already made).

2.6 Typical or flagship projects

As outlined in the previous sections of this case study, the risk capital funds in Mellersta Norrland strive to be consistent in their strategy of only funding activities that are specifically suitable for risk capital as a financial instrument. This may either be recently established startups seeking to grow their operations, or established firms raising capital for new investments. Moreover, while the public funds do not operate with a specific aim to invest more in some sectors than others, they have ended up investing proportionally more in enterprises outside the traditional, natural resource-based sectors, for which the availability of other sources of capital may be lower in the region.

2.7 Overall assessment

The analysis conducted for this case study concludes that the public co-investment funds in Mellersta Norrland, while falling short of achieving some of their pre-defined objectives, have nevertheless brought significant impact and value added to the regional economy and risk finance ecosystem. The funds have promoted increased awareness and understanding about a new form of capital investment in the region, and thereby both increased the demand for equity investments among a range of sectors and encouraged the supply of private risk finance by local private investors, as well as facilitated the local networking of these two groups via their extensive networks and local presence.

A long-lasting impact will, however, require both increased public resources and continuous action to support the as yet underdeveloped private finance ecosystem, both by way of co-investment funds, and via other financial instruments. A regional gap in risk capital has clearly been alleviated, but steady regional economic development cannot rely on co-financed equity investments alone, as the region is home to several important industries and sectors that do not benefit from risk capital. Moreover, continuous capital interventions will be needed in the region over time if the long-term impacts of the co-investment funds are to be realised.

References

- Growth Analysis (2016), Effects and Experiences: Final Evaluation of the Swedish Regional Co-Investment Funds 2009-2015, (Tilväxtanalys: Östersund, Sweden).
- Mason C, Michie R and Wishlade F (2012), Access to finance in Europe's disadvantaged regions: Can 'new' financial instruments fill the gap? Report for the EoRPA Regional Research Consortium 2012/6 (European Policies Research Centre: Glasgow, Scotland).
- Michie R and Wishlade F (2011), Between Scylla and Charybdis. Navigating Financial Engineering Instruments through Structural Funds and State Aid Requirements, IQ-Net Thematic Paper 29(2) (European Policies Research Centre: Glasgow, Scotland).
- Nilsson, J. E. (2012), Expert Evaluation Network Delivering Policy Analysis on the Performance of Cohesion Policy 2007-2013, Task 1: Financial Engineering – Sweden, Final Version (DG Regio: Brussels, Belgium).
- Tillväxtverket (2011), Mid-Term Evaluation of Regional Venture Capital Funds: Implementation and Lessons Learned, (Tillväxtverket: Stockholm, Sweden).
- Tillväxtverket (2016), Förändra, Förbättra och Förstärka: Att Arbeta med Regional Tillväxt I Strukturfondsprogrammet för Mellersta Norrland, (Tillväxtverket: Stockholm, Sweden).
- Tillväxtverket (2017), Räcker Pengarna? Studie Kring Kapital för Företag I Mellersta Norrland, (Tillväxtverket: Stockholm, Sweden).

List of Annexes

Annex 1: CS elaboration process

Annex 2: Flagship projects

Annex 1: CS elaboration process

The first stage of the case study process involved desk-based research examining relevant literature related to the development and implementation of the co-investment funds in Sweden, including a review of a number of implementation reports and evaluations prepared by the European Commission and national agencies responsible for FIs. The desk-based analysis focused primarily on the Mellersta Norrland region, identifying the aims and objectives of the co-investment funds in the region, the key actors involved, the processes adopted, the different types of beneficiaries, the main challenges in their development and implementation, and what impact the funds have had on regional development and growth.

Through the desk-based research, potential interviewees were identified within two main investment funds responsible for FIs in Sweden and the Mellersta Norrland region (Almi Invest and Mittkapital). The research team conducted interviews with Jörgen Larsson, CEO of Inlandsinnovation (formerly Mittkapital), and Eva Nordlander, CEO of Almi Invest in Mellersta Norrland. The interviews were unstructured and built around seven key thematic areas (see attached list of detailed questions): Impact of the financial instrument; value-added of the financial instrument; territorial and governance dimensions of the financial instrument; typical or flagship project examples; and an overall assessment of any further and/or general considerations about the success/failure and impact/value of FI not captured elsewhere.

The interviewees were asked to provide the contact details for several companies that had been the beneficiaries of co-investment funding. The research team arranged interviews with Lars Karbin, Chairman of the Board of Startkapital i Norr AB, Mattias Lööv, CEO of H1 Communication AB, and Tobias Sjölander, CEO of Loxyssoft AB. The interviews focused on discussing the main aims and objectives of the funding projects and assessing what impact the funding had on the business and added value they brought to regional growth.

There is generally a high level of reporting on the co-investment funds in Sweden. These reports provide a good overview of the amounts spent in each different region and a broad sectoral breakdown on the different types of beneficiaries; however, the reports are somewhat weaker on providing more specific detailed information on the impact of specific projects on business growth and regional development. One reason for this is that it is simply too early to assess the impact of co-investment funding on businesses and the region. Analysis in this case study is therefore predominantly based on the assessment of interviewees. While there are potential weaknesses of this qualitative method in terms of data objectivity and scope of observations covered, a combination of desk research and interviews with local stakeholders was judged by the case study team to provide the most comprehensive analysis to answer the assigned research questions. Due to the close industry-networks present in the studied region, the set of conducted interviews provided a good overview and an array of relevant dimensions and phenomena present in Mellersta Norrland. To achieve a holistic image of the operation and impact of the FIs, the different perspectives of the interviewees were referenced against each other and against desk-research findings.

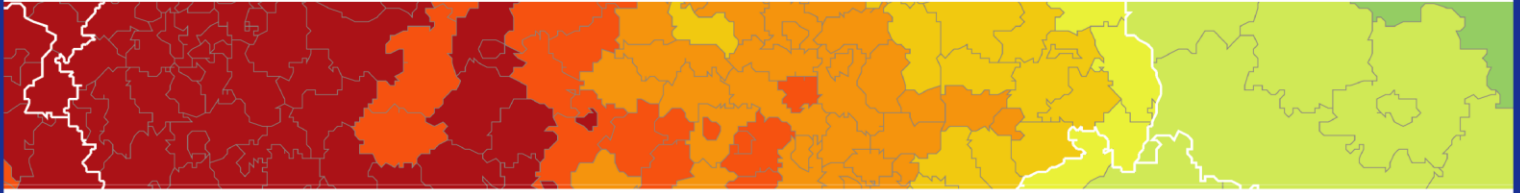
Annex 2: Flagship projects

H1 Communication AB	
Location of the project	Östersund, Mellersta Norrland
Beneficiary name and type	H1 Communication AB (Telemarketing and communications company)
Brief description of the project	The Almi Mitt co-investment fund has been actively supporting and investing in this Östersund-based firm since its emergence in 2007-2008. Investments were needed to cover the costs of expansion, such as hiring new staff. H1 Communication AB specialises in supporting other companies in their telemarketing, answering office telephone calls, etc.
Outcome of FI policy intervention	A total amount of c€2 million have been invested since the start of H1 Communication, in parallel with the private owners to whom Almi's shares were sold in 2015. In 2017 the turnover of H1 was c€10 million and the company had 173 employees.
References	Mattias Lööv, CEO.

Startkapital i Norr AB	
Location of the project	Northern Sweden
Beneficiary name and type	Startkapital i Norr AB (Consortium of private investors from different parts of Northern Sweden)
Brief description of the project	Startkapital i Norr AB was founded to balance the cap of private risk capital available in Northern Sweden, after an increasing availability of public funds inspiring a group of risk investors to collaborate. Introductory congresses were held, attendance at which was much higher than the founders initially expected: around 20 investors from all over Northern Sweden participated with SEK 200,000 each (c€20,000).
Outcome of FI policy intervention	At first, Startkapiutal i Norr had another public-sector backer, but when the mandate of the latter was changed by national-level decision-makers, Inlandsinnovation (Mittkapital) stepped in and took over this role as co-investor. To this day, the two stakeholders have a working relationship and are co-owners of some investments. Perhaps even more valuable is the symbiotic relationship the two stakeholders maintain outside the investments: the public fund can provide connections to stakeholders across Sweden, whereas the private consortium is made up of locals who know the region and its network. The public fund has largely left the administrative and advisory side of mutual portfolio companies to the private investors, and although this initially caused confusion, the mutual relationship has

	developed very well since. The two stakeholders are very important building blocks in each other's existence.
References	Lars Karbin, Chairman of the Board.

Loxysoft AB	
Location of the project	Östersund, Mellersta Norrland
Beneficiary name and type	Loxysoft AB (Telemarketing and contact centre company)
Brief description of the project	The Inlandsinnovation co-investment fund got involved in Loxysoft in 2013-2014, supporting the expansion and internationalisation of the Östersund-based firm which had developed its telemarketing solutions in Östersund since the late 1990s.
Outcome of FI policy intervention	As a result of the Sweden and Norway-based acquisitions made possible by the support of the co-investment fund, Loxysoft grew in a short period of time from 40 to 100 employees. The company is still headquartered in Östersund, but today it also has a strong presence in Stockholm, Gothenburg, Oslo and New York. Apart from financial backing, the support and engagement provided by individuals of the co-investment fund towards the board of Loxysoft is recognised to have brought valuable impact and added value in the development and operation of the company.
References	Tobias Sjölander, CEO.



ESPON 2020 – More information

ESPON EGTC

4 rue Erasme, L-1468 Luxembourg - Grand Duchy of Luxembourg

Phone: +352 20 600 280

Email: info@espon.eu

www.espon.eu, [Twitter](#), [LinkedIn](#), [YouTube](#)

The ESPON EGTC is the Single Beneficiary of the ESPON 2020 Cooperation Programme. The Single Operation within the programme is implemented by the ESPON EGTC and co-financed by the European Regional Development Fund, the EU Member States and the Partner States, Iceland, Liechtenstein, Norway and Switzerland.