



Venture Capital in Spain

MONTERREY VENTURE CAPITAL CONFERENCE 2010

Seminar of Finance Research

Why Spain?

- Spain was selected as a case study because during 2005, 2006 and 2007 the industry of Venture Capital & Private Equity reached peak levels compared to the past, making Spain a legitimate participant in Europe.
- Moreover, Mexico and Spain share a similar cultural background , so it is valuable to understand the factors that led Spain to its current level of PE/VC investment. This allows us to find alternative benchmarks for development of venture capital in Mexico.

2009 VCPE Country Attractiveness Index

2009/2010 VCPE Country Attractiveness Index (Selected Countries)			
Country	Current Ranking	Score	2004 Ranking
United States	1	100	1
United Kingdom	3	84.3	3
Spain	20	58.3	22
Mexico	49	35.8	51

Source: 2009 The Global Venture Capital and private equity country attractiveness Index. Business School University of Navarra

History of Venture Capital in Spain

- 1970's → The government launched the venture capital industry in Spain. The original idea was to establish regional entities that would finance and develop industrial activities. The first of such entities was SODIGA (in Galicia).
- 1986 → The first venture capital association in Spain was founded under the name ASCRI (Asociación Española de Capitales de Riesgo). At the same time, the Spanish market started to developed trustworthiness because of Spain's access to the European Union.
- 1997 – 2002 → The venture capital industry witnessed unprecedented growth rates, ranging between 30%-40% per year (total capital allocated, and in the number of funds participating).

History of Venture Capital in Spain

- 2005 → The Spanish government created four actions to attract new venture capital firms and propel the existing firms as never before:
 - The first action was a new law “Ley 25/2005” that loosened the tributary and legal restrictions for the companies that invested in venture capital.
 - The second action was the NEOTEC CR SOCIEDAD DE FONDOS program that became a fund for funds with an initial capital of €176 million.
 - The third initiative included the creation of the fund “I+D UNIFONDO” to exclusively finance scientific and technological start-ups from college incubators.
 - The fourth action was the creation of the state company “Nacional de Innovación, S.A.” (ENISA), which manages public funding directed to venture capital funds in the tourism sector and industrial development.

Facts

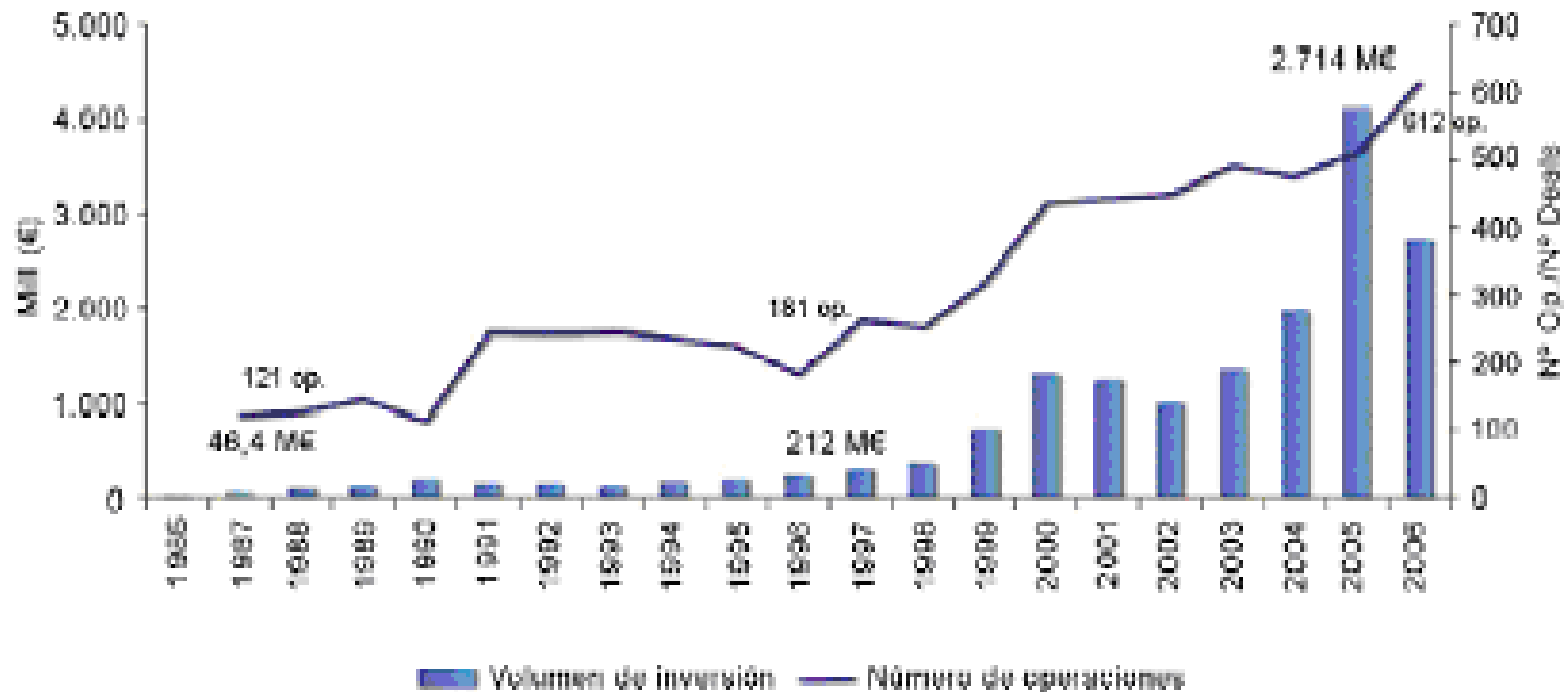
- Venture Capital Investment Entities (legal name) went from 39 entities in 2005 to 196 in 2009. Also, the number of transactions went from 475 up to 1505 during the same period. Furthermore, the value of the transactions increased from €1,966.8 million to €16,687 million.
- During 2008, 89% of the invested capital was domestic capital (in sync with the historical average of 85% since 1987), and 97% of the transactions that took place were between Spanish entities.

Facts

- Among autonomous communities, the last five years have witnessed a continuous domination by the communities of Madrid and Cataluña. Nonetheless, the level of concentration has been diluted since 2004, when Madrid housed 42.11% of the venture capital investment entities and Cataluña, 25%. In 2009 the two communities hosted only 22.5% of total investment entities.
- Spain's investments are concentrated according to the stage of development. In 2004, seed capital represented only 0.3% of venture capital investments and 60.3% of the capital went to expanding companies.

Facts

VC Volume and Number of Investments in Spain (1987- 2008)



Scope of Venture Capital Investment: by Industry

- In 2004 the biotechnology industry only accounted for 0.3% of the total VC investment. Meanwhile Telecommunication (22.8%) and Consumer goods (8.4%) dominated the industry.
- The sectors that attracted the largest amounts of venture capital in 2009 where: “Healthcare/Medicine” (25%), “Consumer goods” (23.5%), and “Energy/Natural Resources” (11.5%). However, the largest share in the number of transactions still belongs to “IT”, with 22%.
- Spain’s market has distinguished itself from other markets due to the uncommon concentration of venture capital in its consumer goods industry.

Spain's VC Industry Leaders

Market Share:

Company	Community of Origin	Start of Operation (year)	Committed capital (millions of euros)
ESPIGA CAPITAL INVERSION	Madrid	1998	48.08
SODIGA GALICIA	Santiago de Compostela	1998	47.93
VISTA DESARROLLO SA	Madrid	1999	47.84
INOVA CAPITAL	Madrid	2000	43.44

SOURCE: El capital-riesgo en España. *Boletín Económico Financiero Cajamar, suplemento n.23, Año VI, Julio 2005.*

Recovered from <http://www.fundacioncajamar.es/boletin/s23.pdf>. p.15

Industry Characteristics

- ❑ Spain's venture capital market is characterized by a large number of transactions for a relatively small amount (less than €250,000); thus the leading factor in the market is the availability of capital.
- ❑ The second most relevant factor is the time of participation (the Spanish market has been characterized by volatility, with constant entrances and exits of firms), even with the domination of local firms.
- ❑ Espiga Capital Inversion Fund, hosted in Madrid, is Spain's VC industry leader:
 - ❑ It has the largest available capital, estimated at €48,080 million.
 - ❑ It has been active in Spain's market since 1998 (only 25 other companies founded before 2000 are still in operation).

Espiga Capital Investment Fund: Keys for success

- Espiga Capital Inversión (ECI) only enters dynamic sectors of the economy, with exception of real estate and financial companies.
- The ECI management team is comprised of professionals with knowledge of selected industries and specific businesses.
- Selected partners and companies must show projected growth above their industry's mean rate.
- ECI prefers investing in family companies; especially those ready to launch new products, acquire competitors, or expand into the international arena.
- Active management from ECI includes participation on company board meetings and in business planning. Yet, the company does not like to intervene in daily operations.

Spain vs. Mexico. LAVCA Ranking

Mexico - Spain

Laws on PE/VC fund formation and operation	2 – 3*
Restrictions on institutional investors investing in PE/VC	2 – 3
Protection of intellectual property rights	2 – 3
Bankruptcy procedures/creditors' rights/partner liability	1 – 3
Capital markets development and feasibility of exits	2 – 4
Strength of the judicial system	2 – 3
Perceived corruption	1 – 3
Quality of local accounting/use of international standards	3 – 4

*Maximum score: 4

Spain has a superior performance in every variable measured by LAVCA, which points out that Spain has a better pro business environment than Mexico. Therefore, the VC industry has developed accordingly.

Concluding Remarks

- The growth of Spain's venture capital industry during the 90's was supported by the its government's effort to create a legal framework for the industry, and by the historically low interest rates in Spain's market after it entered the European Union.
- In comparison to Mexico or the US, Spain's venture capital market is characterized by the large number of transactions for a relatively small amount (less than €250,000).

Concluding Remarks

- Spain and Mexico have strong legislation regarding partner liability, property rights, bankruptcy procedures and creditors' rights. Mexican laws can be even stronger than Spanish ones; but corruption, lack of enforcement and delays from the judicial system makes Mexico score badly, creating a constraint for PE/VC business and investor confidence.
- To reach Spain's level of success, Mexico needs to improve regulations for the creation and operation of PE/VC funds in the market place. It also needs to improve the FICAP's legal structure to encourage the participation of more investors.

Concluding Remarks

- Domestic and foreign pension funds, and insurance firms represent a potential source of fundraising capital. Mexico's legislation needs to allow for the participation of these institutional investors in PE/VC.
- Capital market development is critically important to PE/VC success. The existence of feasible exit strategies is crucial for investors. It is equally important for Mexico to develop its IPO market so they can become an exit option for the VC fund.

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