

# Scale-up the innovation in Europe

*Adopted at the YEPP Council Meeting in Zagreb (23/09/2023)*

## Having regard:

- To the EIC impact report 2021, and the report of the European Parliament of the 4.11.2022 on the implementation of the European Innovation Council<sup>1</sup>
- to the EIT Annual Activity Report 2008-2021<sup>2</sup>
- to the New European Innovation Agenda of the 5.7.2022<sup>3</sup>
- to the European Commission's Annual report on competition policy 2022<sup>4</sup>

## Recognising that:

- EU has a great potential to attract innovative start-ups, and entrepreneurial talent to build a vibrant and competitive ecosystem due to high living standards and economic growth<sup>5</sup>. However, according to the Ease of Doing Business rankings published by the World Bank for the year 2020, only two European Union (EU) countries were in the top 10 (Denmark, Sweden). Moreover, according to the World Investment Report 2022 the in terms of FDI flows for year 2021 only four EU countries were listed as the top 20 host economies<sup>6</sup>.
- EU appears to be losing the global race for innovation. According to the Innovation Scoreboard 2022<sup>7</sup> that performs a holistic analysis of the various factors that affect innovation, the EU has a performance gap with Australia, Canada, South Korea and USA. Additionally, China's global lead extends to 37 out of 44 technologies that Australian Strategic Policy Institute ASPI<sup>8</sup> is now tracking, covering a range of crucial technology fields spanning defense, space, robotics, energy, the environment, biotechnology, artificial intelligence (AI), advanced materials and key quantum technology areas.
- EU has fewer billion-Euro scale-ups (unicorns) than USA and China. The EU Joint Research Center's analysis<sup>9</sup> shows the US has almost six times as many unicorns as the EU, while China has 2 times more. Whereas scale-ups are essentially start-ups with proven success and well-established in the market. These companies are in a better position to attract investment, create jobs, and contribute to the overall economic stability of a region.

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<sup>1</sup> [https://www.europarl.europa.eu/doceo/document/A-9-2022-0268\\_EN.html](https://www.europarl.europa.eu/doceo/document/A-9-2022-0268_EN.html)

<sup>2</sup> <https://eit.europa.eu/newsannual-activity-reports>

<sup>3</sup> <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52022DC0332>

<sup>4</sup> [https://competition-policy.ec.europa.eu/publications/annual-reports\\_en](https://competition-policy.ec.europa.eu/publications/annual-reports_en)

<sup>5</sup> <https://businessnamegenerator.com/the-global-startup-index/>

<sup>6</sup> [https://unctad.org/system/files/official-document/wir2022\\_en.pdf](https://unctad.org/system/files/official-document/wir2022_en.pdf)

<sup>7</sup> <https://op.europa.eu/en/publication-detail/-/publication/f0e0330d-534f-11ed-92ed-01aa75ed71a1/language-en/format-PDF/source-272941691>

<sup>8</sup> <https://www.aspi.org.au/report/critical-technology-tracker>

<sup>9</sup> <https://publications.jrc.ec.europa.eu › JRC127712>

- EU recognizing the global challenges established European Institutions like the European Institute of Innovation and Technology (EIT), the European Innovation Council (EIC) and the European Investment Bank (EIB) to foster and facilitate innovative business creation and boost. While EIT has a budget of almost EUR 3 billion and EIC-EIB dispose of more than €10 billion for the period 2021-2027 under Horizon Europe. Together they may be the biggest “venture capital” in Europe but the total amount is relatively small compared to the size of the European economy (EU GDP was € 14.5 trillion in 2021<sup>10</sup>) and the scale of the challenges facing European innovation. This limited funding makes it difficult for the EU instruments to achieve its ambitious goals and support a wide range of innovative projects and companies.

### **Acknowledging that:**

- The main EU innovation instruments (EIC, EIT, EIB) are part of a complex and fragmented innovation ecosystem in Europe that includes multiple actors, such as national innovation agencies, universities, research institutions, and private companies. This fragmentation makes it difficult for the EU instruments to coordinate and integrate its efforts with other actors in the ecosystem. Despite the systemic barriers to innovation, the main EU innovation actors are lacking a coherence and streamlined approach for their own collaboration limiting and fragmenting the impact of their complementary actions. Instead, they should strive for a unified approach, acting as a support pipeline through single processes.
- EU is mostly focused on investing/funding, centralized projects that primarily involve universities and research institutions rather than equally supporting small and medium-sized enterprises (SMEs). While universities play a crucial role in research and deep tech, SMEs and startups are key drivers of innovation and cutting-edge technology. They have the agility and entrepreneurial spirit necessary to bring research and technology to the market, creating new products, services, and jobs. Therefore, it is important to provide targeted support to SMEs and startups to harness their business potential and facilitate their innovation growth. For example, in the United States, the Small Business Innovation Research (SBIR) program provides funding to small businesses to conduct research and development on new technologies, with the aim of commercializing these technologies and creating new products and services.
- EIC and EIT funding programs have adopted a top-down approach that is not sufficiently market-driven. EIC and EIT should take a more market-oriented approach in their selection processes and funding decisions. Rather than primarily relying on business-based evaluations, they should adopt a more entrepreneurial mindset, resembling a venture capitalist (VC) approach. This would ensure that the supported initiatives are more aligned with market needs and have a higher likelihood of successful commercialization. It's important to note that striking a balance between market-driven selection processes and other considerations, such as scientific excellence or societal and environmental impact, is a complex task. The EIC and EIT programs need to carefully navigate between market-driven approaches and the broader objectives of supporting breakthrough innovation and addressing societal and economical challenges.
- The EIC and EIT bureaucratic procedures and criteria for funding applications are complex and time-consuming, which may deter many potential applicants, especially SMEs and startups,

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<sup>10</sup> [https://european-union.europa.eu/principles-countries-history/key-facts-and-figures/economy\\_en](https://european-union.europa.eu/principles-countries-history/key-facts-and-figures/economy_en)

from seeking funding. The fact that they were set up to support startups and SMEs developing deep-tech innovations; highlights that cash flows are crucial for startups and SMEs, and that long delays in receiving expected funding can bankrupt these kinds of companies. While universities and research institutions can easily adapt under these conditions as they have already secured cash flows. Therefore, the importance of these funds in being able to invest within market-compatible timeframes; deplors the cases where they failed to support the organizations in need.

- Europe does face a challenge to scale-up innovation. Traditional bank products, such as loans and credit lines, continue to be the main source of external finance for European enterprises, while alternative market-based resources such as equity play a relatively minor role. The tax system reinforces the status quo, as interest payments on debt financing are tax deductible, while costs related to external equity financing are not in most Member States. The short-term character of traditional financing and the comparative fiscal disadvantage of equity compared with debt pose significant constraints on innovation investments, especially when scaling up. Additionally, the EU lacks large venture capital (VC) funds that are willing to invest significant amounts in scale-ups compared to the US and China. The fragmented and risk-averse nature of the European VC market, with a focus on early-stage and regional markets, leads to fewer and smaller late-stage investment rounds in Europe. These factors contribute to the challenge of scaling up innovation in Europe. Moreover, EIC and EIT programs have a relatively large number of beneficiaries, resulting in the funding being spread thin and potentially diluting the impact.
- The EU has made extensive efforts over the past two decades to create the ideal market conditions for explosive growth in the digital economy, but unfortunately, none of these attempts have yielded significant results. This has led to the recurring question of how Europe can establish its own Silicon Valley. The core element of Silicon Valley's success can be summarized as a combination of physical infrastructure and a supportive regulatory environment. Silicon Valley has thrived due to the presence of renowned research universities like UC-Berkeley and Stanford, which have acted as a breeding ground for talent and innovation. Additionally, the region benefits from favorable laws and policies that have facilitated its growth. Some key regulatory factors include: Non-compete clauses and employment at will to foster a continuous flow of talent and encouraging competition, it allowed institutional investors to participate in high-risk activities (i.e. pension funds) and lower tax rates for capital gains compared to ordinary income incentivized investment in new technologies.

#### **YEPP Calls on:**

- EIC and EIT to broaden their broader KPIs and impact indicators, the programs can better capture and promote innovation that addresses societal challenges, contributes to sustainable development, and generates long-term economic value.
- EU Member States to explore options like sovereign wealth funds providing SMEs research funding, technology visas, 'friend-shoring' agreements, Research & Development grants between allies, and restructuring taxation systems to redirect private capital towards venture capital and scale-up efforts.

- The EU to continue its efforts to harmonize low tax policies among member states, particularly regarding capital gains tax rates. This would create a more level playing field and reduce discrepancies that hinder innovation and investment in EU Market.
- EIC and EIT to collaborate closely with member states and national innovation agencies to identify and support strategic areas of innovation, fostering a seamless pipeline that connects early-stage support at the national level to scaling up at the European level.
- EIC and EIT to focus on addressing market failures and supporting strategic innovative solutions and adopt an integrated approach to support SMEs.
- EIC and EIT to adopt a more market driven approach to identifying market opportunities, potential customer demand, and the commercial viability of projects by actively scouting the market for innovative ventures, to increase market responsiveness and alignment with founder needs.
- EIC and EIT to increase accountability and efficiency by setting clear performance targets, improve transparency by publishing detailed information of their activities and leverage modern technologies to streamline the process of identifying scalable start-ups (AI), promote their open data, and implement real-time monitoring.
- EIC, EIT and EIB to collaborate closely with European Blockchain Services Infrastructure is an initiative led by the European Commission to develop solutions and services that would a seamless pipeline for funding start-ups that would improve efficiency and Intellectual Property Management.
- EU Member States to continue establishing double taxation avoidance agreements with each other and other nations. These agreements serve the purpose of preventing individuals or companies from being taxed twice on the same capital gains in multiple jurisdictions.
- European Commission to analyze and explore the effects on labour markets and wages of non-compete clauses in Europe (considering duration and scope) and promote policies that follow the principle that the restrictions on employees must not be any greater than necessary to protect the employer's legitimate business interests - "protectable interests".
- EIC and EIT to provide larger amounts of funding to a smaller number of companies in order to better support the selected companies in achieving significant breakthroughs, scaling up in Europe, and making a more substantial impact on innovation and economic growth.