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The European Small Business Finance Outlook 2024

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The European Small Business Finance Outlook 2024

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Executive Summary¹

The European Small Business Finance Outlook (ESBFO) provides an overview of the main SME financing markets (Equity, Guarantees, Securitisation, Inclusive Finance) that are central to the European Investment Fund (EIF)'s mission as Europe's main public provider of financing solutions for SMEs and mid-caps. The current ESBFO publication is an update of the December 2023 edition.

Economic outlook

- Since December 2023, *the global economic outlook* has remained steady, with growth projected at 3.2% for 2024 and 2025 and inflation expected to decline to 4.3% by 2025. While advanced economies near inflation targets, developing markets face challenges from financial volatility.
- *The EU's economic outlook* remains uncertain, with geopolitical tensions and energy security vulnerabilities posing significant risks. GDP growth is projected at 0.9% in 2024, rising to 1.8% by 2026, as inflation declines steadily from 6.4% in 2023 to 2.0% in 2026.
- The labour market remains strong, with unemployment at a new record low of 5.9% in October 2024. However, employment growth is slowing, and productivity gains, though improving, are constrained by weak innovation and business dynamism.

SME finance environment

- The EIF SME Access to Finance Index (ESAF) highlights significant disparities in SME financing conditions across EU Member States. Finland, Germany, and Sweden lead due to strong equity markets, while Portugal, Greece, and Czechia face the least favourable conditions. High borrowing costs and inflation continue to challenge debt and equity financing.
- Overall, the latest wave of the ECB's SAFE survey reveals a mixed picture of the Euro area SME financing landscape. While structural issues persist, with one in four SMEs continuing to report significant financing challenges, there are signs of recovery in some areas, particularly with improving economic conditions and increased willingness from public and private financiers.
- Structural challenges persist in SME financing. While 14% of SMEs use bank loans, nearly half consider them relevant but inaccessible. Equity financing faces even greater hurdles: although 12% of SMEs see it as a relevant funding source, only 1% actually acquire it, reflecting significant barriers to its use.

¹ This paper benefited from comments and inputs of EIF colleagues, for which we are very grateful: Cristina Dumitrescu, Helmut Kraemer-Eis, Ewa Kolodziej, Jesper Skoglund and Wouter Torfs. We would also like to thank colleagues from AECM, AFME, ECB, EMN, GEM and the Invest Europe research team for their support. All errors are of the authors.

Private equity

- Since 2022, PE/VC markets have been hit by the combined effects of the Russian war of aggression against Ukraine, the subsequent geopolitical disruptions and in particular the difficult macroeconomic environment, which continued into 2023. Following the start of the monetary tightening cycle (with the ECB raising its key interest rates in 2022 and 2023 for the first time since more than a decade), financial conditions became less favourable and the fundraising and exit environment became very challenging. In addition, market corrections set in after a long period of continuous record activity levels. In this market environment, experienced fund managers were still able to attract investments into their funds in 2022, but an overall fundraising decline was observed in 2023.
- During the full year of 2023, the PE investments in portfolio companies based in Europe dropped by 18% to EUR 96.3bn. Investment declined in the buyout segment (–26% to EUR 62.6bn). Considerable decreases were also recorded for growth and turnaround/rescue capital segments. VC investments, which are of particular importance for the financing of young innovative companies with high growth potential, dropped by 26% to EUR 12.9bn.
- Total amounts raised by PE funds in Europe decreased by 32% to a level of EUR 132.9bn in 2023. At the same time, VC fundraising decreased by 42% to EUR 14.2bn. In 2023 and during the various European PE/VC market crises of the past 15 years, the European ecosystem benefitted substantially from market-stabilising public activity. In 2023, the share of government agencies' contributions to VC funds rose to a record level of 37%.
- In 2023, the PE exit market weakened further. The considerable decrease in the total PE divestment amount (–15% to EUR 30.6bn) was mainly due to substantially lower activity in the growth capital (–35% to EUR 5.3bn) segment of the market, but also divestments in the buyout (–8% to EUR 22.4bn) and venture (–16% to EUR 2.4bn) capital segments decreased.
- *EIF Equity Survey* results indicate a still difficult fundraising and exit environment in the first half-year of 2024. *EIF VC Survey* respondents reported important challenges for their investees in 2024, particularly with regard to securing equity financing. At the fund level, alongside recurring challenges, respondents reported a very difficult exit environment and severe fundraising issues. Expectations for the coming months have become more optimistic.
- The difficult macroeconomic environment and important structural weaknesses continue to weigh on the access to funding in the European PE market and, in particular, the VC and growth market segments. This indicates the need for continuous analysis of the market needs and for a strong policy response in support of the European PE/VC markets and its final beneficiaries, the European enterprises.

SME guarantees

- In light of the negative macroeconomic and geopolitical developments in recent years, even though new dedicated programmes were set up to support SMEs under strain, these

interventions were overcompensated by the gradual phasing out of the extensive support programmes that had been rolled out in response to the Covid-19 crisis.

- As a result, based on AECM data, both the *total outstanding guarantee volume* as well as the *volume of newly-granted guarantees* continued to decrease in 2023, but remain well above their pre-pandemic levels.
- The *ratio of new to outstanding guarantees* now stands at an exceptionally low level by historical standards.
- The decrease in the *number of outstanding guarantees* is much less pronounced than the decrease in volumes.
- The *total number of supported SMEs* as well as the *average size of outstanding guarantees* in portfolio also continued their descent from the peak observed in 2020.
- The increase in GDP as European economies gradually recover, on the one hand, and the significant decrease in total outstanding as well as new guarantee volumes, on the other, means that the *relative importance of guarantees* (both new and outstanding) over GDP has decreased further, and it is now much closer to its pre-pandemic level.

SME securitisation

- The European SME securitisation (SMESec) market remains underdeveloped, with subdued activity, particularly in true sale transactions. SMESec issuance remained particularly weak throughout 2023 and into 2024 with no SME securitisation activity during the first three quarters of 2023, with only a modest EUR 4bn recorded in Q4. This level of issuance is far below historical trends. However, synthetic SMESec transactions, often unrated and bilateral, are rising as alternative financing tools, reflecting a shift in market dynamics.
- Economic crises and rising default rates have stressed SMEs and SMESec portfolios, but structural protections and regulatory reforms, including the EU Green Bond Standard and Capital Markets Union (CMU) initiative, aim to revive the market and align it with green and digital transition goals.
- Regulatory obstacles, such as high capital charges and extensive compliance requirements, hinder market growth. Proposed solutions include balanced regulatory adjustments and the creation of a European securitisation platform to boost participation and liquidity.

Inclusive Finance

- The latest market survey data show that, by the end of 2022, the gross microloan portfolio reported by 156 microfinance institutions (MFIs) had grown to EUR 5.3 billion, serving approximately 1.3 million active borrowers.
- European MFIs are aligning with broader green and digital transitions. While 55% of MFIs offer green microloans, many face challenges such as client awareness and adapting financial products. Digitalisation, a key focus for 74% of MFIs, aims to enhance

operational efficiency and client satisfaction, but requires substantial investment and technical expertise.

- To expand outreach, MFIs require borrowed funds (often exceeding EUR 10 million) and smaller equity investments (EUR 1-5 million), along with grants and technical assistance. These resources are critical for addressing challenges in green and digital transitions and for providing financial and non-financial services to vulnerable groups.

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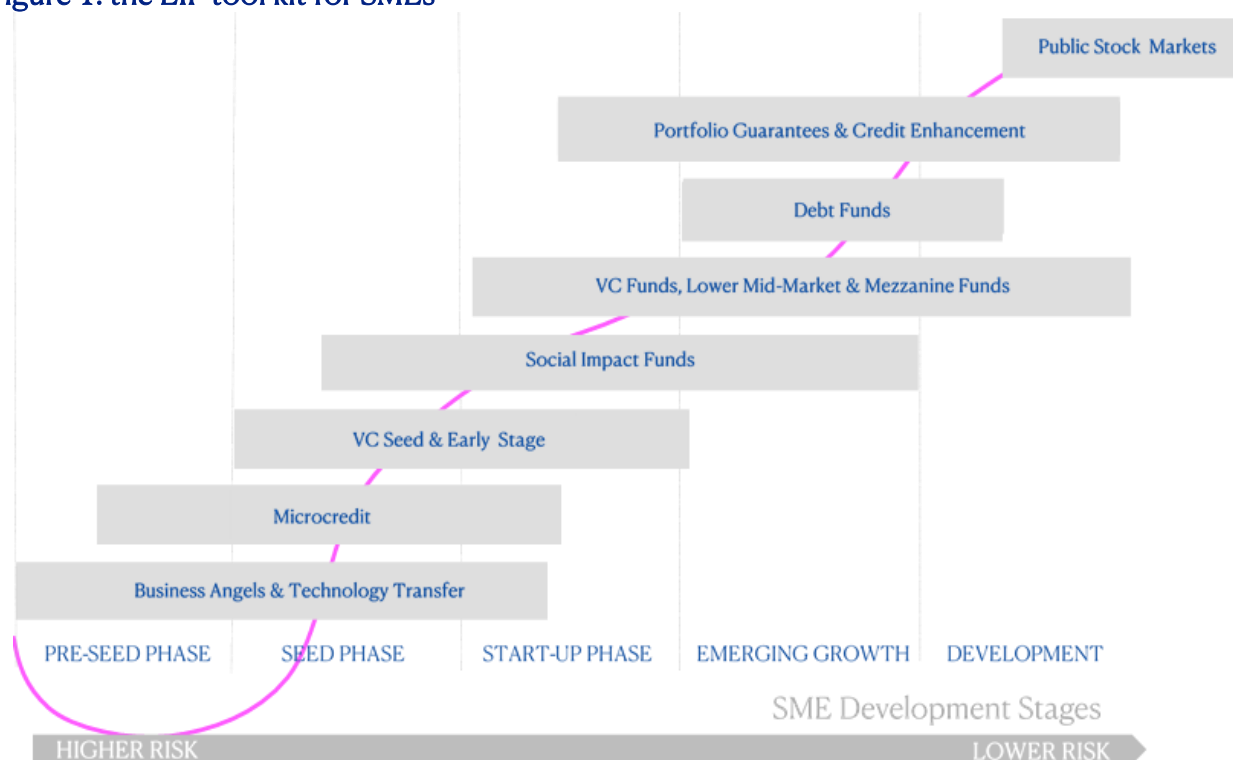
1 | Introduction

1.1 | The European Investment Fund

This European Small Business Finance Outlook (ESBFO) provides an overview of the main SME financing markets (Equity Investments, Guarantees, Securitisation and Inclusive finance) that are central to the European Investment Fund (EIF)'s mission.

The EIF is the European Investment Bank (EIB) Group's specialist provider of risk financing for entrepreneurship and innovation across Europe. It focuses on the whole range of small and medium-sized enterprises (SMEs), starting from the pre-seed, seed-, and start-up-phase (technology transfer, business angel financing, microfinance and early stage VC) up to the growth and development stage (formal VC funds, mezzanine funds, debt funds, and portfolio guarantees/credit enhancement, Figure 1). It delivers the full spectrum of financing solutions (equity instruments, guarantee and credit enhancement instruments, as well as microfinance) through financial intermediaries.

Figure 1: the EIF tool kit for SMEs



By supporting entrepreneurship throughout Europe, the EIF contributes to the European Union's (EU) thematic priorities, by promoting innovation, fostering inclusive growth, enhancing SME digitalisation and helping Europe to achieve the environmental targets of the EU Green Deal.²

1.2 | SMEs in Europe

SMEs,³ the primary target group of EIF's activities, are firms that employ fewer than 250 workers and have an annual turnover below EUR 50m or a balance sheet total below EUR 43m (Table 1).

Table 1: EU definition of SMEs*

	Employees	Turnover	Balance sheet total
Micro	<10	≤ EUR 2m	≤ EUR 2m
Small	<50	≤ EUR 10m	≤ EUR 10m
Medium	<250	≤ EUR 50m	≤ EUR 43m

*Within the category of non-SMEs, it is possible to distinguish between mid-caps and large corporates, the former being defined as enterprises that employ no more than 2,999 employees, with an additional distinction of small mid-caps, employing no more than 500 employees.

Source: European Commission (2024a)

Accounting for 99.8% of all non-financial enterprises in Europe, SMEs contribute significantly to European job creation and economic growth (Figure 2, panel b).⁴ In 2023, 26 million European SMEs employed around 89 million workers (65.3% of total employment) and generated 53.3% of European value added (EUR 4,878bn). SMEs' employment and value-added shares had been declining since 2010, with a notable decrease in their relative contribution to EU value added by over a percentage point since 2019. However, recent data from 2023 indicates a positive shift, with SMEs' value-added share on its way to recovery, showing an increase compared to previous years.

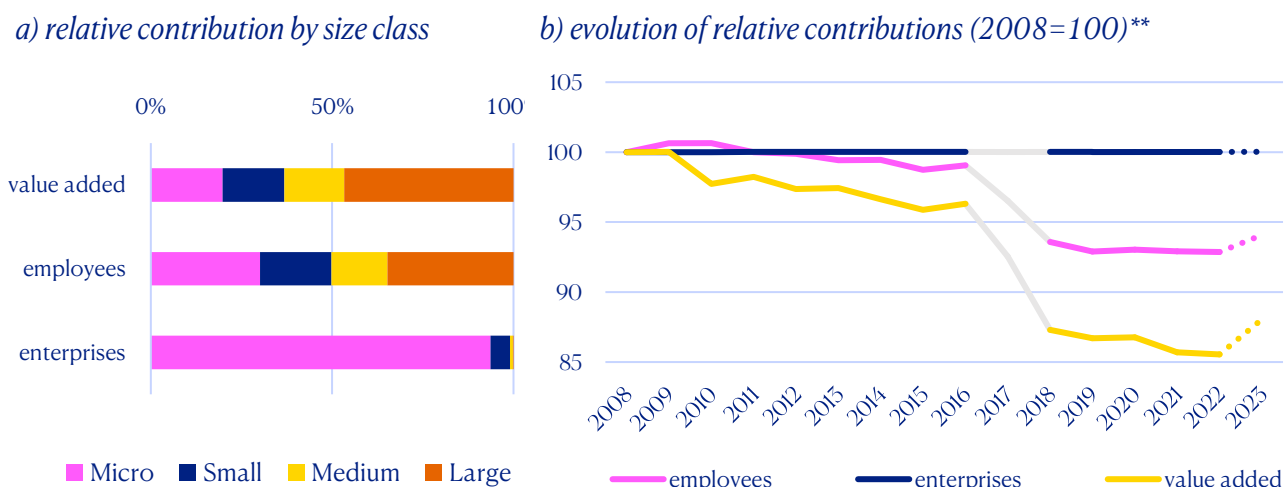
The relative importance of SMEs in national production and employment varies substantially between EU Member States. For example, Greek and Cypriot SMEs, employing more than 80% of the total workforce, contribute significantly more to aggregate employment than French SMEs, which only employ about half of the French workforce. Differences in the relative contribution of SMEs to national economies can reflect differences in national sectoral structures, as firm-size distribution differs widely across sectors. For service sectors, SMEs are important job creators, with employment shares well above 80% in high-skilled services, the hospitality sector, construction and real estate.

² For more information on the European Investment Fund and its mission, see www.eif.org.

³ As defined by the European Commission (Commission Recommendation 2003/361/CE of 6 May 2003).

⁴ Not accounting for the stark drop in measured shares driven by a change in the definition of what constitutes a corporate entity, which was implemented throughout the EU Member States between 2017 and 2018.

Figure 2: SME employment and value added shares in the EU (2023)*



d) by sector

* Excluding financial services sectors.

** The decline of employment and value added shares during 2017 and 2018 (grey lines) is driven by a structural break in the data, caused by a gradual switch from legal to statistical units as a proxy for an enterprise. Post-2022 data are estimated values.

*** NACE section M: Professional, scientific, and technical activities.

Source: European Commission (2024a), authors' calculations

Regardless of the cross-sector and cross-country diversity in SMEs' relative importance, their sizeable contribution to value added and employment underscore the essential role they play in the EU economy. Unfortunately, due to their nature, SMEs often encounter challenges in accessing finance. Therefore, this publication aims to inform policy makers, professionals and academics on recent trends on SME external financing markets, in order to foster an informed public debate on SME financing for the benefit of European SMEs.

The remainder of this publication is structured around the financing instruments make up EIF's most important target markets. Chapter 2 | and 3 | prelude instrument-specific analyses by providing a discussion of the current economic outlook and an overview of the recent SME business environment. Chapters 4 | and 5 | and 6 | discuss recent trends on European private equity, guarantee, securitisation and Inclusive Finance markets.

2 | Economic outlook

Global outlook

Since the publication of the previous edition of the ESBFO in December 2023, the outlook of the global economy has remained steady. Global growth is expected to remain stable but subdued at 3.2% for 2024 and 2025, with inflation projected to decline to 4.3% by 2025. While advanced economies approach inflation targets faster, developing markets face persistent risks such as financial volatility, commodity price shocks, and China's economic slowdown. The global economy has shown resilience, avoiding recession despite synchronised monetary tightening, but challenges like regional conflicts, elevated food prices, extreme weather events, and geopolitical tensions persist (IMF, 2024).

European outlook

The EU's economic outlook remains highly unpredictable, with risks predominantly skewed to the downside. Geopolitical tensions, driven by Russia's ongoing war of aggression against Ukraine and the escalating conflict in the Middle East, exacerbate vulnerabilities in European energy security. The EU general government deficit is expected to decline gradually from 3.1% of GDP in 2024 to 2.9% in 2026, while the debt-to-GDP ratio is projected to rise slightly, reaching 83.4% for the EU by 2026, reflecting persistent fiscal challenges and the impact of higher interest rates. After a prolonged period of widespread stagnation, the EU economy returned to growth in the first quarter of this year. As anticipated in the spring projections, this growth continued at a modest but consistent pace through the second and third quarters, supported by easing inflationary pressures. Conditions now suggest the potential for a mild increase in domestic demand, despite the elevated uncertainty (European Commission, 2024b).

Table 2: European Commission EU Autumn 2024 forecast

(Real annual percentage change, unless otherwise stated)	Forecasts					
	2021	2022	2023	2024	2025	2026
GDP growth	6.3	3.5	0.4	0.9	1.5	1.8
Inflation	2.9	9.2	6.4	2.6	2.4	2.0
Unemployment rate (%)	7.1	6.2	6.1	6.1	5.9	5.9
Labour productivity	4.7	1.2	-0.7	0.1	0.9	1.3
Total investment	4.0	2.1	1.8	-1.6	2.1	2.8
<i>Equipment investment</i>	7.6	3.3	3.0	-2.2	2.1	2.2
<i>Construction investment</i>	5.8	0.3	0.6	-1.5	0.8	3.3
Public Investment (% of GDP)	3.4	3.3	3.5	3.7	3.8	3.8

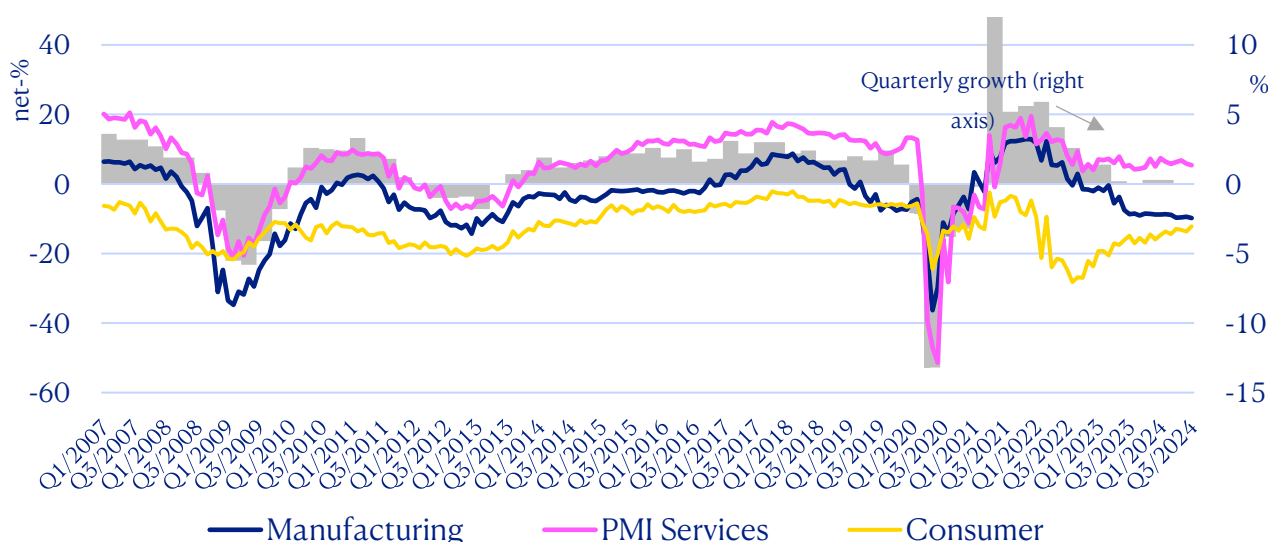
Source: European Commission (2024b)

According to the Autumn Forecast, real GDP growth in the EU is projected to reach 0.9% in 2024. Growth is expected to accelerate to 1.5% in 2025, driven by a rise in consumption and a recovery in investment following the contraction of 2024. By 2026, economic activity is forecasted to grow by 1.8%, supported by sustained demand expansion. The disinflationary trend that began at the end of 2022 continued through the summer of 2024. Despite a slight uptick in October, primarily due to energy prices, EU headline inflation is expected to drop significantly, from 6.4% in 2023 to 2.6% in 2024, and continue to decline to 2.4% in 2025 and 2.0% in 2026. The labour market showed impressive resilience, with the EU unemployment rate reaching a new record low of 5.9% in October 2024. However, employment growth is expected to slow from 0.8% in 2024 to 0.5% in 2026. After contracting in 2023, productivity is projected to stagnate in 2024, followed by a cyclical rebound in 2025 and further improvement in 2026. Despite this recovery, productivity growth is likely to remain constrained, likely due to persistent weak in innovation and business dynamism (European Commission, 2024b).

Economic sentiment indicators

In recent months, the European Commission's confidence indicators reveal a mixed picture, with sentiment trends diverging between the demand and supply side of the economy (Figure 3). Consumer confidence reached a record low during the first quarter of 2023, after which it started to increase again on account of moderating inflationary pressures. Consumer confidence remains relatively low by historic standards, matching the levels observed in the immediate aftermath of the financial crisis. Contrary to consumer confidence, sentiment among industrial and service sector companies has continued to decline, with industrial confidence dipping into negative territory from Q1/2023 onwards, consistent with recent evolution in macro-economic conditions and the ongoing geopolitical uncertainty.

Figure 3: EU-27 Economic confidence indicators and quarterly GDP growth*



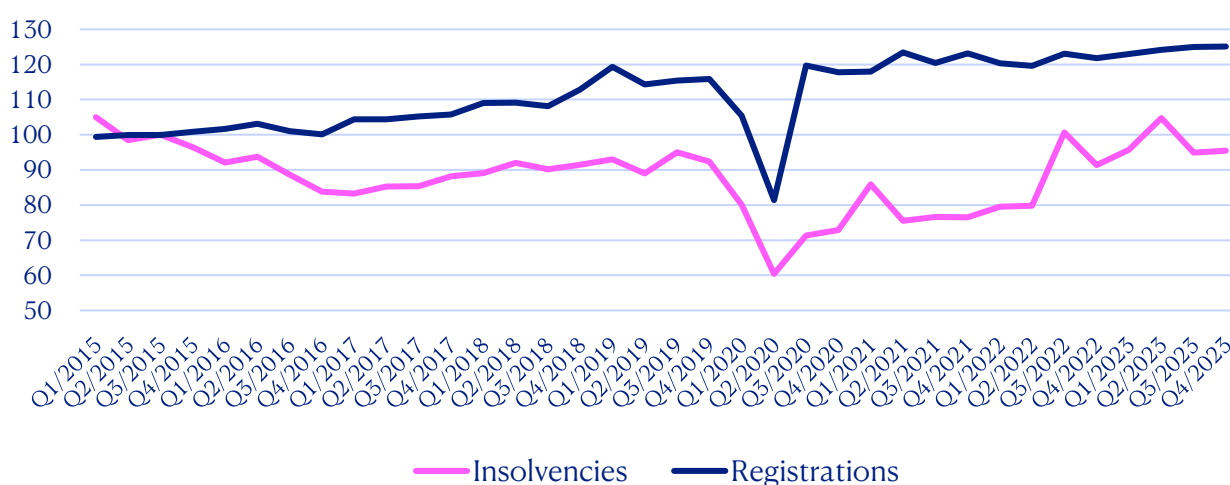
* Growth numbers refer to year-on-year growth vis-à-vis the same quarter one year earlier (European Commission, 2024b). Confidence indicators are survey-based measures constructed for each surveyed sector and are calculated as arithmetic means of answers to a selection of questions closely related to the reference variable they are supposed to track.

Insolvencies

In the early phase of the pandemic, corporate bankruptcies surprisingly declined by 35% in the first half of 2020, driven by newly implemented bankruptcy protection laws and delays in registering insolvencies during lockdowns. However, as pandemic recovery measures were gradually phased out, insolvencies began to rise from Q4 2021 onward. After seven consecutive quarters of consistent increases, insolvencies have recently started to decline, steadily nearing pre-pandemic levels (Figure 4).

Figure 4: Business dynamics in the EU-27

Evolution of business insolvencies and new business registrations (Q4/2014 = 100)



* Bankruptcies are defined as the number of legal units that have started the procedure of being declared bankrupt, by issuing a court declaration, at any time during the reference quarter Q (which is often provisional and does not always mean cessation of an activity). New registrations are defined as the number of entered legal units in the registration register at any time during the reference quarter Q, according to the respective administrative or legal procedure. The data on the absolute number of registrations of new businesses and bankruptcies on quarterly basis is provided by the national statistical institutes of the EU and EFTA Member States to Eurostat, on a voluntary basis (Eurostat, 2021). Due to the experimental nature of these data, interpretation should proceed with caution.

Source: Eurostat, authors' calculations

Furthermore, corporate demography in the EU has been negatively impacted by stagnating business creation. After having declined throughout the first half of 2022, European business registrations have increased only slightly since, consistent with the current sluggish recovery prospects of the EU economy and the negative impact of current macro-economic and geopolitical uncertainty on entrepreneurship dynamics.

Overall, the current macro-economic outlook paints a bleak picture of the European economic recovery process. Economic growth prospects remain at historically low levels and inflationary pressures appear more persistent than initially anticipated. This suggests that a near-term reversal of the ECB's monetary policy stance is unlikely, implying capital costs for European corporates in general, and SMEs in particular, are expected to remain elevated for the foreseeable future. In accordance with these dynamics, corporate investment remains depressed and has yet to recover completely from the contraction caused by the Covid crisis. This will

continue to impact European business dynamics, which has recently been characterised by a significant rise in insolvencies and stagnating business creation.

Box 1: Impact of the COVID crisis and national policy responses on EU SMEs and midcaps

1 year after: decrease in firm creations and corporate population

An EIF working paper (Brault, 2023) offered an initial assessment of the impact of the first 12 months of the COVID crisis on EU SMEs and midcaps. It matched weekly Orbis bankruptcies and firm creations to COVID-19 national fiscal policy responses drawn from an ESRB inventory. These first findings showed an initial decrease of bankruptcy rates of 22%, followed by a return to historical trends. However, firm creation rates decreased by 11%, leading to a 0.77% decrease in EU corporate population. National fiscal policies, mainly credit guarantees, seemed effective in limiting bankruptcies, but had a weaker correlation with firm creations. In contrast, the fiscal policy response in the US prioritised individual subsidies, which facilitated a rapid sectoral reallocation and boosted firm creation.

3 years after: insufficient policy support to firm creations and young firms

An LSE Capstone thesis co-supervised by EIF researchers (Alessandri et al., 2024) provided a more comprehensive analysis until end-2022. Cell calibration based on Eurostat data enhanced the representativeness of the Orbis database. Panel data regressions controlled for the intensities of the pandemic, containment measures, and amendments to bankruptcy laws. EU corporate population shrank by 0.9%, equivalent to 430,000 "missing" firms. This impact was primarily driven by a lack of firm creations, and was heterogeneous across countries and firm ages. Younger firms also experienced an increase in bankruptcy rates. In contrast, the US experienced a prolonged decrease in bankruptcies and a sustained rise in firm creations. EU national fiscal policy responses did not promote firm creations, but had a limited mitigating impact on bankruptcies. A 1% increase in policy response was associated with a 2.4% decrease in bankruptcy rates. Emergency lifeline measures, mainly loans and credit guarantees, drove this impact, but did not mitigate its heterogeneity, and benefited older more than younger firms.

These studies hence provide crucial insights into the impact of the crisis, the effectiveness of fiscal policy responses, and the lessons to be drawn. Devoting more recovery funds to promote entrepreneurship would allow to re-ignite firm creations. During the crisis, more individual subsidies to a small extent, and more confinement measures to a large extent, increased firm creation rates. The more employees were physically dissociated from their employers via lockdowns, and the more they were individually supported, the more they moved away from failing firms and created new ventures. In the medium-run after the crisis, now that "winning" sectors are better identified, targeted grants at individual and start-up level could help further support the growth of those new companies. Public equity support can also complement grants by focusing on seed capital for the youngest and most promising start-ups, and on scale-up support in the long run. Reducing information and access barriers to policy take-up would enhance response policies, especially for start-ups. The most vulnerable countries, sectors, and firms, need to be better targeted at EU-level. A balanced approach between safeguarding firms from bankruptcies and promoting firm creation would maximise business dynamism, increase employment opportunities, and promote a more sustainable economic growth. The EIF is well placed to spear-head this needed EU-level response.

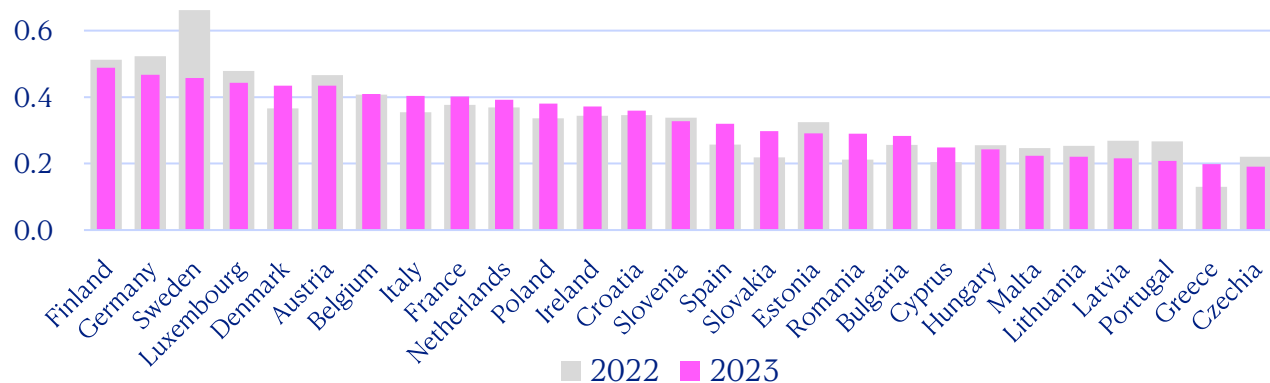
3 | SME finance environment

3.1 | The EIF SME Access to Finance Index (ESAF)

The discussion on the general SME access to finance environment is introduced by the EIF SME access to finance index (ESAF). The ESAF is a composite indicator that summarises the state of SME financing for each of the EU Member States. Box 2 provides an overview of the ESAF's components. The results of the latest update, using data for 2023, are presented in Figure 5.⁵

This update marks the 11th iteration of this analysis, covering a decade starting from 2013. Sweden, Portugal, and Germany experienced the most significant declines in their ESAF indices (see Figure 5). Despite these negative developments, Germany and Sweden remained among the top three countries, joined by Finland in the top position, thanks to the strong equity markets in these Member States (see Figure 6). Croatia, France, and Slovenia rank in the middle overall but provide the best conditions for loan markets. Conversely, Portugal and Greece had the least favourable conditions, with Czechia, for the first time, occupying the lowest position in the ranking.

Figure 5: The 2023 EIF SME Finance Index (September 2024 update)



Source: Torfs (2023, updated)

⁵ The results are based on the most recent data available as of September 2024 and pertain to the full year 2023, or the second half of 2023 for all survey-based indicators. Data on the "Median interest rate charged to SMEs for credit line or bank overdraft applications in the last 6 months" was discontinued; consequently, exclusively for this year, the 2022 values were used for the 2023 overall index and subindices. The ESAF Index is a relative indicator, which measures SME financing conditions for any given EU Member State relative to other EU countries, and its interpretation should proceed accordingly. For more details on the ESAF and its interpretation, see Gvetadze et al. (2018).

Box 2: The four ESAF subindicators

Loans:

- Percentage of SMEs using bank loans in last 6 months
- Percentage of SMEs using grants or subsidised bank loans in last 6 months
- Percentage of SMEs not applying for a bank loan because of possible rejection in last 6 months
- Interest rate for loans under EUR 250k (floating rate with IRF up to 1 year)
- Interest rate spread (under EUR 250k vs over EUR 1m for floating rate with IRF up to 1 year)

Equity:

- Venture Capital Investments / GDP
- Value of IPO market / GDP
- Percentage of SMEs using equity capital in last 6 months

Credit and Leasing:

- Percentage of SMEs using bank overdraft, credit line or credit card overdraft in last 6 months
- Percentage of SMEs not applying for the above because of fear of possible rejection in last six months
- Percentage of SMEs using leasing or hire-purchase in the last 6 months
- Median interest rate charged to SMEs for credit line or bank overdraft application in last 6 months

Macro Factors:

- Gap between actual and potential GDP
- Bank non-performing loans to total gross loans
- Percentage of SMEs feeling that there are no financing obstacles

Source: Torfs (2023)

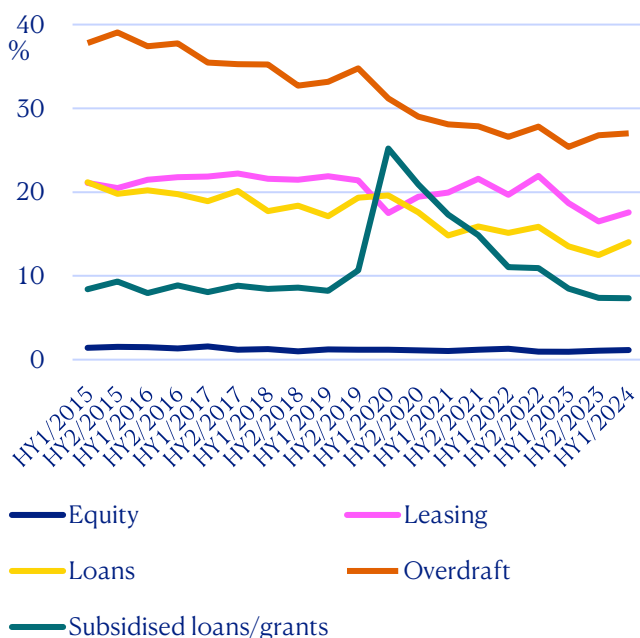
Figure 6: The 2023 EIF SME Access to Finance sub-indexes



Source: Torfs (2023), updated

Dynamics in the 2023 update of the ESAF were driven by a variety of factors. While the use of subsidised financing product dropped below pre-pandemic levels, debt and credit & leasing

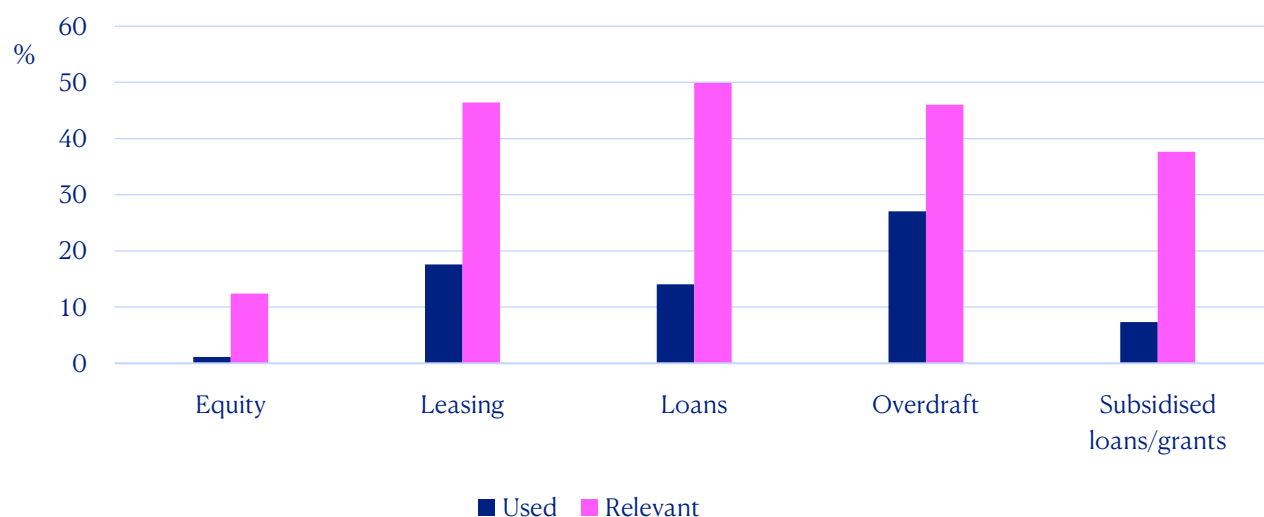
Figure 7: Share of Euro area SMEs using...



conditions within Europe diverged, as the impact of inflation on borrowing costs differed significantly between countries. High rates also created headwinds for equity markets, as fundraising conditions deteriorated and the share of SMEs reportedly using equity financing fell to an all-time low (Figure 7).

According to the ECB's SAFE survey, SMEs use less external financing instruments than their larger peers, presumably due to difficulties in accessing finance. For example, bank loans are used by 14% of SMEs. Interestingly, almost half of SMEs indicated that bank loans are relevant sources of financing, far exceeding the rate at which they use it. As for equity, 12% of SMEs consider it a relevant source of financing; however, only 1% actually acquire it, reflecting significant barriers to its use (Figure 8).

Figure 8: Relevance and use of different financing sources for SMEs, HY1/2024

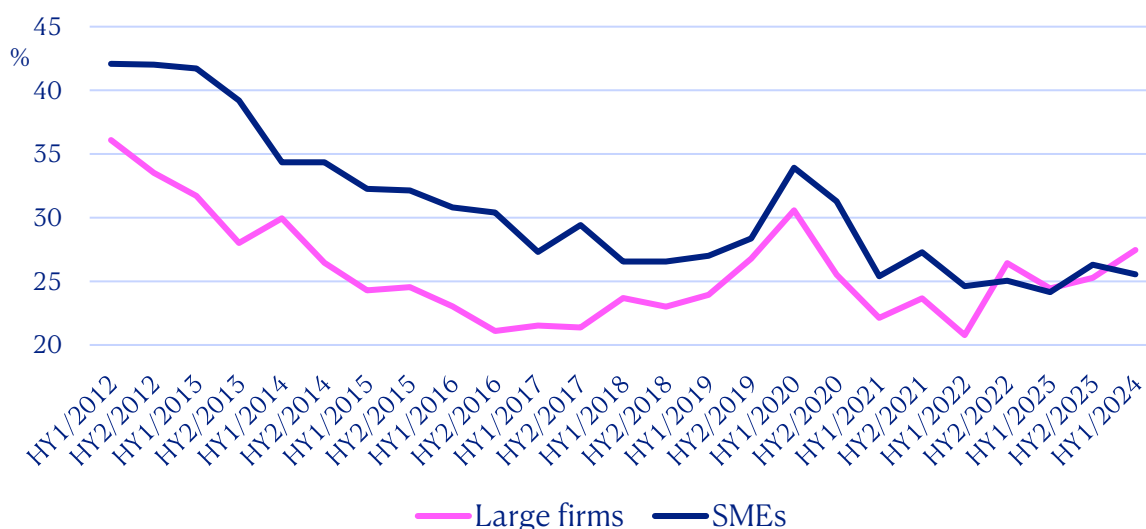


Source: ECB SAFE

3.2 | SMEs' perspective on access to finance

SME access to finance issues surged during the pandemic but stabilised afterward, highlighting persistent structural challenges. The share of SMEs reporting access to finance as a significant problem has remained relatively steady at around 25% in recent years. According to the latest data, this share rose slightly to 26% in the first semester of 2024. Despite overall stabilisation, the data underscore the ongoing need for targeted policy measures to address structural barriers to SME financing.

Figure 9: Percentage of SMEs reporting access to finance to be a highly important issue*

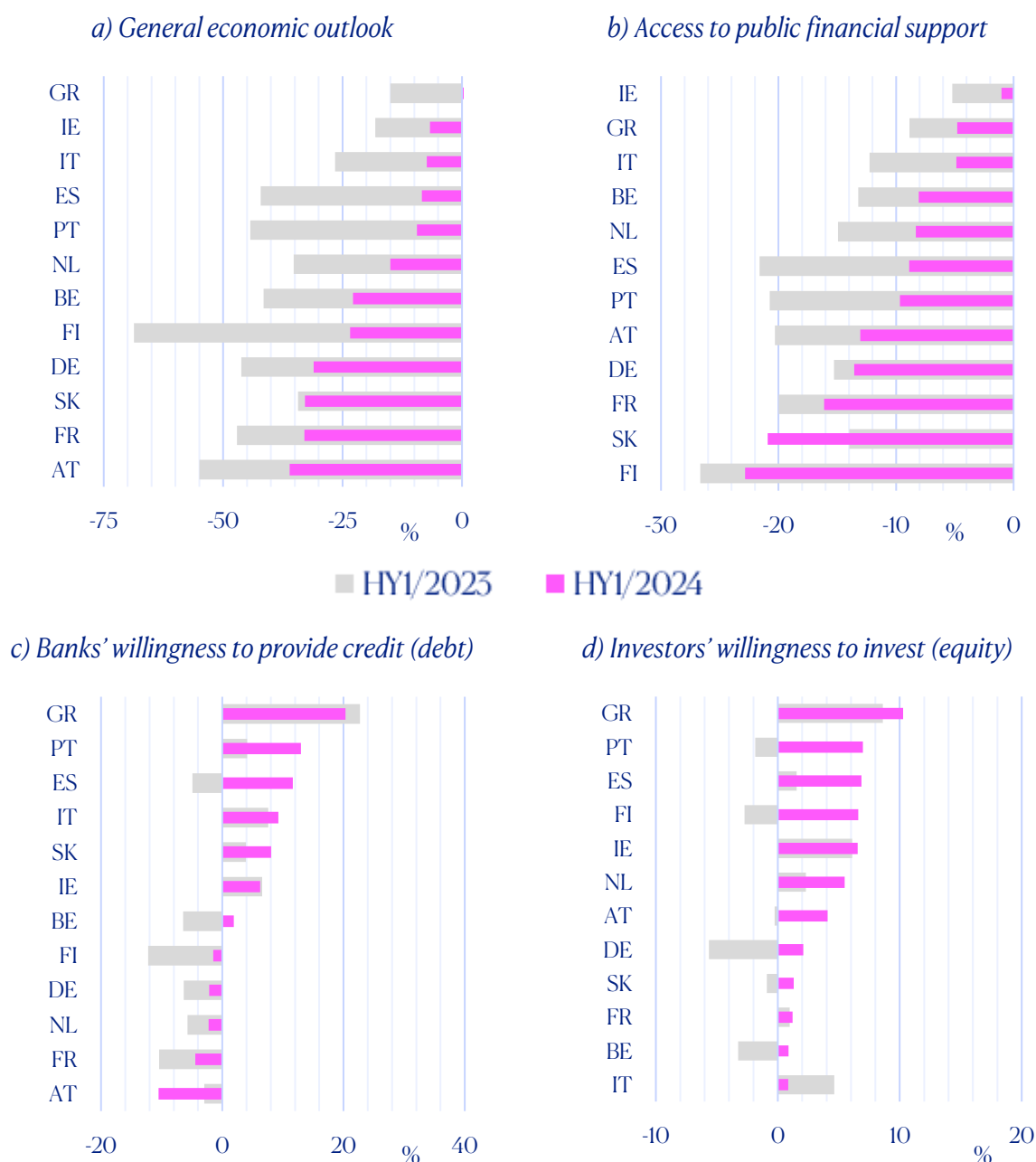


* Ranking it 7 or more on a scale up to ten, when asked how pressing of a problem access to finance was in the six preceding months.

Source: ECB SAFE (ECB, 2024), authors' calculations

Comparing contributing factors across Euro area countries (Figure 10), SMEs are univocal about the negative contribution of the general economic outlook and lack of public support, albeit to a differing extent. The reduced availability of external finance in the Netherlands and Finland was mainly caused by a deterioration in the general economic outlook and worsened access to public financial support. On the other hand, Greek and Portuguese SMEs saw improved access to finance due to banks' increased willingness to provide credit. A mixed picture emerges when considering the contributing factors related to debt and equity availability, with about half of Euro area countries viewing these factors as contributing positively to either domain.

Figure 10: Factors driving the availability of external financing by Euro area Member State*



* Net-percentages, calculated as the difference between the share of positive vs negative respondents, based on the SAFE Survey question 11: For each of the following factors, would you say that they have improved, remained unchanged or deteriorated over the past six months? The outcome is to be interpreted as a rate of change, for example, a positive percentage implies that in the aggregate, conditions related to that factor have improved during the considered period.

Source: ECB SAFE (ECB, 2024), authors' calculations

Overall, the latest ECB SAFE survey highlights the complexities of the Euro area SME financing landscape. While structural issues persist, with one in four SMEs continuing to report severe access-to-finance challenges, there are signs of recovery in some areas, especially with improving economic conditions and selective enhancements in public and private financing willingness. However, elevated interest rates and the ongoing phase-out of public support programmes add to the complexities of SME financing.

4 | Private Equity

Private equity (PE)/venture capital (VC)⁶ is an essential source for start-ups, young, and high growth companies to create value, often through innovation. External equity should not be viewed as a substitute for traditional, mainly bank-centred, SME financing instruments. Rather, it serves a specific group of SMEs and mid-caps (including start-ups), which significantly contribute to the innovativeness, productivity and development of the overall economy.

The justification for public intervention in the area of SME financing in general, and external equity financing in particular, is rooted in a number of factors, such as the presence of information asymmetries in the relationship between financier and recipient, the presence of fixed costs of investment and the existence of positive externalities originating from SMEs' innovation activities.⁷ In the PE/VC market, the long investment cycles can also deter private investors, especially in early stage financing, while public agents can be considered as more "patient" investors.

Against this background, it is one of EIF's aims to play a crucial role in establishing a sustainable VC ecosystem in Europe. We provide an overview of the European PE/VC market activity and prospects in this chapter. In the following, we mainly cover PE/VC funds (in terms of investments, fundraising, and divestments), as this is also the main focus of EIF activities. We do not provide information about PE/VC investments by business angels or corporate acquisitions outside of dedicated corporate venture programmes (i.e. corporate VC investments directly off the balance sheet), in line with the PE/VC statistics provided by Invest Europe.^{8,9} The numbers and analyses provided in this chapter cover Europe as a whole (except if stated differently). A brief overview of selected differences to EU-27 time series is presented in Box 8.

4.1 | Investment activity

Over the past 25 years, European PE activity exhibited booms and busts. The most notable peak periods were observed in 2000 and 2006, when the total amounts raised by PE funds located in Europe reached EUR 48bn and EUR 112bn, respectively, according to the statistics of Invest Europe (Figure 11; Box 3 provides more information on the Invest Europe data).

⁶ In this chapter, we follow the Invest Europe approach that includes VC as a subcategory of private equity.

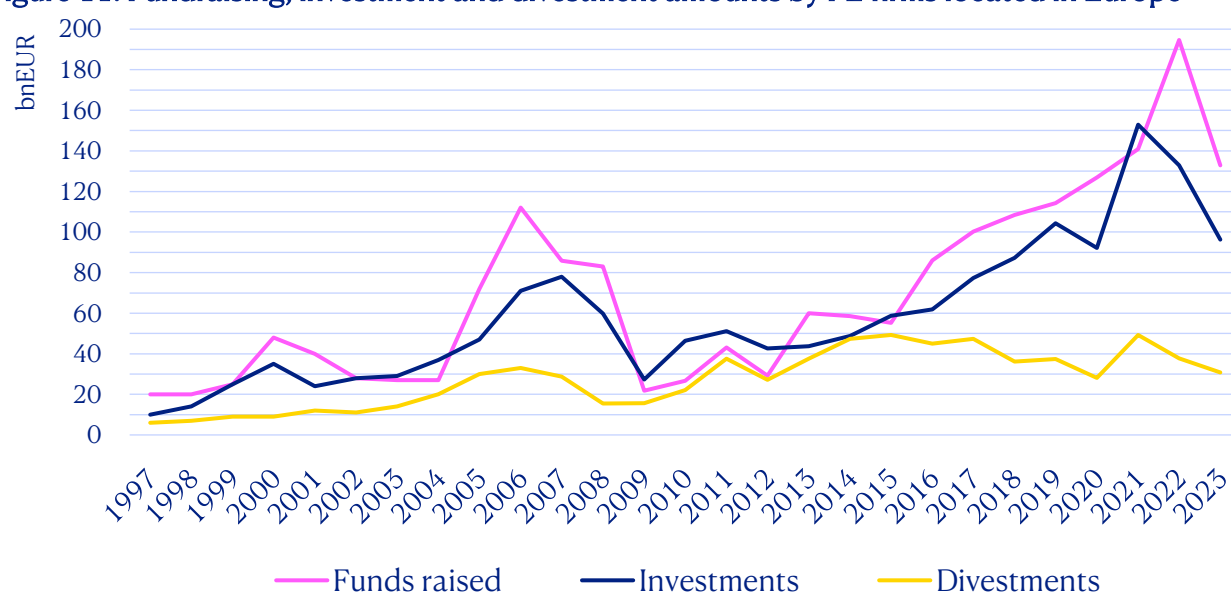
⁷ See Section 5.1.2 | for an overview of the rationale for public intervention in SME financing.

⁸ See Kraemer-Eis et al. (2023) for overviews of business angel activities and corporates.

⁹ In addition to PE/VC, private debt (or direct lending) funds have gained importance as an alternative asset class for investors and a new financing source for SMEs and mid-caps in recent years. Similar to PE, private credit funds are operated by alternative investment fund managers, originating SME lending opportunities and providing funding in the form of debt, rather than equity. See Kraemer-Eis et al. (2023) for more insight about that market in Europe.

During the same years, the overall PE investment levels reached EUR 35bn and EUR 71bn (and even increased further to EUR 78bn in 2007). However, both booms were followed by significant downturns, i.e. the “dotcom crisis” in the early noughties and the financial and economic crisis from 2007 onwards. The severe crash of the European PE activity in 2008-2009 was followed by a rebound, and fundraising and investment reached new record levels at EUR 114bn and EUR 104bn, respectively, in 2019. In the Covid-19 crisis, the market activity suffered only a temporary setback, when investments went down to EUR 92bn in 2020. The crisis was immediately followed by another record period, with new all-time highs reached for investments in 2021 (at EUR 153bn) and for fundraising in 2022 (at EUR 195bn). Total divestment amounts also increased and were at EUR 47bn in 2021.

Figure 11: Fundraising, investment and divestment amounts by PE firms located in Europe*



* In this diagram, investment and divestment data are based on the “industry approach” (or “office approach”), i.e. by PE firms located in Europe, in contrast to the “market approach”, which is based on the location of the portfolio companies.

Source: Invest Europe, authors' calculations

Box 3: Introductory information on Invest Europe data

In this chapter, numbers, diagrams and statements are largely built on statistics from Invest Europe (formerly EVCA, the European Private Equity & Venture Capital Association), and we would like to thank our colleagues from the Invest Europe research team for their support.

Invest Europe monitors direct PE investment funds that primarily focus on investments in Europe. The funds included in the statistics are PE funds making direct PE investments, mezzanine PE funds, co-investment funds and rescue/turnaround funds. Please note that Invest Europe PE statistics do not include infrastructure funds, real estate funds, private debt funds, distressed debt funds, primary funds-of-funds, secondary funds-of-funds, accelerator/incubator funds, and business angel activity.

Box 3 continued:

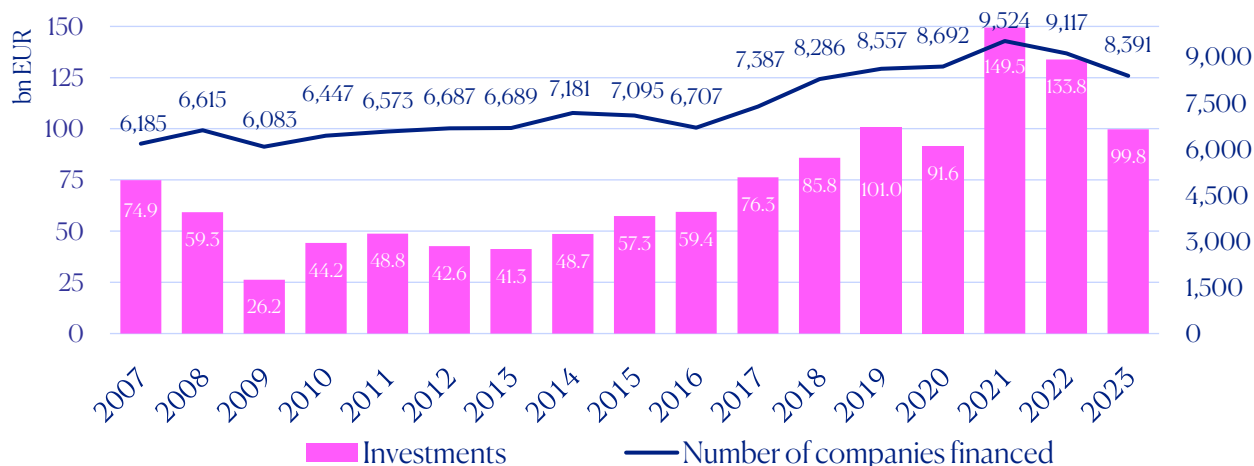
Invest Europe statistics can differ from the numbers reported by other data providers for the reason just mentioned and others, like differences in methodology, definitions and interpretations of the PE fund and investment stages and geographical definitions (e.g. of “Europe”).¹⁰

With data from more than 1,150 fund managers across Europe, the Invest Europe statistics released in May 2024 cover 90% of the EUR 1,004bn in capital under management in Europe (based on end-2022 figures). Data since 2007 was restated and complemented with additional information. To a certain extent, this resulted in revised numbers in the Invest Europe statistics and this document.

See Invest Europe (2024a) for more details.

In 2022, however, PE investments were hit by the combined effects of the Russian war of aggression against Ukraine, the subsequent geopolitical disruptions and the more difficult macroeconomic environment, which continued into 2023.¹¹ Following the start of the monetary tightening cycle (with the ECB raising its key interest rates in 2022 and 2023 for the first time since more than a decade), financial conditions became less favourable. In addition, market corrections set in after a long period of continuous record investment levels. In that year, PE funds located in Europe (statistics based on the “industry approach”; Figure 11) invested EUR 96.3bn, a decrease by 18% compared to 2022. At the same time, investments by PE funds from all over the world (including Europe) in portfolio companies based in Europe (“market approach”) dropped by 25% to EUR 99.8bn (Figure 12). The number of European companies financed decreased by 8% to 8,391.

Figure 12: PE investment in European portfolio companies*



* Investment activity by PE firms in portfolio companies based in Europe (“market approach”). All investment figures are equity value, i.e. excluding leverage.

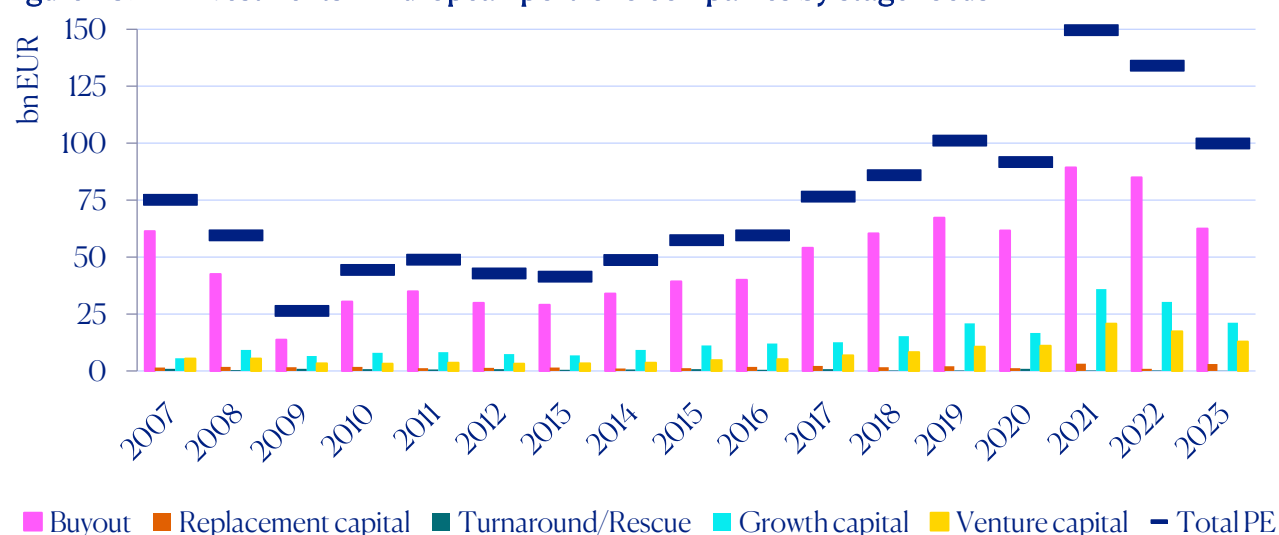
Source: Invest Europe, authors’ calculations

¹⁰ Data on the PE and VC market is scarce and often inconsistent across databases due to limited disclosure and varying collection methods. As Kaplan and Lerner (2016) note, this makes it “difficult to paint in definitive terms the level of investment activity and fund performance,” though they acknowledge that data quality has improved and is expected to continue improving.

¹¹ See Kraemer-Eis, Block, Botsari, Lang, Lorenzen and Diegel (2023) for an overview of the impact of the Russian war against Ukraine, the subsequent difficult geopolitical situation and the macroeconomic environment on PE and VC market players.

A differentiation by stage focus (Box 4 provides an overview of the Invest Europe investment stage definitions) reveals that investments declined in most parts of the PE market in 2023, i.e. the buyout (by –26% to EUR 62.6bn), growth (–30% to EUR 21.1bn) and turnaround/rescue capital segments (–42% to EUR 0.2bn), while the replacement capital segment (+214% to EUR 3.0bn) increased substantially (Figure 13).

Figure 13: PE investments in European portfolio companies by stage focus



Source: Invest Europe, authors' calculations

Box 4: Invest Europe definition of investment stages for private equity

Venture Capital

Seed: Funding provided before the investee company has started mass production/distribution with the aim to complete research, product definition or product design, also including market tests and creating prototypes. This funding will not be used to start mass production/distribution.

Start-up: Funding provided to companies, once the product or service is fully developed, to start mass production/distribution and to cover initial marketing. Companies may be in the process of being set up or may have been in business for a shorter time but have not sold their product commercially yet. The use of the capital would be mostly to cover capital expenditures and initial working capital. This stage contains also the investments reported as “Other early stage” which represents funding provided to companies that have initiated commercial manufacturing but require further funds to cover additional capital expenditures and working capital before they reach the break-even point. They will not be generating a profit yet.

Later-stage venture: Financing provided for an operating company, which may or may not be profitable. Later-stage venture tends to involve financing into companies already backed by VCs, typically in C or D rounds.

Box 4 continued:

Growth

A type of PE investment (often a minority investment) in relatively mature companies that are looking for primary capital to expand and improve operations or enter new markets to accelerate the growth of the business.

Buyout

Financing provided to acquire a company. It may use a significant amount of borrowed capital to meet the cost of acquisition. Typically involves purchasing majority or controlling stakes.

Turnaround / Rescue

Financing made available to an existing business, which has experienced financial distress, with a view to re-establish prosperity.

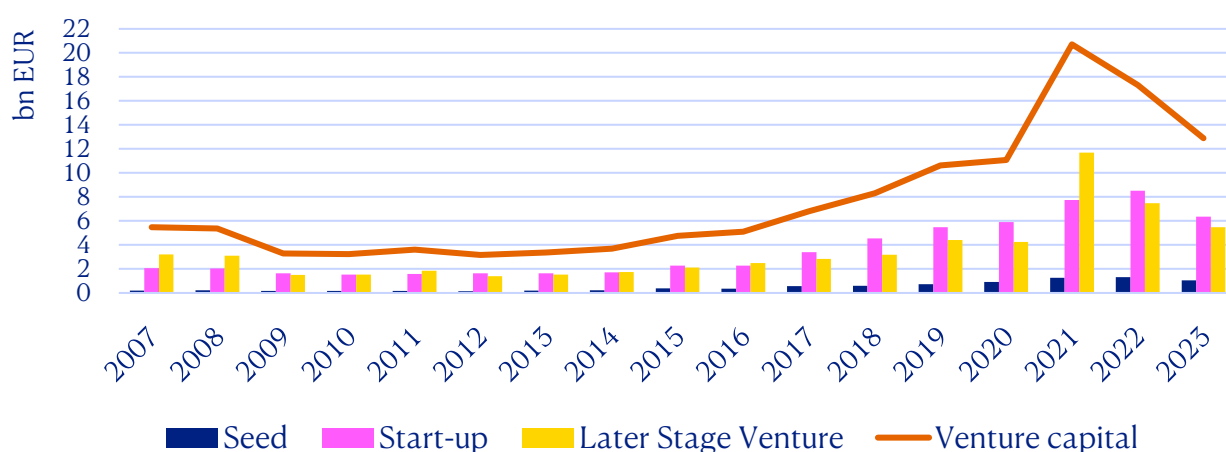
Replacement capital

Minority stake purchase from another PE investment organisation or from another shareholder or shareholders.

Source: Invest Europe (2024a)

VC investments dropped by 26% to a level of EUR 12.9bn in 2023. In terms of number of companies financed, the VC segment accounted for the majority of PE investments (4,764 out of 8,391). Within the VC market segment, the investment activity decreased in all sub-segments, i.e. for seed (–21% to EUR 1.0bn), start-up (–25% to EUR 6.4bn) and later stage venture (–27% to EUR 5.5bn), (Figure 14).

Figure 14: VC investment amounts by stage focus

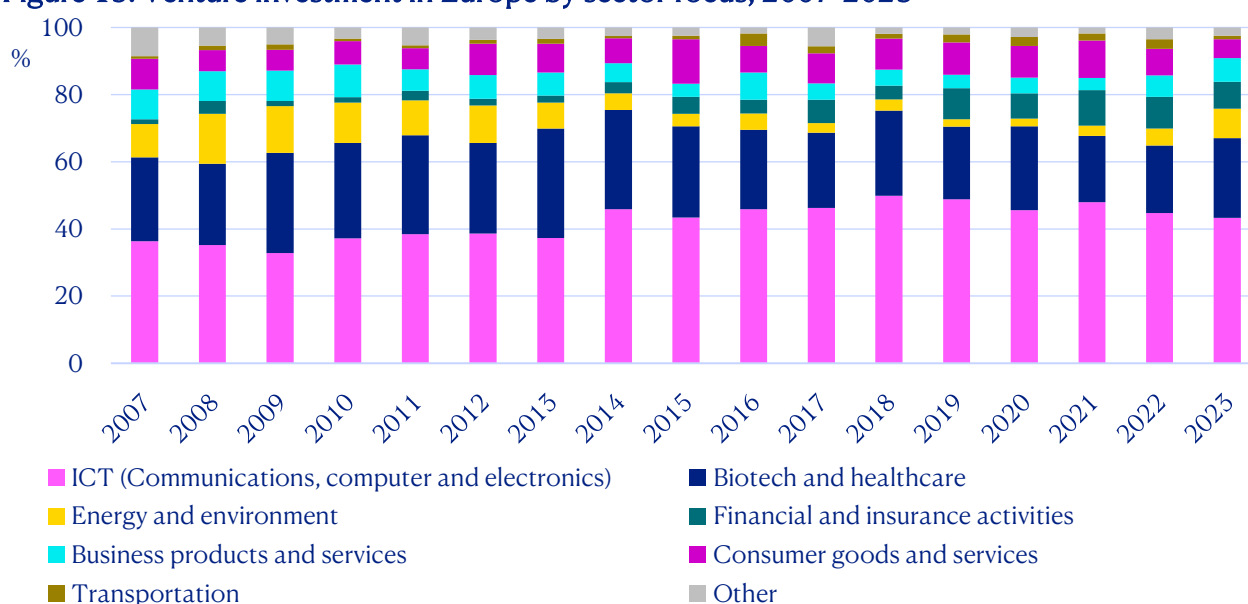


Source: Invest Europe, authors' calculations

Developments in venture investment by sector are shown in Figure 15. The relative importance of sectors has a certain stability over time: ICT (communications, computer and electronics) and biotech & healthcare have remained by far the most relevant industries for venture investment in

Europe since 2007. Despite a high level of investments in both sectors, the developments over time were different. Over the past ten years, the share of ICT in total annual VC investment activity was at 46%, on average, substantially higher than in the years before (37%, 2007-2013). At the same time, the share of biotech & healthcare venture investments decreased from 28% in 2008 to 24%. The share of investments in the energy and environment sector decreased from 15% in 2008 to 2% in 2019,¹² before increasing again over the past four years to a level of 9% in 2023. Moreover, the developments in the ICT sector had a substantial impact on structural changes in the VC market.

Figure 15: Venture investment in Europe by sector focus, 2007-2023*



* Our category "Other" contains the sectors Agriculture, Chemicals and materials, Construction, Real estate, and "Other" from the Invest Europe statistics.

Source: Invest Europe, authors' calculations

Following EIF's definition (see EIF, 2019), the PE lower mid-market (LMM) covers fund strategies targeting equity and mezzanine investments at growth and buyout stages and with a particular focus on SMEs. EIF provides its core LMM products (equity, hybrid debt-equity¹³ and private debt) as alternative sources of long-term finance to established businesses and later-stage technology companies.

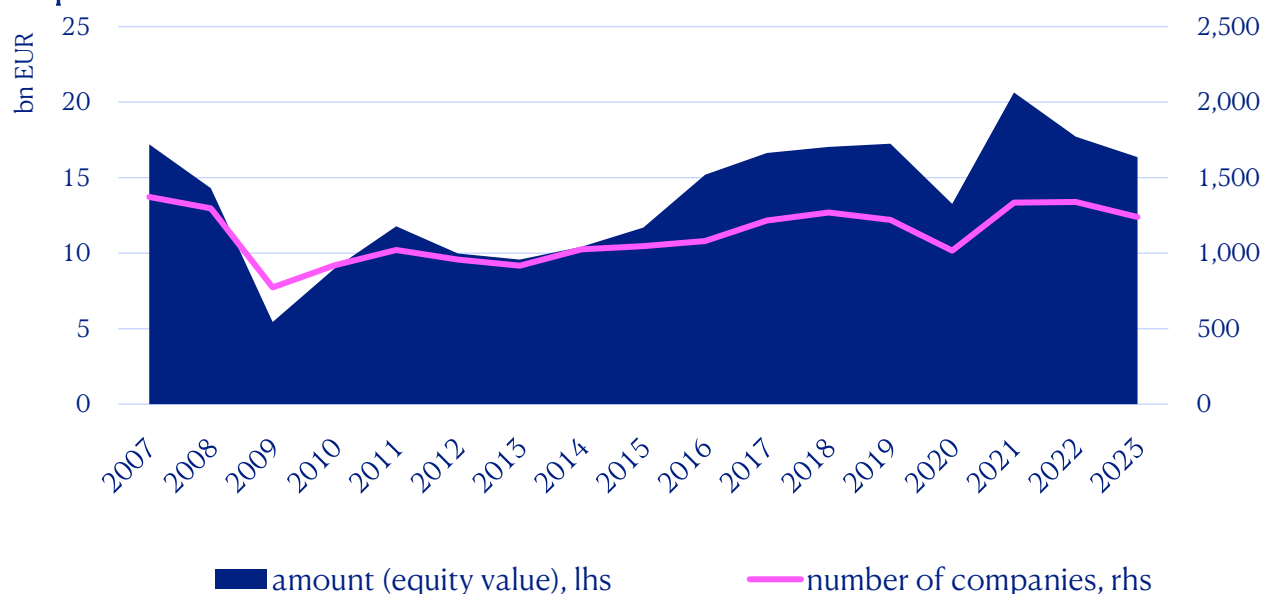
Small and lower mid-market buyout investments in European portfolio companies have been negatively impacted by the difficult macroeconomic environment. Investment amounts (equity

¹² This development might be due to a re-positioning of traditional Cleantech VCs, who have stopped investing in capital-intensive companies to focus on digital solutions for energy and environment. This strand of investments is then typically classified under ICT. Similar considerations might apply for biotech & healthcare investments.

¹³ Hybrid debt-equity/mezzanine finance is a diverse asset class in between traditional senior debt and equity instruments. According to the OECD (2014), "this form of finance has not received as much public attention as VC or specialised exchanges for SMEs, but it holds potential to respond to [...] critical problems in SME finance."

value) dropped by 8% to EUR 16.3bn in 2023 (Figure 16). At the same time, the number of companies financed fell by 7% to 1,239.

Figure 16: Small and lower mid-market buyout equity investments in European portfolio companies*



* In the Invest Europe statistics, buyout investment sizes below EUR 15m are defined as small buyout investments. Buyout investment sizes between EUR 15m and EUR 50m are classified as lower mid-market.

Source: Invest Europe, authors' calculations

4.2 | Fundraising activity

Following the worsening of financial conditions (see above), the fundraising and exit environment became very challenging. In this market environment, experienced fund managers were still able to attract investments into their funds in 2022, but an overall fundraising decline was observed in 2023.

In 2023, total funds raised by PE firms located in Europe decreased by 32%, compared to the year before, to a level of EUR 132.9bn (Figure 17). This slump was preceded, however, by the record year 2022, when PE fundraising had reached EUR 194.6bn. The fundraising decline in 2023 was driven by negative developments in all market segments, i.e. decreasing amounts raised by buyout funds (–28% to EUR 95.4bn), which represent the largest part of the PE market, growth capital funds (–22% to EUR 17.2bn), generalist funds (–37% to EUR 4.4bn) and mezzanine funds (–80% to EUR 1.9bn).¹⁴

¹⁴ Box 5 provides an overview of the Invest Europe fund stage focus definitions.

Box 5: Invest Europe's definitions of fund stage focus

Buyout fund: Funds acquiring companies by purchasing majority or controlling stakes, financing the transaction through a mix of equity and debt.

Generalist fund: Funds investing in all stages of PE.

Growth fund: Funds that make PE investments (often minority investments) in relatively mature companies that are looking for primary capital to expand and improve operations or enter new markets to accelerate the growth of the business.

Mezzanine fund: Funds using a hybrid of debt and equity financing, comprising of equity-based options (such as warrants) and lower-priority (subordinated) debt.

Venture Capital funds:

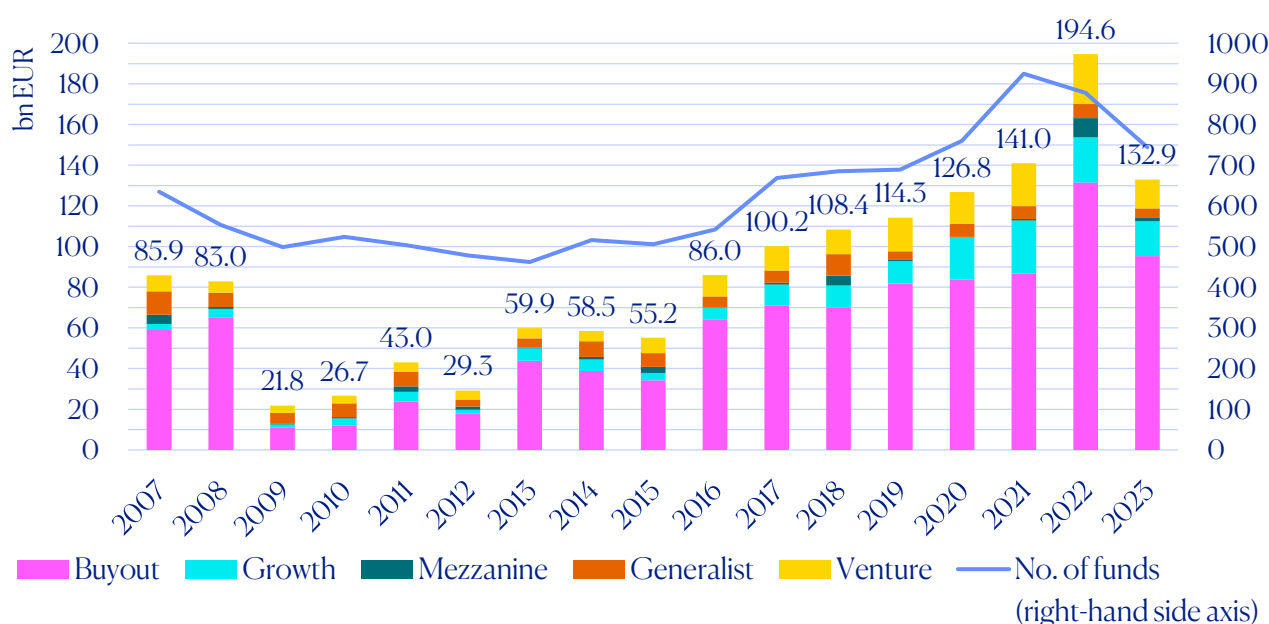
Early-stage fund: VC funds focused on investing in companies in the early stages of their lives.

Later-stage fund: VC funds providing capital for an operating company which may or may not be profitable. Typically, in C or D rounds.

Venture fund (all stages/ dual focus): VC funds focused on both early and later stage investments.

Source: Invest Europe (2024a)

Figure 17: Private equity fundraising*



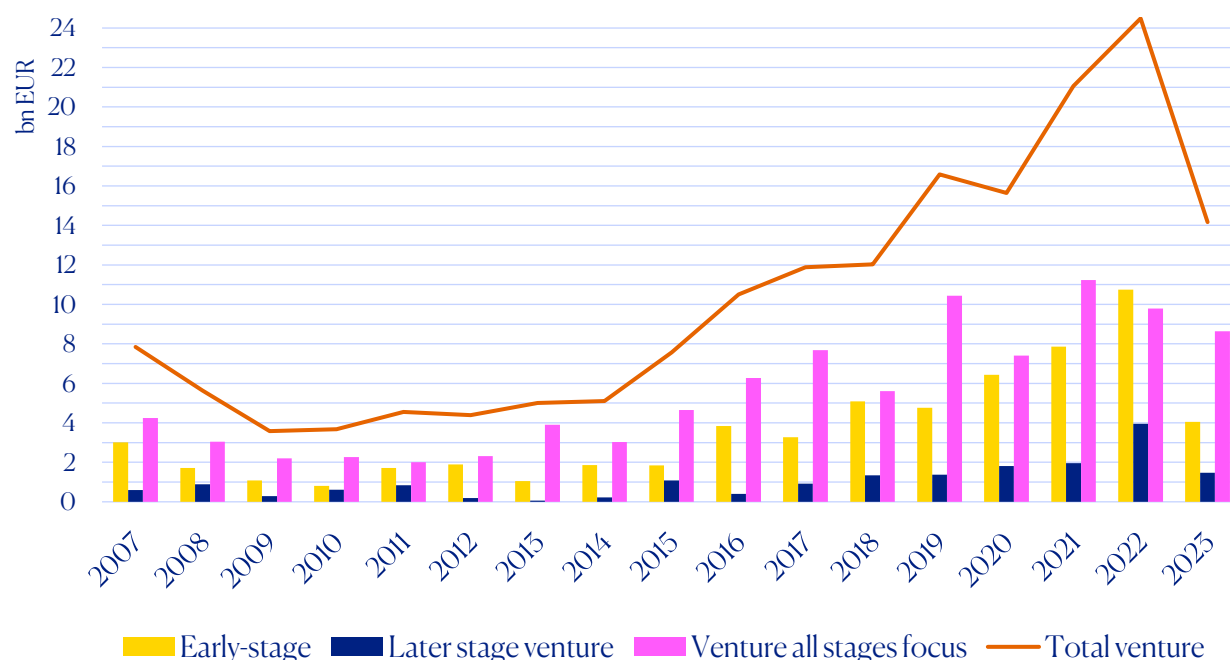
* Amount = Incremental amounts raised during period by PE funds located in Europe. No. of funds = Number of PE funds located in Europe and raising new capital during period.

Source: Invest Europe, authors' calculations

In the VC segment, fundraising decreased by 42% to EUR 14.2bn (Figure 18). Despite this strong decline, which followed on the record year 2022, the 2023 level still denotes the fifth highest

total VC fundraising amount ever reached.¹⁵ Lower fundraising amounts were recorded in all venture sub-segments, i.e. for funds with a focus on the early stage (–62% to EUR 4.0bn), funds with a focus on later-stage venture (–63% to EUR 1.5bn) and funds with a dual focus on all venture stages (slightly less pronounced, i.e. –12% to EUR 8.6bn). Fundraising linked to final closings (total venture, amounts raised since inception) was at EUR 11.8bn in 2023, which denotes a decrease by 21% compared to 2022.

Figure 18: Amounts raised by VC funds located in Europe*



* Incremental amounts raised during period.

Source: Invest Europe, authors' calculations

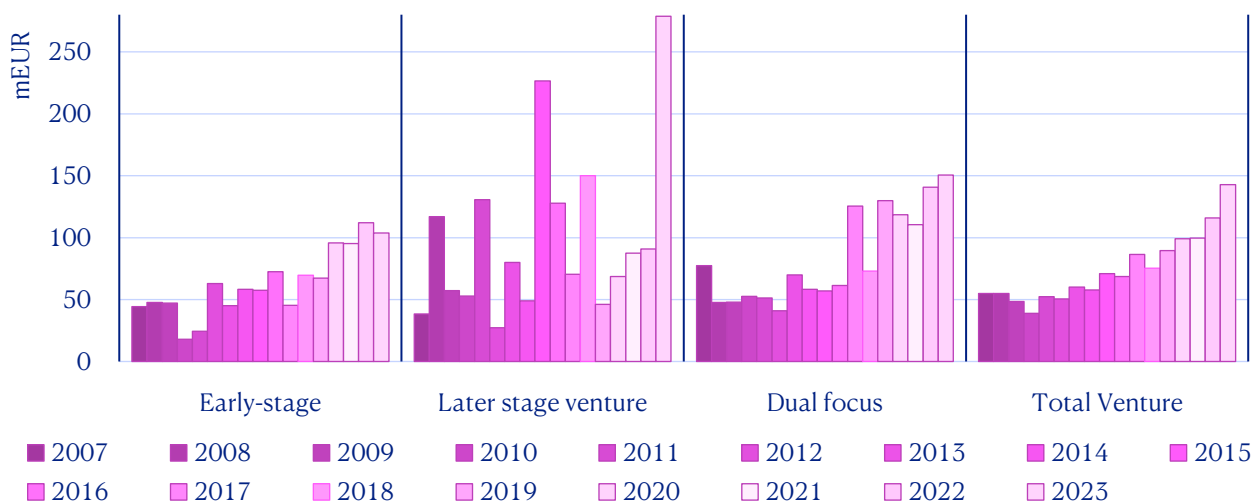
In 2023, the average size of VC funds closed within the year increased by 23% to EUR 142m (Figure 19). This amount constitutes the highest value ever registered in the Invest Europe statistics since 2007. The average size increased strongly for funds with a focus on later-stage investments, but this is based on only a small number of final later-stage fund closings. Funds with a dual focus on all venture stages also increased in average fund size at final closing. In contrast, the average size of funds that target early-stage investments decreased. The number of final venture fund closings also decreased (from 129 to 83) in 2023. The limited number of late-stage venture fund closings coupled with their relatively modest sizes raises concerns about meeting the financing needs of high-growth innovative companies.

The results outlined in Figure 20 are biased by a relatively large group of VC funds in the US that are considerably bigger than their peers in the set of “large funds” in Europe. While PitchBook data for 2023 show 28 US venture fund closings at a size larger than USD 500m (data retrieved 8 November 2024), Invest Europe/EDC statistics show only 6 funds of a similar size that performed a final closing in Europe in 2023. While such figures can only be interpreted as an

¹⁵ Invest Europe started publishing fundraising by fund stage focus in 2007.

approximation of the “gap” between European and US funds, as underlying definitions for the collection of European and US data are not always identical, it is visible that Europe has a considerable lack of large venture funds.

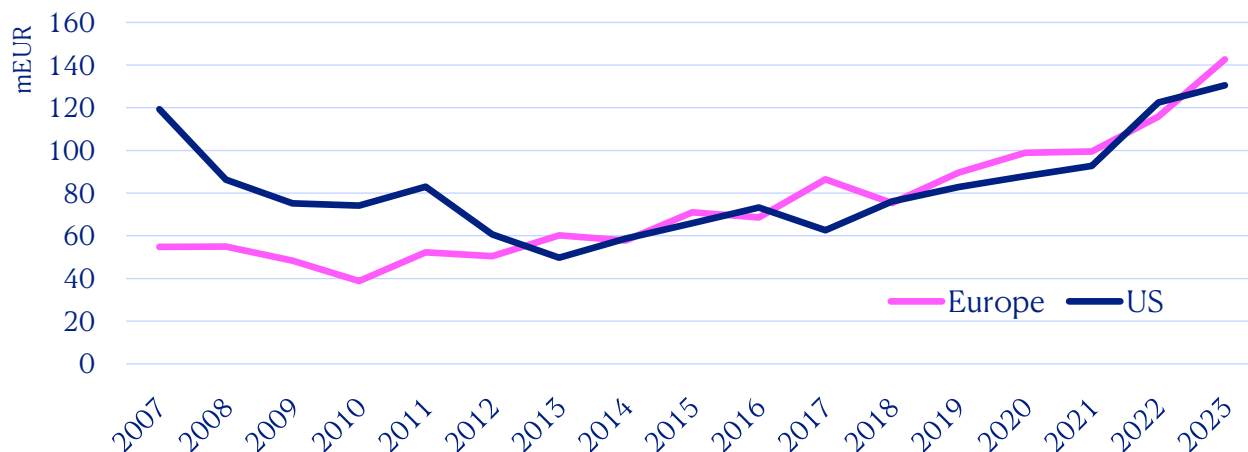
Figure 19: Average VC fund size (at final closing; cumulative amounts raised since inception) *



* The results for 2023 are based on 83 final VC fund closings (36 funds with an early-stage focus, 8 funds with a later-stage focus and 39 venture funds with a focus on all stages).

Source: Invest Europe, authors' calculations

Figure 20: Average VC fund sizes in Europe and the USA

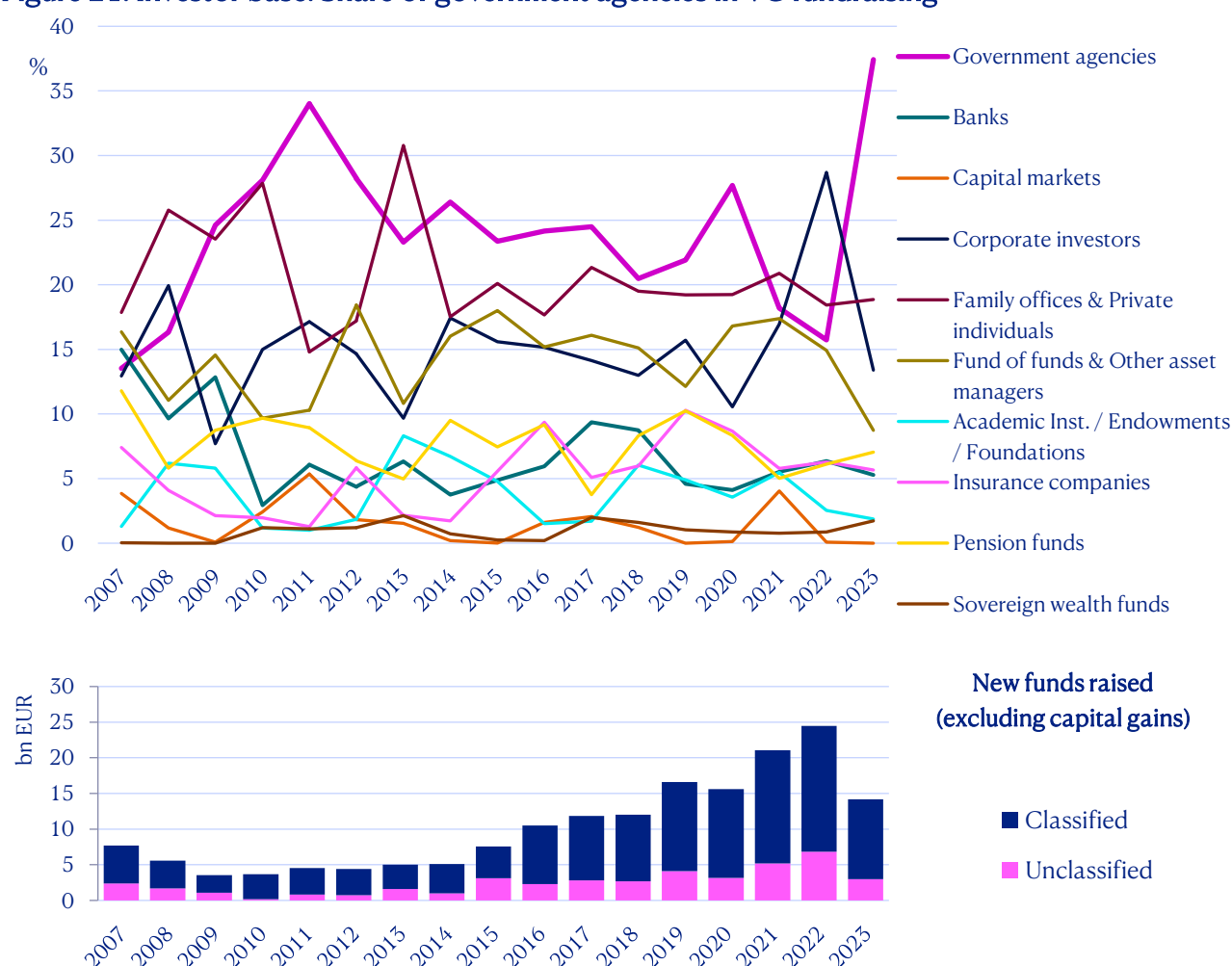


Source: Invest Europe, NVCA, authors' calculations

The European VC ecosystem benefitted substantially from market-stabilising public intervention during and after the Great Financial Crisis, when investors exhibited a cautious sentiment for risk capital. Since 2012, a normalisation has set, although public support has continued to play an important role for market development. However, even during the Covid-19 crisis, the share of government agencies investment in VC funds did not reach a new record high. These changes are visible in the variations of the investor base during the past years (Figure 21). According to

Invest Europe figures, the share of government agencies' contribution to VC fundraising increased from 14% in 2007 to 34% in 2011, before it came down again in the subsequent years. In the exceptional Covid-19 crisis year of 2020, the share of government agencies' investment in VC funds increased again and reached a level of 28%. The two following years saw a decline in government agencies' activities, but 2023 showed a turnaround, with their contributions to VC funds rising to a record level of 37%. It remains to be seen, however, if this level will be confirmed by revised Invest Europe data, once the currently unclassified VC fundraising data will become assigned to specific fund investor categories. In nominal terms, government agencies contributed EUR 4.2bn to European VC fundraising in 2023 (+50% compared to 2022).

Figure 21: Investor base: Share of government agencies in VC fundraising*



* Percentage of incremental amounts raised during year (in contrast to final closings only). Excludes capital gains. Unclassified sources of funds have been extrapolated.

Source: Invest Europe, authors' calculations

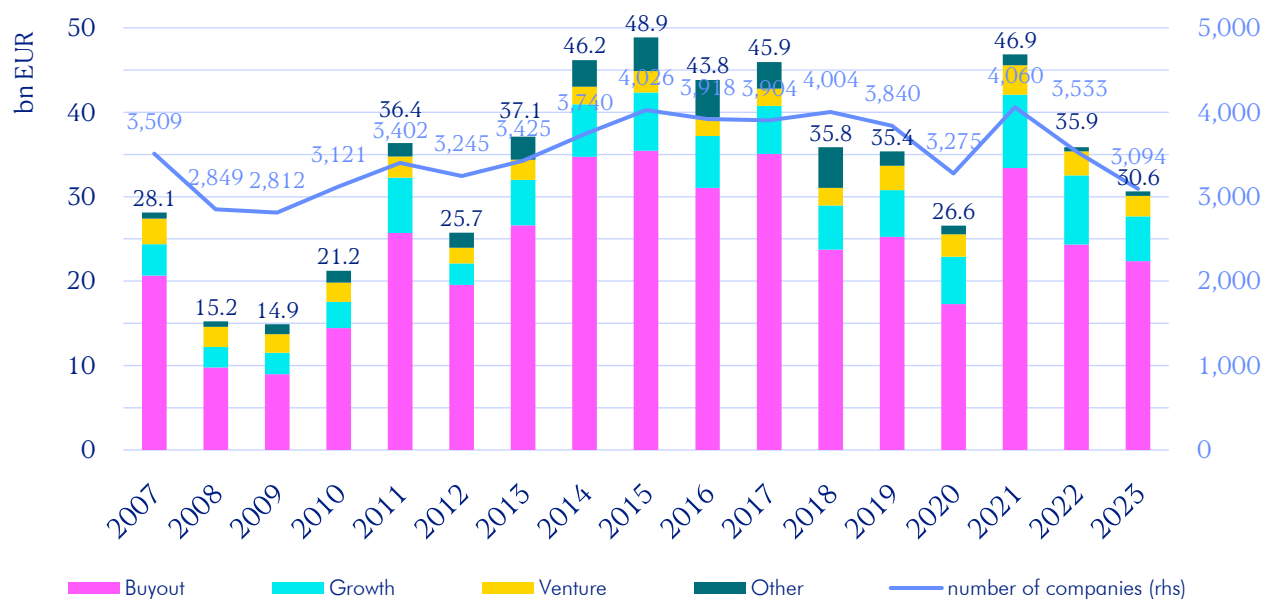
Even if a very high importance of government agencies is unsatisfying for the long term, it is noteworthy that they have played their role and supported the market in a counter-cyclical way, not only during the Covid-19 crisis, but even more so during the Global Financial Crisis, when

total VC fundraising levels more than halved. This led almost “naturally” to an increased share of government agency fund investors. Moreover, the contributions of public investors to VC funds increased not only in relative but also in absolute terms, i.e. from an average EUR 0.7bn p.a. in 2007-2009 to, on average, EUR 1.5bn in the years thereafter. Since the Covid-19 crisis year 2020, the average annual volume contributed by government agencies to VC fundraising amounted to EUR 3.3bn

4.3 | Divestment activity

In 2023, the exit market weakened further. The total PE divestment value decreased by 15% to EUR 30.6bn, which constitutes the second lowest level since 2013 (Figure 22).¹⁶ The number of companies divested dropped by 12% to 3,094 in 2023.

Figure 22: Total PE divestments (by amount at cost) of European portfolio companies



Source: Invest Europe, authors' calculations

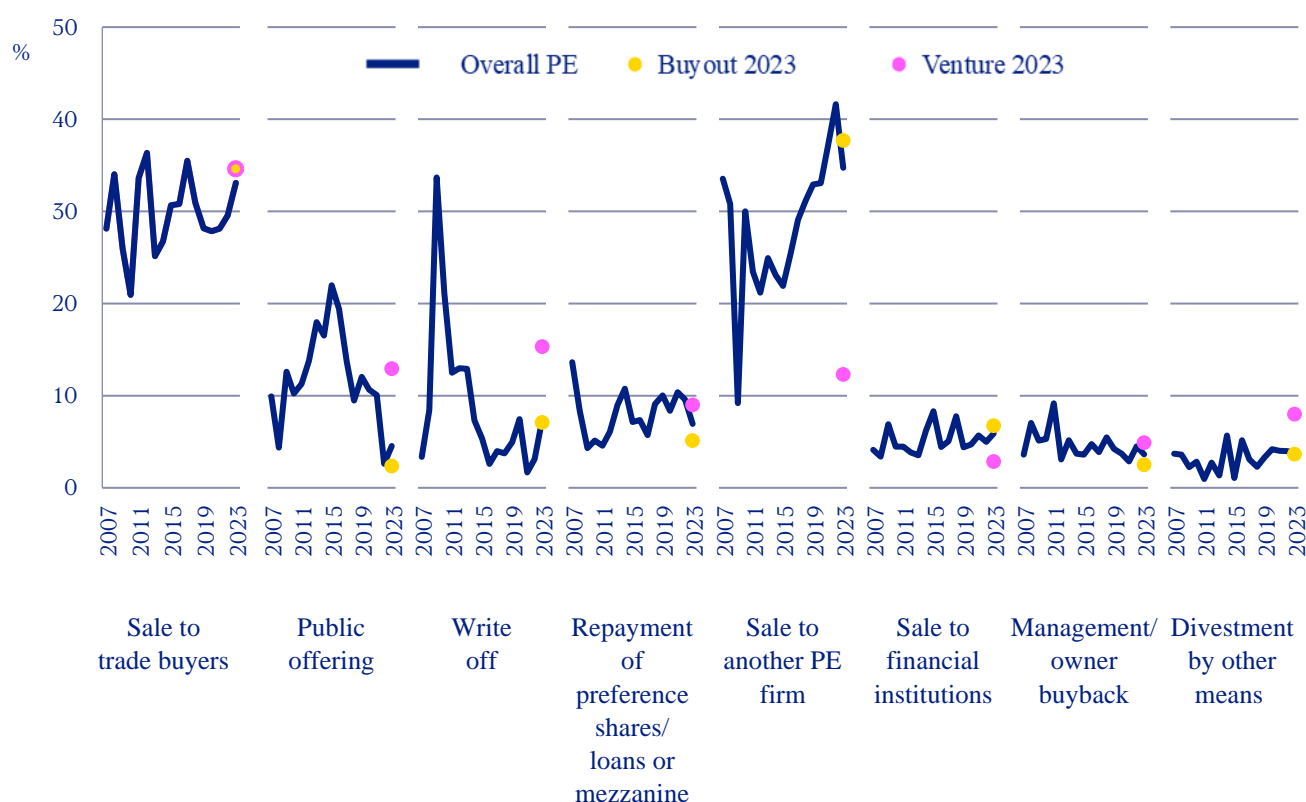
The slump in the total divestment amount in 2023 was mainly due to substantially lower activity in the growth capital (–35% to EUR 5.3bn) segment of the market, but also divestments in the buyout (–8% to EUR 22.4bn) and venture (–16% to EUR 2.4bn) capital segments decreased.¹⁷

¹⁶ Invest Europe statistics show divestment amounts at cost, i.e. the total amount divested is shown as the total amount that had been previously invested, not including any profit on the investment.

¹⁷ The numbers for venture, growth and buyout capital divestments do not sum up to total PE divestments, as total PE divestments also include the rescue/turnaround and replacement capital market segments.

The relative importance of write-offs has remained at comparatively low levels over the past decade. As regards overall PE, the percentage of write-offs over total divestment amounts had strongly decreased between 2010 and 2016, before the trend reversed in 2017. However, despite a jump in 2020, the figures were still far below the values reached in the aftermath of the Global Financial Crisis. The level even reached a record low of 1.7% in 2021, before increasing to 7.4% 2023, due to the difficult macroeconomic environment (Figure 23). Trade sales and sales to another PE house together accounted for more than two thirds of the total PE divestment amounts in 2023. The share of public offerings slightly decreased, on average, since its record high in 2015.¹⁸ In the VC market, the relative importance of write-offs increased to a level of 15.3% in 2023. This is the highest value since 2017, but still far from the average level of 20.3% reached between 2009 and 2017. At the same time, the share of public offerings over total venture exits increased to 12.9%.

Figure 23: Divestment routes (amount divested at cost; percentage of total)*



* "Overall" figures are *not* the weighted average of the "buyout" and "venture" figures, as they also include the growth, rescue/turnaround and replacement capital market segments.

Source: Invest Europe, authors' calculations

¹⁸ In the Invest Europe data, the category "Public Offerings" includes first divestment following flotation (IPO) and sale of quoted equity post flotation.

Box 6: Invest Europe definition of exit routes

Management/ Owner buy-back: The buyer of the company is its management team.

Public offering:

First divestment following flotation (IPO): The sale or distribution of a private company's shares to the public for the first time by listing the company on the stock exchange.

Sale of quoted equity post flotation: It includes sale of quoted shares only if connected to a former PE investment, e.g. sale of quoted shares after a lock-up period.

Repayment of preference shares / loans or mezzanine: If the PE firm provided loans or bought preference shares in the company at the time of investment, then their repayment according to the amortisation schedule represents a decrease of the financial claim of the firm into the company, and hence a divestment.

Sale to another private equity firm: The buyer of the portfolio company is a PE firm.

Sale to financial institution: A financial institution is an entity that provides financial services for its clients:

Depository institutions: deposit-taking institutions that accept and manage deposits and make loans, including banks, building societies, credit unions, trust companies, and mortgage loan companies.

Contractual institutions: Insurance companies and pension funds.

Investment institutions other than direct PE firms.

Trade sale: The sale of a company's shares to industrial investors.

Write-off: The value of the investment is eliminated and the return to investors is zero or negative.

Note: Recapitalisations are not considered in the divestment statistics.

Source: Invest Europe (2024a)

4.4 | Private equity prospects

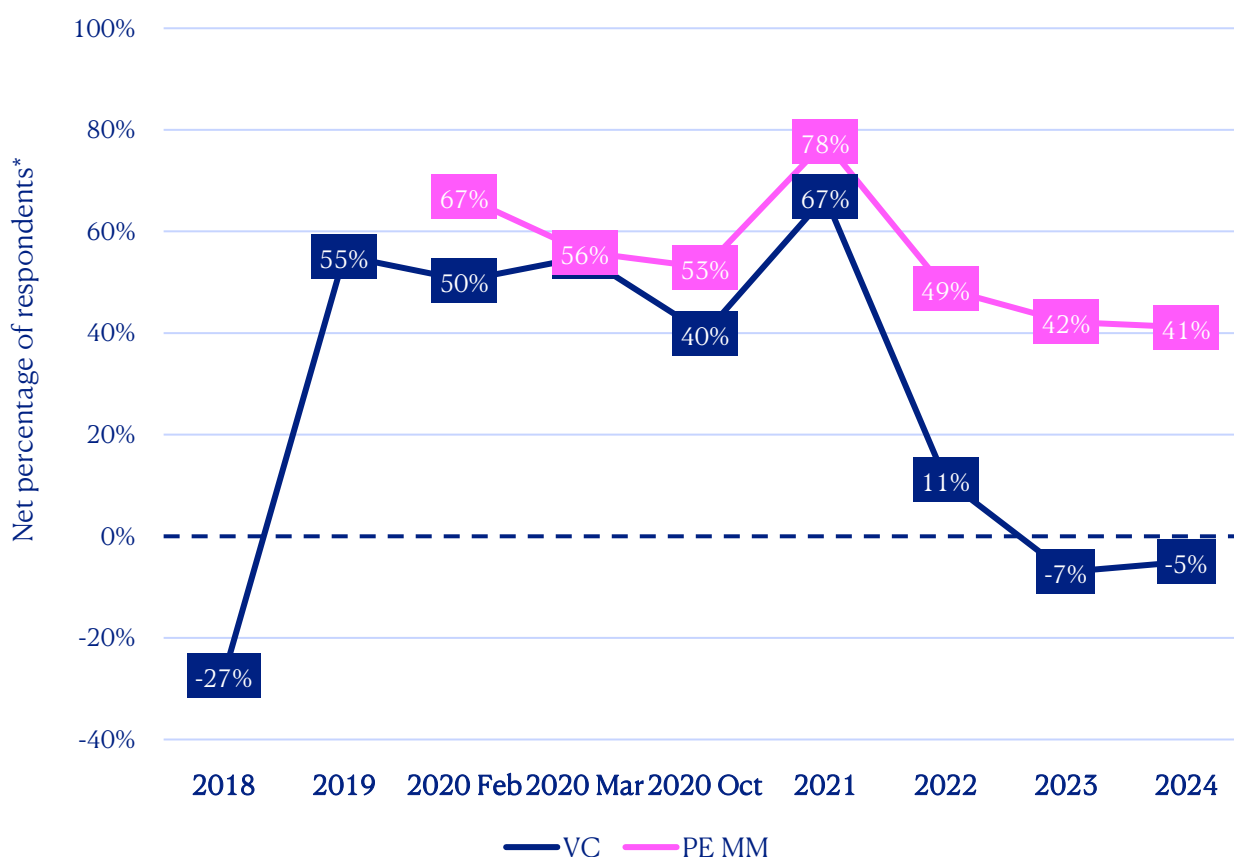
4.4.1 | Current situation and market actors' concerns

Following the severe crisis of European PE and VC markets in the years 2008-2009 and subsequent years, remarkable positive developments have been observed in the subsequent years. Also during the Covid crisis, despite the measurable harm of the initial 2020 lockdowns, the VC and PE industry did not suffer for a longer term. By the end of 2020, VC firms under strict lockdown had caught up in terms of activity rate (both in deals and volumes) with their no-lockdown benchmark (Crisanti et al, 2021; Kraemer-Eis, Botsari, Gvetadze, Lang, and Torfs, 2021). In 2021, many market activity indicators reflected another peak year for European PE/VC.

The drop in market activity since 2022, as well as signals for a recent positive turnaround, are also reflected in the results of the 2024 waves of the *EIF Equity Survey* (combined *EIF VC Survey* and *EIF Private Equity Mid-Market Survey*). In a nutshell, they clearly report a still difficult fundraising and exit environment in the first half-year of 2024. At the same time, the survey respondents conveyed expectations for an improvement of the situation in the second half of 2024 and the first half-year of 2025.

In most survey categories, the market sentiment among VCs was considerably worse than among PE fund managers. The fundraising environment constitutes a notable exception, for which both *EIF Equity Survey* respondent groups reported a similarly negative picture of the current situation. Access to finance of portfolio companies is rated significantly better by PE MM fund managers (net balance level of +41%) than by VCs (-5%); see Figure 24. Similar to previous years, securing equity finance has been the biggest challenge for VC portfolio companies in 2024, while PE MM fund managers most frequently reported recruiting of high-quality/skilled professionals to be the key challenge for their portfolio companies.

Figure 24: Access to finance of portfolio companies

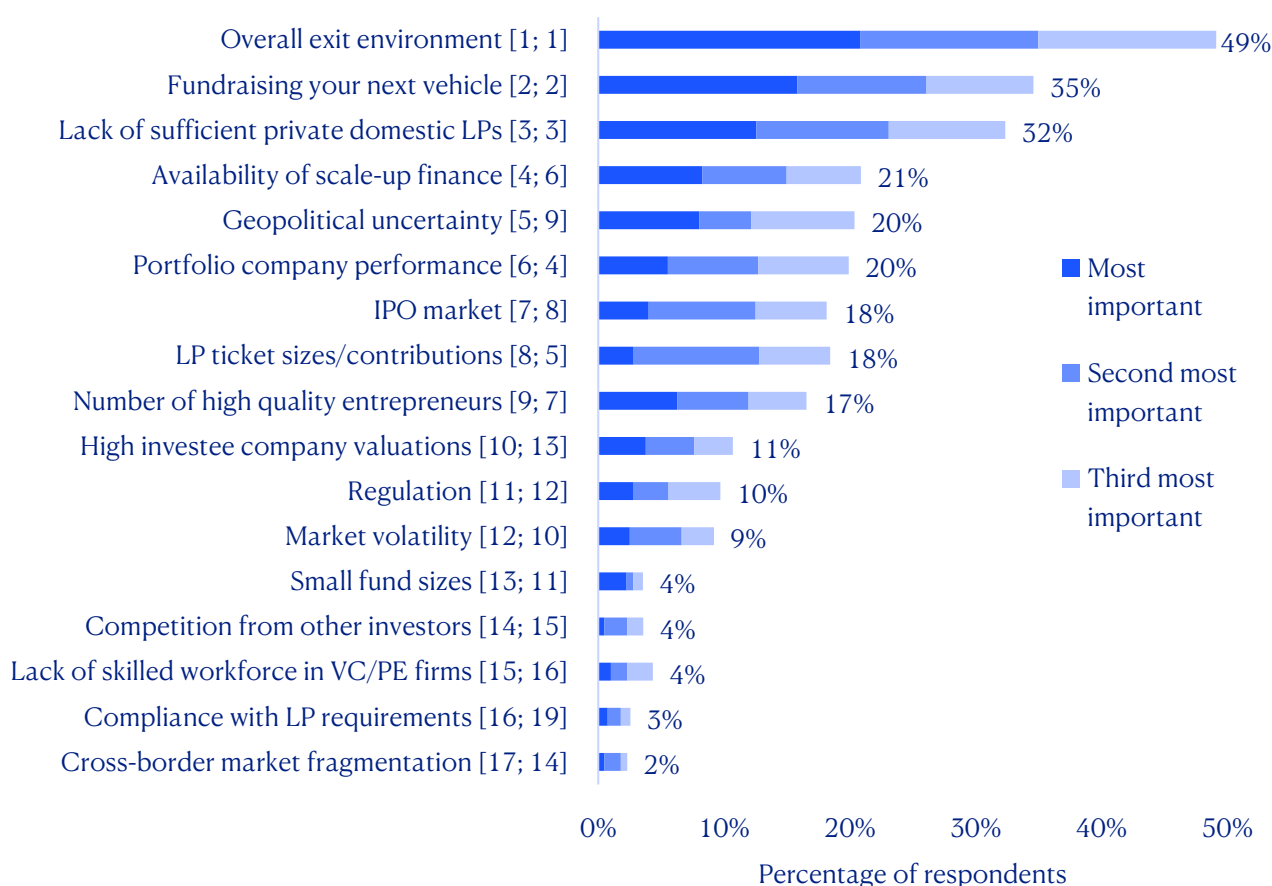


* The diagram shows the aggregated responses for the *EIF Equity Survey* question "How would you rate the access to external finance of your portfolio companies?" The figure depicts net balances, which refer to the percentage of respondents stating either "bad" or "very bad" minus the percentage of respondents stating either "good" or "very good".

Source: *EIF Private Equity Mid-Market Survey; Kraemer-Eis and Croce (2023)*

At the fund manager level, the exit environment constituted the biggest challenge for VCs in 2024, while fundraising and the lack of sufficient private domestic LPs were also frequently stated as concerns; see Figure 25 and Botsari and Lang (2024) for details. For PE MM fund managers, geopolitical uncertainty, fundraising, exit environment, and portfolio company performance are the top challenges, according to the *EIF PE Mid-Market Survey*.

Figure 25: Biggest challenges in VC business*



* Diagram shows the results for the *EIF VC Survey 2024* question “Please select the biggest challenges you currently see in the venture capital business.” The graph shows the total percentage of responses with respect to the items selected by each respondent as their three most important challenges (as far as applicable). The first number in brackets [a;b] corresponds to the current ranking of the challenge while the second number represents the respective ranking of the challenge in the *EIF VC Survey 2023*.

Source: Botsari and Lang (2024), based on *EIF VC Survey 2024*

While many market sentiment indicators of the *EIF Equity Survey* that cover the current situation have still not left negative territory in 2024, expectations for the 12 months following the survey improved considerably for most of the reported categories. Going forward, despite important challenges, fund managers’ improved expectations seem to signal that the crisis trough could have already been reached and a moderate upturn could be expected. See Box 7 for an overview of the *EIF Equity Survey*.

Box 7: The EIF Equity Survey (EIF Venture Capital and EIF Private Equity Mid-Market Survey)

The *EIF Equity Survey*, i.e. the combined *EIF Venture Capital and Private Equity Mid-Market Survey* (EIF VC and PE MM Survey), is a survey among VC and PE general partner (GP)¹⁹/management companies targeting VC and PE mid-market investments in Europe. The surveyed population includes VC/PE firms in which EIF invested as well as firms in which EIF has not invested.

The first *EIF VC Survey* wave was conducted in November/December 2017. The *EIF PE MM Survey* was launched in 2020. The latest survey wave was performed in summer 2024, when the *EIF VC Survey* and the *EIF PE MM Survey* were merged for the first time. The main topics of the questionnaire covered the market sentiment and EIF's added value, products and processes. The survey results are always published at https://www.eif.org/news_centre/markets-and-impact/index.

These EIF surveys complement both recent and future quantitative analyses of the economic impact of the EIF's equity operations in the market for VC and PE MM financing. The surveys provide the opportunity to retrieve unique market insight. To the best of our knowledge, the combined *EIF PE MM Survey* and *EIF VC Survey* currently represent the largest regular survey exercise among GPs in Europe.

The already large outreach of the EIF surveys, which are coordinated by EIF's Market Assessment & Research, and the high relevance of the questionnaire topics for both market participants and policy makers have further increased through a cooperation with Invest Europe since 2021. Moreover, VC sentiment studies, such as those based on the *EIF Equity Survey*, enable a better understanding of the current environment and industry outlook over time and therefore have considerable practical relevance for policy makers, investors and entrepreneurs seeking financing. In market downturns and periods with high geopolitical and macroeconomic uncertainties, which could have far-reaching and long-lasting consequences and may change the long-run framework conditions for SMEs, it becomes even more important to be able to generate timely, relevant and impactful market information that feeds into efficient policy design (Kraemer-Eis, Botsari and Lang, 2023).

The *EIF Equity Survey* is going to be repeated on a regular basis in order to derive robust results and implications. As such, future waves will include additional policy implications and improvements in the EIF's processes and products, as well as a comprehensive market overview of the PE/VC landscape.

4.4.2 | Structural challenges affecting European PE and VC

The PE and VC markets have been challenged by the economic developments of the last years, including several severe economic and financial market crises, which resulted in significant structural changes in the global and European economic landscape. The digitalisation of the economy, which has been further intensified by the Covid-19 crisis and beyond, has led to a differentiation of market segments. On the one hand, companies in research-intensive sectors continue to follow more traditional growth models with capital-intensive development stages at the beginning of their life. On the other hand, companies in the digital space are able to start their activities with very limited resources but are exposed to unprecedented needs for funding in

¹⁹ Independent VC fund managers act as general partner in a limited partnership in which the fund investors invest as limited partners. This is the most common legal structure for VC funds in Europe.

globalisation of their business models. As a result, depending on the sector and the business models of the companies, time-spans from start-up to global leader have shortened considerably and require companies to scale quickly to overcome the risk of seeing their business model being out-dated before they capture a significant market share.

Innovative fast-growing firms that are scaling up into larger companies contribute considerably to the overall economic activity, in particular during crises. Despite being disproportionately hit during crises, high growth enterprises, in particular the larger ones, still significantly contribute to economic activity. The economic significance of such firms for short-run growth is almost entirely based on large HGEs, both in phases of expansion but even more so during recoveries (Benedetti Fasil et al., 2021).

On a global level, the VC market has adapted to the new diversity of its target sectors. This has led to a bifurcation of the market between relatively small funds aiming at scouting emerging business models and a still relatively new class of giant VC funds that expanded globally from the US, providing large scale capital to businesses in their worldwide market expansion. In the large-scale technology growth capital market, Europe has still too few established players.

A comparison of PE/VC statistics confirms that the gap between the VC markets in the US and in Europe is particularly big at the later stage (AFME, 2017; Echiksone 2017; Benedetti Fasil et al., 2021). These differences are also reflected by substantial distinctions in fund and deal sizes: At the scale-up stage, US companies are funded by significantly larger funds than their European peers. Furthermore, the average VC-backed US company typically receives higher amounts than its EU counterpart (details are provided in AFME, 2017, Kraemer-Eis and Lang, 2017, and Benedetti Fasil, 2021).

The Covid-19 crisis as well as the current difficult macroeconomic conditions have underlined the need for broader availability of scale-up financing sources, particularly in periods of a difficult exit environment and very challenging IPO markets, which entail an increased risk that investors need to sell companies early (Botsari, Kiefer, Lang and Pal, 2021; Kraemer-Eis et al., 2022). See Kraemer-Eis, Botsari, Gvetadze, Lang and Torfs (2021) for an overview of the scale-up financing gap.

Recent results of the *EIF Equity Survey* reveal that securing equity financing has indeed remained the biggest challenge for VCs' portfolio companies (Botsari and Lang, 2024). While fundraising is, on average, the biggest challenge seen in VC business over time, the exit environment has strongly increased in importance as a challenge over the last two years, even surpassing fundraising as the first most important challenge. Insufficient IPO market liquidity and a thin M&A market are mentioned as key challenges for exits. At the same time, three out of the top-four challenges are related to fundraising, including the lack of private domestic LPs and the availability of scale-up financing (whose importance as a challenge increased over the last year).

On the positive side, VCs see promising investment opportunities in several sectors, particularly in the areas of AI and energy/climate. Fund managers' confidence in the long-term growth prospects of the European VC industry picked up slightly from last year's all-time low, and remains well above the average threshold on the 1-10 confidence scale (Botsari and Lang, 2024).

Over the past two decades, the European VC market has matured and the performance of European VC funds has improved (see, also for details, Invest Europe, 2024b). Should these trends continue over the medium to long term, and not get completely interrupted by the current crisis, the potential returns of early-stage companies would have significantly positive impacts on the performance of VC investing.

The geographical fragmentation of the European VC market

The European VC market has remained fragmented. Whilst the traditional core markets in Europe (e.g., the UK and Scandinavia) still have a relatively high market activity and others have caught up over more recent years (e.g., Spain), other countries continue to struggle with the size of their domestic VC market which is in no relation to their share in the aggregate GDP of the EU (e.g. Italy and Romania). Figure 26 provides an overview of VC investments as a share of GDP for European and selected OECD countries as well as a European average. Sizable differences in the development of the VC markets prevail and several markets not only suffer from subcritical size but from an institutional investor base that is not sufficiently ready to invest in this asset class (see Kraemer-Eis, Botsari, Gvetadze, and Lang, 2018). See also section 3.1 | for an overview of differences in SME financing in general, with a sub-category looking at national equity markets, between EU Member States.

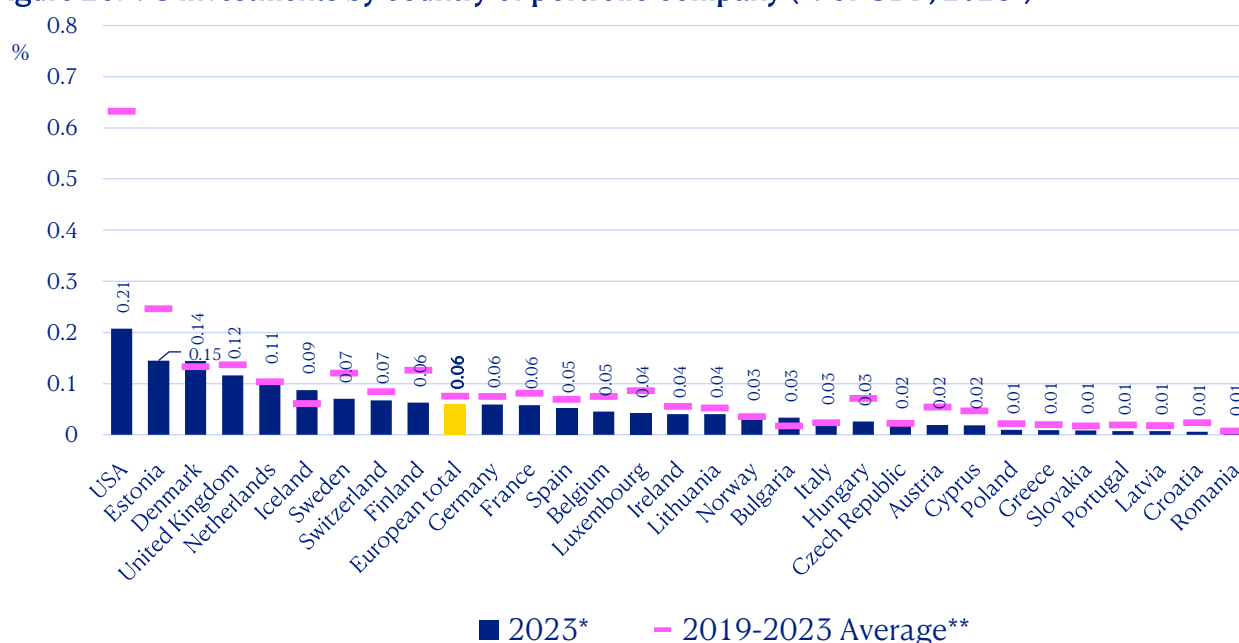
However, when looking into the geographic dispersion of European VC activity in more detail, the picture becomes more complex. VC investors tend to target tech “hubs” rather than certain regions, based on the expertise developed in those hubs. A start-up’s location is likely to have a major influence on the amount of VC that the enterprise receives as well as the number of funding rounds it goes through (Nepelski et al., 2016, who provide a detailed overview of European VC-backed start-up hotspots). EIF research has shown that European hubs, typically backed by EIF investments, act as the beating heart of a complex network of national and international investments. This claim is supported by data on EIF-backed investment amounts originated by hubs between 1996 and 2014: 23% of these remained in the hub, 40% reached out to other in-country locations and the remaining 37% travelled beyond the national frontier (Kraemer-Eis, Signore and Prencipe, 2016).

Since higher cross-border investments can be interpreted as the signal of a deeper integration of the European VC market, EIF may hold a vantage point in fostering the consolidation of a European-wide VC ecosystem. In addition, cross-border VC investments have been facilitated to a certain extent by EU-wide overarching rules and regulations. Moreover, VC firms tend to cluster together much more than their investees. A recent EIF - Invest Europe study found, based on data covering investments between 2007 and 2020, that more than 50% of all VC firms operate in very large cities in comparison to 34% of all start-ups (Crisanti et al., 2021). An updated EIF - Invest Europe study (see Crisanti et al., 2023), which uses investment data covering the years 2007 until 2021, finds that the top 10 European VC hubs account for 69% [51%] of total outgoing [incoming] VC investment volumes, and approximately two-thirds of total volumes in the European VC ecosystem involve actors from two distinct VC hubs. However, there is still much disintegration in terms of company structure, legal system, regulation, taxations, etc. Another reason for improved cross border investments is that the main hubs have

attracted talents from different countries who retain links to their home countries and in turn attract additional human capital and/or companies to the various hubs.

Asdrubali (2023) finds that, besides GDP (or market capitalisation) and distance, the quality of institutions and especially the degree of global financial integration do play a role in shaping cross-border VC flows. At the same time, the uneven development of the financial market within Europe appears to matter little for cross-border VC flows. Hence, policies shaping the institutional framework of the financial markets can facilitate cross border activities and foster an international VC ecosystem for investment.

Figure 26: VC investments by country of portfolio company (% of GDP, 2023*)



* 2023, or latest available year.

** 2019-2023 average, if available.

Note: European total refers to Europe as covered by Invest Europe. See OECD (2017) for an overview of the international comparability of VC data. Countries with VC investments of less than 0.01% of GDP in 2023 are not shown.

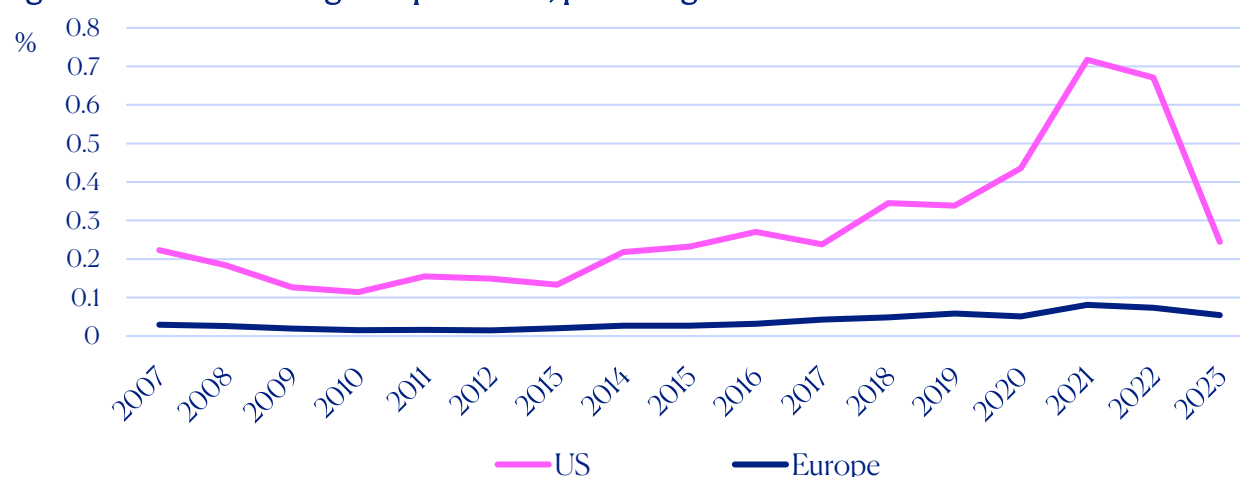
Sources: Invest Europe, OECD, authors' calculations

VC market size and implications for European startups and scaleups

The comparison of VC investment data between Europe and the US or other countries outside Europe is not straightforward for several reasons (see OECD, 2017, for an overview). For example, data for the US often does not separate out what share of capital is invested by formal VC/PE funds, which leads to US investment figures being higher than the related fundraising. Figure 27 shows a comparison of VC fundraising as a share of GDP in Europe and the US from 2007 to 2023. Although VC fundraising is, on average, lower than VC investment in the US, its level is still substantially higher than in Europe and confirms the diagnosis of a comparatively small European VC market. Despite the decline in market activity in recent years, the gap – in absolute and relative terms (relative to GDP) is still substantial.

European tech companies are often acquired by non-EU buyers, particularly from the US, which “raises the issue of whether the missing scale-up phenomenon in Europe could be linked to the lack of serial tech buyers, that is, incumbents in highly innovative and competitive sectors” (Prencipe, 2017). There is some evidence that foreign VC investment, in particular from the US, increases the likelihood of foreign exits and emigration of entrepreneurs (Braun et al., 2019). While the size of the relocation effect of foreign VC is limited (estimates by Weik and Braun, 2021, suggest that approximately 10% of early US VC investments lead to relocation), the effect is more pronounced when startup financing conditions are poor (Weik et al., 2023). Moreover, there is also some evidence that European startups that migrate to the US receive more VC funding and produce more innovation and reach a bigger scale by exit. A large part of this difference in innovation and scale can be explained by the US funding advantage. At the same time, the likelihood for a successful exit of these companies is not higher than for their peers that stay in Europe (Weik, 2023). These findings shed light on the global movement of startups and suggest that the outflow can be addressed by improving startups' local financing conditions (Weik et al., 2023). Governmental efforts to increase domestic supply of VC should also have a positive impact (Braun et al., 2019).

Figure 27: VC fundraising Europe and US, percentage of GDP*



* The underlying definitions (categorisations) for the collection of European / US data are not identical, hence differences can only be interpreted as approximation.

Source: Invest Europe, NVCA, PitchBook, authors' calculations

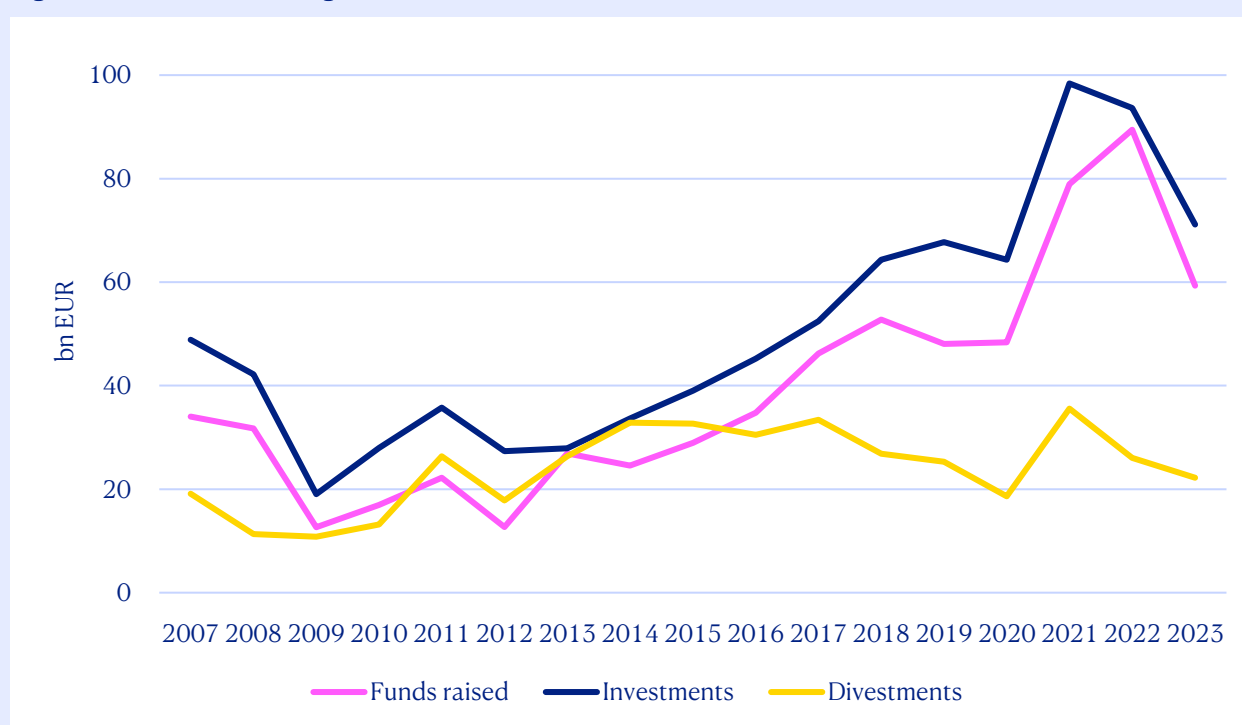
Some of the challenges described in the preceding sections continue to weigh on the access to funding in the European PE market and, in particular, the VC and growth market segments. This supports a view that public backing is needed in order to strengthen the market, which is particularly true for new funds, which typically receive less private investment. See Kraemer-Eis et al. (2023) for a more detailed overview.

As mentioned at the beginning of Chapter 4, the numbers (typically based on Invest Europe statistics) and analyses provided in this chapter cover Europe as a whole, except if stated differently. A brief overview of selected differences to EU-27 time series is presented in Box 8.

Box 8: Selected Invest Europe data for EU-27

Comparing Invest Europe PE/VC market activity figures between Europe and the EU-27 does of course lead to different levels of fundraising, investments, and divestments, but does not show bigger in terms of latest developments. In 2023, funds located in the EU-27 accounted for 45% of total amounts raised by funds located in Europe. The shares of investments in [divestments of] EU-27 portfolio companies (71%) [(72%)] over total investments [divestments] in European portfolio companies was much higher. These percentages are roughly in line with the average of the last ten years. The numbers reflect that EU-27 companies are net recipients of European PE/VC funds' investments based outside the EU-27. In terms of amounts, EU-27 PE fundraising was at EUR 59.3bn in 2023, while investments [divestments] accounted for EUR 71.1bn [EUR 22.2bn]; see see Figure B8.1.

Figure B8.1: PE fundraising, investment and divestment amounts in the EU-27*



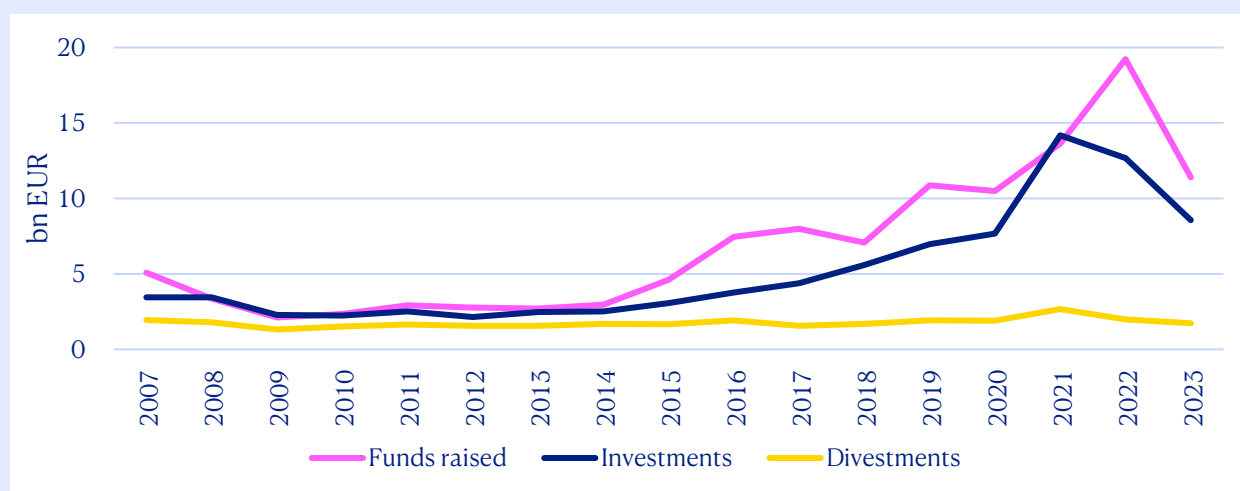
* In this diagram, investment and divestment data are based on the “market approach”, which is based on the location of the portfolio companies. This approach offers sufficient granularity to split the results by country (group).

Source: Invest Europe, authors' calculations

In Venture Capital, the EU-27 shares in total European fundraising (67%), investment (68%) and divestment (75%) are closer to each other than in the case of overall private equity. This is also reflected in EU-27 VC fundraising continuously being above EU-27 VC investments (see Figure B8.2). In terms of amounts, EU-27 VC fundraising was at EUR 11.4bn in 2023, while investments [divestments] accounted for EUR 8.6bn [EUR 1.7bn].

Box 8 continued

Figure B8.2: VC fundraising, investment and divestment amounts in the EU-27*



* In this diagram, investment and divestment data are based on the “market approach”, which is based on the location of the portfolio companies. This approach offers sufficient granularity to split the results by country (group) and stage focus.

Source: Invest Europe, authors' calculations

5 | SME debt products

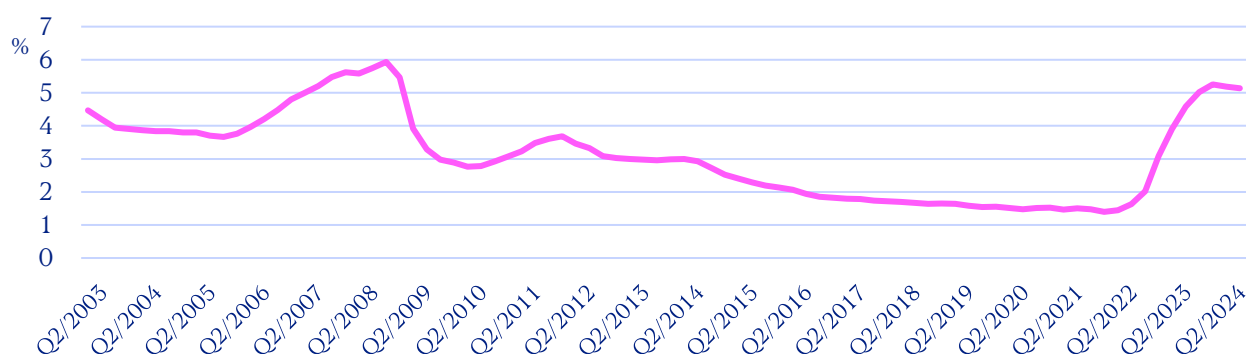
5.1 | SME guarantees

5.1.1 | Bank lending activity & SME bank financing conditions

The bank-lending channel has traditionally been the most important source of external financing for SMEs, particularly in Europe, where SMEs heavily rely on bank-based debt instruments to finance working capital needs and long-term investments. Corporate debt-reliance intensified during the Covid-19 pandemic, as European SMEs heavily depended on public financial support, such as public guarantee schemes or subsidised lending, to address urgent short-term liquidity needs.

After a long period of either declining or stagnating interest rates, corporate borrowing costs have risen sharply over the past years. By the end of 2021, the ECB's corporate borrowing cost indicator had bottomed out at 1.35%. Since then, rates have steadily increased, pushing the indicator to 5.25% by the end of 2023—a level not seen since 2008. In 2024, the indicator stabilised slightly, reaching 5.1% (Figure 28).

Figure 28: Composite cost of borrowing*



* To Euro area non-financial corporations.

Source: ECB, authors' calculations

Secured lending, achieved through the use of collateral or guarantees, plays a crucial role in enhancing SMEs' access to finance. By reducing the risk perceived by lenders, secured lending can result in lower interest rates and more favourable loan terms. Additionally, it offers a layer of

security that enables larger borrowing amounts or longer maturities, which are critical for SMEs seeking to capitalise on investment and growth opportunities.

5.1.2 | Credit Guarantee Schemes as a policy response to market failures in the SME bank-lending market

Credit Guarantee Schemes (CGSs) “are used widely across economies as important tools to ease financial constraints for SMEs and start-ups” (OECD, 2013). This is because guarantee mechanisms, “whereby should the borrower default the guarantor compensates a pre-defined share of the outstanding loan” (OECD, 2015), reduce the risk of lenders and favour the provision of financing to viable businesses that are constrained in their access to finance – either due to lack of collateral or a short credit history and operational record.

Credit guarantee programmes expanded substantially in the years 2007-2011, as governments responded to the global financial crisis; and more recently in 2020, in response to the Covid-19 crisis. SMEs were more vulnerable to the economic impact of the pandemic and in greater need of government support compared to their larger counterparts, given that SMEs typically have thinner equity cushions, lower liquidity buffers, fewer financing options and less-diversified revenue sources (IMF, 2020; see Brault, 2023). Among the credit-support programmes aimed at mitigating the effects of the crisis on SMEs, guarantees on loans emerged as the preferred credit-support instrument, accounting for the vast majority of the announced government support volumes.

Carefully designed guarantee schemes have positive macroeconomic effects, meaning that the costs for the tax payers due to default payments are outweighed by the positive stimulating effects of guarantees on the economy. Therefore, CGSs “remain the most wide-spread instrument in use across countries” to ease SMEs’ access to finance (OECD, 2018). While CGSs do not alleviate information asymmetries directly, and hence do not address the root of the market failure, they can increase the incentives of lenders to supply credit to SMEs by providing a substitute for collateral, and if designed correctly, increase overall welfare.

The EIF plays an important role in alleviating problems experienced by SMEs in accessing finance. Through a wide range of financial intermediaries, such as banks, leasing companies, guarantee funds, mutual guarantee institutions, promotional banks and other financial intermediaries, the EIF effectively provides both financing to SMEs and guarantees for SME financing. Apart from EIF guarantees for securitised SME financing instruments, the EIF offers guarantees/counter-guarantees for portfolios of microcredits, SME loans or leases.²⁰ In doing so, the EIF predominantly focuses on pan-European mandates on the back of the EU budgetary guarantee from the European Commission. This activity is complemented with a more targeted intervention on the back of the mandates from national and regional authorities, mainly in their capacity as Managing Authorities of the EU shared management resources.

²⁰ See for more information the EIF website www.eif.org.

5.1.3 | Market size and activity in 2023

Market information concerning CGSs in Europe is gathered by AECM, the European Association of Guarantee Institutions.²¹ In the following, based on data from the latest AECM Scoreboard,²² we provide information about the use of guarantees in countries with at least one AECM member to show the state and development of this important market segment.

According to the OECD (2013), guarantees are particularly relevant “in those countries where a network of local or sectoral guarantee institutions is well established”. Key figures based on *outstanding guarantees* on SME loan portfolios (as of 31 December 2023) are presented in Table 3.

As a result of the unprecedented support measures implemented by guarantee institutions in the context of the Covid-19 crisis, the outstanding guarantee volume with regard to guarantees originated from and implemented by AECM members during 2020 had reached an all-time high, at almost EUR 331bn. By contrast, the return to normality for business activities from 2021 onwards saw the gradual phasing out of these extensive support programmes as well as the early reimbursement of emergency loans that were no longer needed. But before even SMEs could fully recover from the shock of the pandemic, they already stumbled into the next crisis caused by the Russian aggression against Ukraine. SMEs had to face new challenges amid high macroeconomic and geopolitical uncertainties – inter alia soaring energy prices, high inflation, rising interest rates, supply chain disruptions, and trade sanctions. Many AECM members set up new dedicated programmes with favourable conditions to support SMEs that were under strain due to these negative developments. However, these interventions were overcompensated by the phasing out of Covid measures. This, in turn, translated into the evidence discussed further below, that both the total outstanding guarantee volume as well as the volume of newly-granted guarantees continued to decrease in 2023.

At the end of 2023, the total outstanding guarantee volume stood at approximately EUR 206bn, representing a 23% decrease compared to 2022 (and a 34% decrease compared to 2021). Despite this significant drop, the volume of total outstanding guarantees remains well above the pre-pandemic level. More than one-third of this volume is attributed to France - in the context of Bpifrance implementing the French government’s PGE (Prêt Garanti par l’Etat) programme, while another one-fifth approximately is attributed to the United Kingdom - with British Business Bank being the implementing institution of Her Majesty’s Treasury (HMT) extensive support programme.

Consequently, the core countries in terms of total *volumes* of guarantee activities are France (EUR 71bn), the United Kingdom (EUR 37bn), Italy (EUR 16bn), and Türkiye (EUR 16bn). The United Kingdom, Türkiye, and France also have the highest total *number* of outstanding guarantees. In the EU-27, Poland, Hungary, Romania, and Spain also feature high in the ranking

²¹ We thank our colleagues from AECM for their support. AECM currently has 45 members in 23 EU Member States plus Azerbaijan, Bosnia and Herzegovina, Kosovo, Moldova, Serbia, Switzerland, Türkiye, and the United Kingdom. In the AECM member countries, the AECM members cover all or almost all SME guarantee activity. Some AECM members are national associations or networks and thus have their own member organisations. AECM has purely private, mutual, public, and public-private mixed members. *Source:* AECM.

²² See AECM Statistical Yearbook 2023: <https://aecm.wildapricot.org/resources/AECM%20Statistical%20Yearbook%202023.pdf>

(but by a relatively large margin compared to France and Italy). Overall, at the end of 2023, AECM members had almost 6 million guarantees in their portfolio (only 0.6% lower compared to 2022), suggesting that any decrease in the number of outstanding guarantees is much less pronounced than the decrease in volumes.

The outstanding guarantee volume compared to 2022 increased the most in Bulgaria (+92%), Hungary (+14%), Ireland (+10%), and Croatia (+10%). By contrast, the largest decrease was observed in Austria (–55%), Malta (–47%), and Switzerland (–47%). Across countries, the average annual growth rate was –9%, significantly higher than the percentage decrease of –23% recorded overall, reflecting the fact that this decrease was substantially driven by the phasing out of significant parts of the volume of large AECM members.

The total number of *supported SMEs* in the portfolios of the AECM members reached almost 4.7m in 2023, representing a 10% (20%) decrease compared to 2022 (2021). Out of that, in the EU, the total number of supported SMEs stood at almost 1.7m (the discrepancy reflects the large number of SME beneficiaries in the UK and Türkiye). The increased number of SMEs that had been supported in earlier years – when SMEs had found themselves at the epicentre of the Covid-19 crisis, facing increased liquidity needs and being in greater need of support – highlights the anti-cyclical role of guarantee institutions.

The *average size* of outstanding guarantees in portfolio continued its descent from the peak observed in 2020 to reach a level of almost EUR 35k, slowly returning to pre-pan-demic level. The highest average size was documented in Austria (EUR 239k), followed by Malta (EUR 173k), Estonia (EUR 163k), and Germany (EUR 159k).

Interestingly, while France, the United Kingdom and Türkiye feature at the top of the list regarding outstanding guarantee volumes, they exhibit relatively small average sizes of guarantees (EUR 45k, EUR 22k, and EUR 10k, respectively), reflecting the presence of large populations of SMEs borrowing small loans in their portfolios.

The volume of newly-granted guarantees in the full-year 2023 decreased by 8% relative to 2022 and reached EUR 45bn (Table 4). This constitutes a significant improvement compared to the 50% decline experienced in 2022, while the new guarantee volume for 2023 remains well above the pre-pandemic levels. As was also the case for the volume of outstanding guarantees, four countries (Türkiye, France, the United Kingdom, and Italy) account for 40% of this total new guarantee volume.

The highest increase in new guarantee activity was documented in Bulgaria (+509%), Malta (+140%), Serbia (+115%), and Croatia (+113%). By contrast, new guarantees decreased the most in Latvia (–54%), the United Kingdom (–54%), Ireland (–53%), Estonia (–52%), and France (–45%).

Table 3: Outstanding guarantees and number of supported SMEs in portfolio as of 31 December 2023, AECM members by country*

Country	Volume [kEUR]	% change from 2022	Number	Implied average guarantee size [kEUR]***	Number of SME beneficiaries
Austria	1,622,491	-54.8%	6,800	238.6	5,186
Belgium	1,364,258	4.4%	12,807	106.5	11,164
Bosnia-Herzegovina	20,222	-17.7%	335	60.4	295
Bulgaria	166,225	92.4%	3,388	49.1	3,064
Croatia	385,018	9.7%	2,883	133.5	2,615
Czechia	2,010,000	-15.9%	20,076	100.1	19,949
Estonia	134,899	-15.2%	829	162.7	598
Finland	1,841,974	-5.5%	19,271	95.6	22,929**
France	71,331,131	-30.1%	1,579,905	45.1	716,794
Germany	6,347,327	0.4%	39,851	159.3	32,962
Greece	3,232,955	-25.5%	116,854	27.7	29,578
Hungary	8,546,117	13.8%	94,214	90.7	71,039
Ireland	1,697,549	10.0%	23,251	73.0	2,121
Italy	15,659,807	-5.2%	132,566	118.1	124,891
Kosovo	116,245	-0.4%	6,790	17.1	10,157**
Latvia	257,629	-6.6%	1,821	141.5	1,788
Lithuania	277,004	-39.4%	2,430	114.0	2,011
Luxembourg	253,775	9.2%	1,870	135.7	505
Malta	122,491	-46.8%	706	173.5	624
Netherlands	1,300,797	-19.6%	11,602	112.1	11,602
Poland	9,252,875	-17.5%	201,795	45.9	300,147**
Portugal	5,577,752	-30.3%	107,508	51.9	71,980
Romania	7,940,636	6.7%	64,588	122.9	47,706
Serbia	3,467	-6.7%	112	31.0	112
Slovenia	294,190	-2.0%	3,254	90.4	15,725**
Spain	7,621,990	7.5%	114,856	66.4	175,477**
Switzerland	5,759,798	-46.5%	78,752	73.1	78,752
Türkiye	15,641,414	3.7%	1,591,043	9.8	1,302,126
UK	37,411,722	-32.6%	1,680,126	22.3	1,630,168
Total	206,191,758	-22.6%	5,920,283	34.8	4,692,065

* The statistics do not include the business figures of one Hungarian AECM member and of one Romanian AECM member that only have a Counter Guarantee activity.

** In the case of Finland, Kosovo, Poland, Slovenia, and Spain, the number of SME beneficiaries is reported to be higher than the number of guarantees. This is due to different reporting approaches (e.g., the number of SMEs refers to a member count, instead of the actual beneficiaries of guarantees in that particular year).

*** The fact that some AECM member organisations may include former 'inactive' SME beneficiaries in their portfolio even though the guarantee scheme already reached its maturity could distort the total number of SME beneficiaries. Therefore, for the purpose of computing the implied average guarantee size, the 'Total Number of Guarantees Outstanding' rather than the 'Total Number of SME Beneficiaries' is taken into consideration.

Source: AECM, authors' calculations

Table 4: Newly granted guarantees in the full-year 2023, AECM members by country*

Country	Total 2023	% change from 2022	% outstanding
Austria	277,621	-30.2%	17.1%
Belgium	567,863	7.8%	41.6%
Bosnia-Herzegovina	11,281	14.3%	55.8%
Bulgaria	113,398	509.4%	68.2%
Croatia	128,406	113.1%	33.4%
Czechia	343,899	-44.5%	17.1%
Estonia	29,534	-51.5%	21.9%
Finland	870,065	-2.5%	47.2%
France	3,874,175	-45.0%	5.4%
Germany	1,154,193	-10.0%	18.2%
Greece	533,477	-11.9%	16.5%
Hungary	4,734,937	3.3%	55.4%
Ireland	175,546	-52.7%	10.3%
Italy	1,180,718	-5.6%	7.5%
Kosovo	59,922	25.4%	51.5%
Latvia	40,901	-54.0%	15.9%
Lithuania	173,126	-1.7%	62.5%
Luxembourg	72,293	20.3%	28.5%
Malta	11,030	139.6%	9.0%
Netherlands	311,263	-4.9%	23.9%
Poland	10,913,016	-11.8%	117.9%
Portugal	471,423	-17.3%	8.5%
Romania	3,411,701	-11.0%	43.0%
Serbia	952	114.9%	27.5%
Slovenia	57,955	-6.5%	19.7%
Spain	2,572,204	13.1%	33.7%
Switzerland	71,870	2.3%	1.2%
Türkiye	10,106,167	21.9%	64.6%
UK	2,739,952	-54.0%	7.3%
Total	45,008,888	-8.4%	21.8%

* The statistics do not include the business figures of one Hungarian AECM member and of one Romanian AECM member that only have a Counter Guarantee activity.

** For the Polish AECM member, the total new guarantee activity in the full-year 2023 exceeded the total volume of outstanding guarantees for the same period. As a result, new guarantees in Poland are in excess of 100% of outstanding guarantees in portfolio. If the Polish AECM member in question mostly offers short-term guarantees and if the duration of the latter is less than one year, then it is reasonable to assume that many of the newly-granted guarantees are reported in the related statistics on new guarantee volumes, but are not subsequently reflected in the statistics on outstanding guarantees.

Source: AECM, authors' calculations

In the full-year 2023, the share of newly-granted guarantees in the overall portfolio reached approximately 22% of the total volume of outstanding guarantees for the same period (still higher than the 18% recorded in 2022). This share is usually around one-third of the outstanding volume. Hence, while 2020 saw the highest ever registered ratio of new over outstanding guarantee volume (almost 85%), this metric has now decreased to an exceptionally low level.

Figure 29: Volumes of outstanding guarantees in portfolio and of new guarantee volumes granted in the full-year 2023 scaled by GDP*



* 31 December 2023 or latest available data.

Sources: AECM, Eurostat, World Bank, authors' calculations

The *relative importance of guarantees* compared to the value of economic activity in each country is approximated by the share of outstanding guarantee volume (respectively, new guarantee volume) over GDP (Figure 29). After a decrease in the GDP of most countries in 2020, as a result of the recession inflicted by the pandemic, European economies recovered in subsequent years, reaching a GDP exceeding the pre-pandemic levels. At the same time, as discussed already, the phasing out of support programmes led to a significant decrease in the total outstanding guarantee volume, but also, and even more so, in the new guarantee volume. Consequently, the share of the overall AECM members' outstanding (new) guarantee volume in the GDP of AECM countries further decreased from 1.4% (0.3%) in 2022 to 1.0% (0.2%) in 2023 – much closer to the pre-pandemic level of 0.7% (0.2%).

Hungary leads the ranking (outstanding guarantees at 4.4% of GDP), while France (at 2.5%), and Romania (also at 2.5%) complete the top three. Relative to GDP, Hungary, Poland, and Romania are the three countries that recorded the highest amount of *new guarantees* in 2023 (2.4%, 1.5%, and 1.1%, respectively).

5.2 | SME Securitisation

European corporates still rely heavily on bank lending; however, non-financial corporate finance has been gradually shifting towards more capital market activity in recent years (see Figure 30). For SMEs, the possibility to substitute bank lending with other sources of finance exists only to a limited extent.

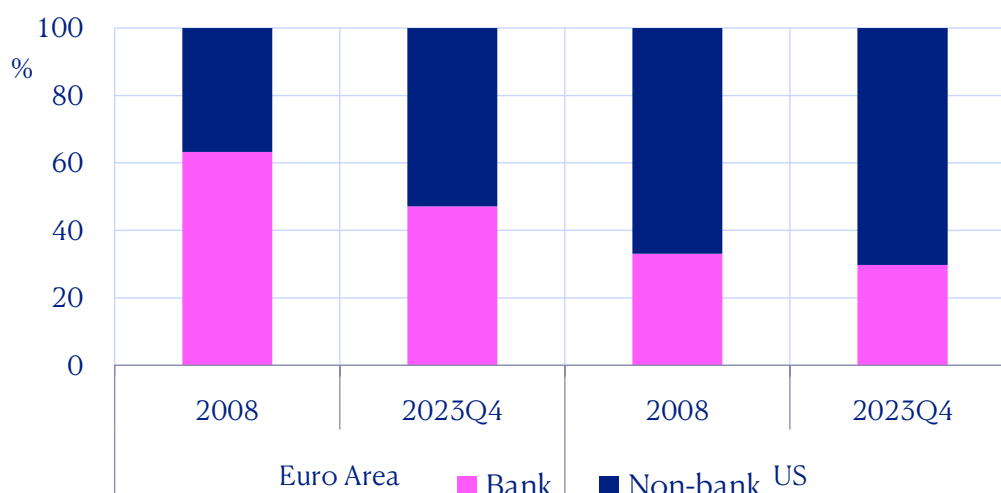
Although capital market funding in the Euro area has been increasing since the financial crisis, this trend primarily benefits large corporations. SMEs, due to their limited direct access to capital markets, can benefit from a well-functioning securitisation market, which provides indirect access by transforming illiquid SME loans into a liquid asset class. Securitisation can strengthen banks' capacity to supply new loans, mitigate credit supply frictions, and positively affect investment, sales, and employment. Moreover, securitisation creates opportunities for investors by enabling banks and borrowers to access a wider range of investors. Different tranches of asset-backed securities can be tailored to match the risk appetites and preferences of various investors.

By transferring credit risk to external investors through "true sale" transactions—where the portfolio risk is separated from the risk of the originator via a nonrecourse assignment of assets to a special purpose vehicle (SPV)—banks can free up regulatory capital, enabling them to extend more loans. In contrast, synthetic securitisation does not involve selling the assets to an SPV; instead, only the credit risk of the assets is transferred to the market through mechanisms such as credit default swaps or credit-linked notes. Both forms of securitisation such as default swaps or credit-linked notes offer highly rated assets that align with investors' mandates and provide attractive yields. If properly executed, securitisation can enhance funding options for SMEs and help banks comply with the Basel III framework while addressing European economic challenges (ESM, 2021).

Loans to SMEs are a key driver of economic activity, with securitisation serving as a scalable tool to support financing. In developed capital markets, public sector support for SMEs—such as guaranteeing mezzanine tranches—can create multiplier effects, making it an efficient use of public resources. This is especially crucial given the scarcity of public financial resources and the high public debt burden in many key countries. Strengthening SME securitisation could be one of the most effective ways to channel funds into the real economy without creating excessive distortions.

Despite its advantages for banks, investors, and SMEs, the SME securitisation (SMESec) market in Europe remains underdeveloped. Reviving and developing primary securitisation markets is essential to ensuring sufficient credit supply for SMEs during crises and recovery phases. Additionally, the development of other securitisation segments indirectly benefits SMEs by freeing up bank balance sheet space for further SME lending. However, these benefits are contingent on using the freed-up capital and fresh liquidity for new SME lending, aligning with the EIB Group's business framework.

Figure 30: Bank/non-bank debt financing of non-financial corporations in the Euro area and the US



Source: ECB, authors' calculations

5.2.1 | SMESec market activity²³

The European securitisation market has grown steadily from the beginning of the previous decade until the outbreak of the GFC. However, it remains significantly smaller than the US market. During the financial crisis, issuance remained initially at high levels in Europe, but these volumes were almost exclusively driven by the eligibility of ABS as collateral for ECB liquidity operations;²⁴ then the overall market activity decreased to the levels seen in 2003/2004.

Issuance

European *total (true sale) securitisation issuance* in 2023 showed with EUR 213bn (EUR 94.8bn placed vs. EUR 118.5bn retained) y-o-y a slight increase (- 12.8%). In HY2/2023 a volume of EUR 82bn was issued, compared to EUR 652bn in the US. In Q1/2024 EUR 60.7bn was issued in Europe, an increase of 69% compared to Q1/2023.

Following a strong dip in issuance during the initial phase of the pandemic, the market has struggled to recover to its previous levels, especially in 2023. While 2022 saw volumes of EUR 29.3bn, close to those of 2021 (EUR 28.4bn), this activity was primarily driven by a surge in Q4.

SMESec issuance remained particularly weak throughout 2023 and into 2024. As shown in Figure 31, there was no SME securitisation activity during the first three quarters of 2023, with only a modest EUR 4bn recorded in Q4. This level of issuance is far below historical trends.

²³ If not flagged otherwise, the data source is AFME, the Association for Financial Markets in Europe. Please note, AFME changed sources of securitisation data. Historical data (i.e., data reported prior to Q1/2020) might be not comparable with current data. Moreover, collateral type categorisations have been subject to changes.

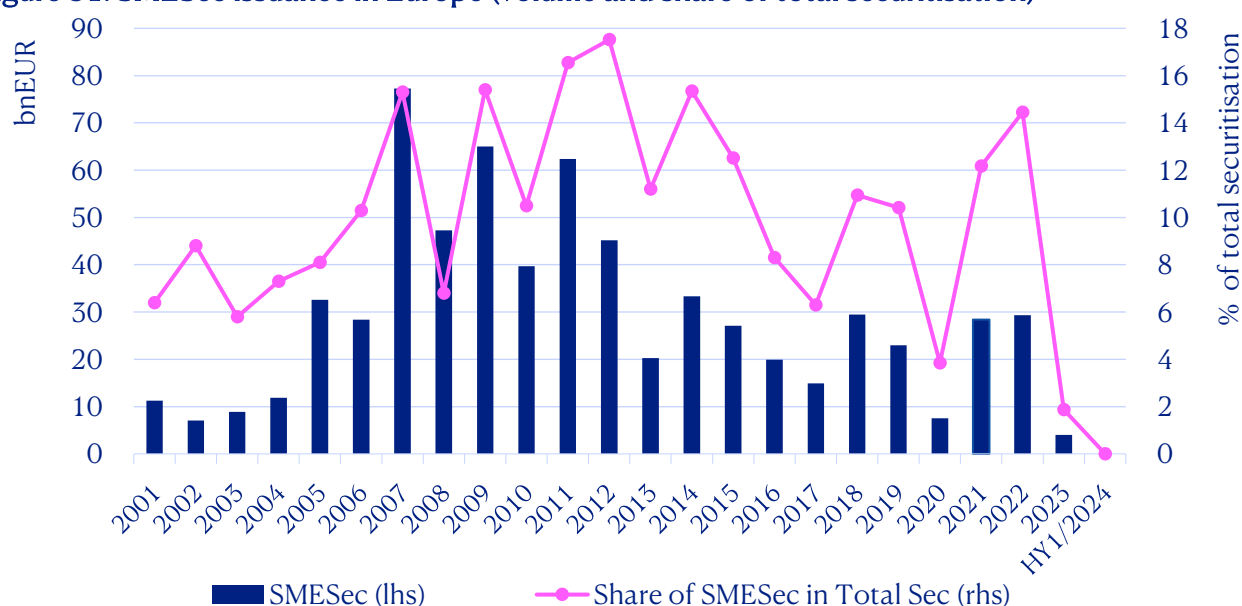
²⁴ The ECB's asset repurchases or "repo" facility allows (among other assets) Asset Backed Securities to be used as collateral for funding.

However, this momentum did not carry into 2024, as no SME securitisation activity was registered in Q1 2024.

While the official figures show minimal activity in SME securitisation, it is important to highlight the rise in synthetic SME transactions, such as unrated bilateral deals, which are not captured in these statistics. These synthetic deals have become a significant alternative financing source, especially as true sale transactions remain largely absent. This shift in the market suggests that while traditional SME securitisation remains subdued, alternative forms of securitisation continue to play a role in supporting SME financing.

Typical originators of traditional SMESec - also often active as repeat originators - are large banks or banking groups – some of them are active as originators in several countries, but also mid-sized banks. In the field of leasing, non-bank asset finance providers are also active as originators. Typical originators of synthetic securitisation are credit institutions, in particular large/systemically important banks using internal rating-based models for calculating capital requirements. However, recently also some standardised banks, including “non-traditional” jurisdictions (e.g. Central and Eastern Europe), have stepped into synthetic transactions, based on support given by the EIB/EIF and in response to the introduction of the SEC-SA (Standardised Approach) risk weight approach under the new EU securitisation framework (EBA, 2020).

Figure 31: SMESec issuance in Europe (volume and share of total securitisation)



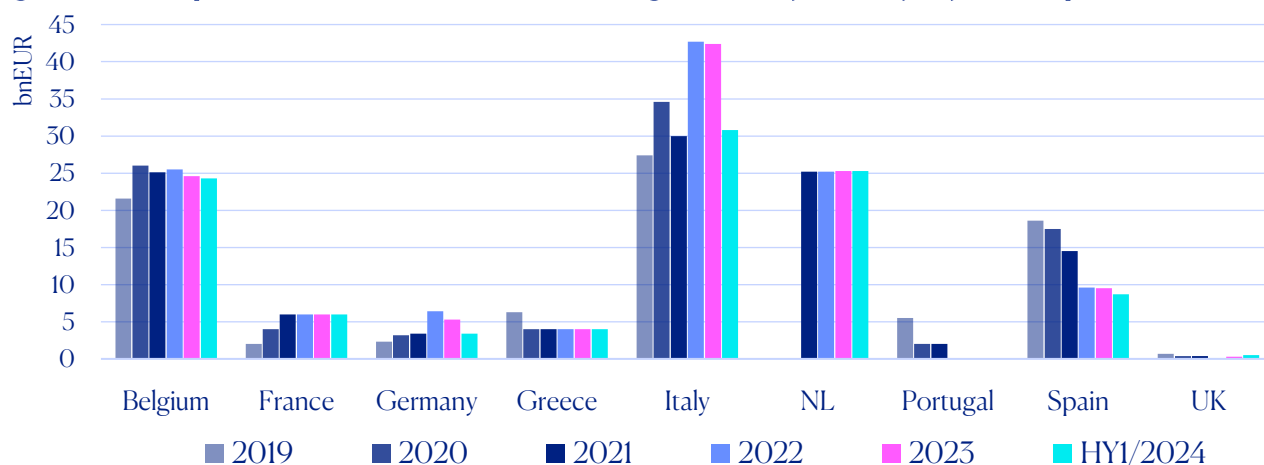
Source: AFME, authors' calculations

Outstanding

At the same time, the European market is lacking investors - due to various reasons, e.g. return expectations that cannot be met, lack of attractiveness for insurers (driven by Solvency II), or extensive due diligence requirements.

Breaking down SMESec volumes per end of HY1/2024 by country shows that the main three countries together represent almost 80% in terms of outstanding: Italy, Belgium, and the Netherlands (see Figure 32).

Figure 32: European true sale SMESec outstanding volume by country (by end of period, bnEUR)



Source: AFME, authors' calculations

SMESec performance trends

The performance of SMESec transactions is influenced by several factors, including transaction structure (such as embedded protections like excess spread), SME credit risk (e.g., recovery rates), portfolio composition (e.g., rating distribution, obligor concentration, industry concentration), and macroeconomic conditions. Although faced with financial and sovereign crises and prolonged economic challenges, the European securitisation market has shown strong resilience, with relatively low default rates in both true sale and public synthetic balance sheet transactions.

Prior to the financial crisis, SMESec volumes were small relative to the overall securitisation market, leaving limited time for the market to fully develop. However, this limited track record also contributed to the relatively conservative structures of SMESec transactions, which partly explains their stronger performance in Europe compared to other European securitisation segments and the US market.

After the financial crisis, the positive performance of SMESec transactions continued, even amidst worsening economic conditions driven by political event risks and the pandemic. Performance remained stable, although in January 2024, the performance of European SME ABS slightly

deteriorated compared to the previous year. However, cumulative defaults improved, falling to 1.38% from 1.44% (Moody's, 2024).

Overall, the performance of structured finance in Europe has been robust, with securitisation funds supporting diverse economic activities. However, despite these solid performance metrics, the recovery in European securitisation issuance remains slower than in the US (Moody's, 2024).

5.2.2 | SMESec prospects

SMEs are especially vulnerable to higher costs/inflation and supply chain disruptions, hence the collateral forecast for most SMESec markets was already negative before the start of the Russian war against Ukraine, varying across countries and sectors (see, e.g. Moody's, 2022, 2023a).

The economic uncertainty driven by uneven recovery from the Covid-19 crisis and the phase-out of public economic support schemes has been exacerbated by rising interest rates and geopolitical tensions, including the ongoing Israel-Hamas conflict. These conditions amplify financial stress on SMEs while also increasing investors' appetite for higher yields.

SME default rates are increasing in general – with related impact on SMESec portfolios. Following the Covid-19 crisis, with massive public support for SMEs, insolvencies in most European countries are rising – reflecting economic reality in an environment of inflation, rising interest rates, and overall difficult macroeconomic conditions.²⁵ Also, payment moratoria might affect SMESec portfolios. Moreover, SMEs' leverage increases with potential long-term debt affordability issues, especially in case economies experience a slow recovery from current disruptions. Despite the rising default rates in Europe, according to Moody's (2023a), the performance of EMEA SMESec transactions was overall positive (as per early 2023). Moreover, the implementation of the EU restructuring and insolvency framework²⁶ in many European countries (including the largest four: France, Germany, Italy, and Spain) is seen to be credit positive for European SMESec (Moody's, 2023b).

As described, even years after the financial crisis, the European SMESec market had not recovered – and it is now negatively affected by the economic effects of the series of new economic shocks. Several direct and indirect support measures are aiming at a market revival, amongst which are important regulatory adjustments.

The existing regulatory and prudential framework in Europe is a major obstacle to securitisation growth, especially when compared to less stringent frameworks in jurisdictions like the U.S. European rules impose high capital charges on securitisation tranches for banks and insurers, which reduces the attractiveness of these instruments. Additionally, complex reporting requirements and stringent due diligence add administrative burdens that further deter market participation. Addressing these regulatory constraints, the European Commission is urged to

²⁵ See Brault (2023) for a detailed analysis of recent trends in EU corporate demography.

²⁶ EU Directive on Restructuring and Insolvency of 20 June 2019 (2019/1023). The directive will help SMEs avoid early bankruptcies by facilitating restructuring plans and will harmonise restructuring frameworks.

evaluate supply- and demand-side limitations in the securitisation market, including reviewing the adequacy of prudential treatment for banks and insurers and simplifying reporting and due diligence requirements to encourage broader market participation (Noyer et al, 2024).

Reviving the securitisation market aligns with the goals of the Capital Markets Union (CMU), which seeks to enhance funding channels and diversify financing sources across EU Member States. The CMU emphasises securitisation as a vital tool to support lending capacity and transfer risk from banks to investors. There is a growing political consensus around securitisation's potential role in stabilising the European economy by easing credit constraints and promoting economic resilience.

Recognizing this, the European Central Bank's Governing Council issued a statement on 7 March 2024, underscoring the role of securitisation in transferring risks away from banks to enable greater lending to the real economy while creating new opportunities for capital markets investors²⁷. Shortly thereafter, on 11 March 2024, the Eurogroup also emphasised the importance of reviving the European securitisation market to promote a more robust and efficient financial ecosystem²⁸.

To ensure the securitisation market's revival, regulatory adjustments must be expedited. This includes a proposed rebalancing of capital charges, allowing banks and insurers to benefit from securitisation without excessive prudential penalties. There is also advocacy for creating a European securitisation platform to pool costs and streamline securitisation processes. The platform would support small- to mid-sized institutions, enabling broader market participation and liquidity. Rapid regulatory changes and the establishment of a securitisation platform could increase lending capacity, particularly vital for addressing Europe's digital and green transition financing needs. This alignment with the CMU would foster a resilient and integrated capital market, making securitisation an effective tool for channelling funds into the real economy. In addition, the CMU-driven measures and regulatory adjustments are expected to strengthen the EU securitisation market, enabling it to better support the EU's green and digital transitions and economic resilience objectives by channelling more funds into the real economy (Walter, 2024).

Integrated EU capital markets and the relative complexity of securitisation techniques require significant expertise and highlight the necessity for specialised institutions. As a respected player in the European securitisation market, the European Investment Fund (EIF), in close cooperation with the European Investment Bank (EIB), plays an important role through market presence, reputation building, and signalling.

²⁷ [Statement by the ECB Governing Council on advancing the Capital Markets Union](#)

²⁸ [Statement of the Eurogroup in inclusive format on the future of Capital Markets Union - Concilium](#)

6 | Inclusive finance

6.1 | Microfinance and social inclusion

6.1.1 | What is Microfinance?

Microfinance is traditionally defined as the provision of essential financial services to microenterprises and individuals who aim to start or expand their own businesses or income-generating activities. It is often complemented by business development services, such as mentoring, training, and coaching.

The main achievement of microfinance is to reach unbanked²⁹ clients; however, in some European countries, bankability is no longer a serious issue. Introducing the concept of Inclusive Finance in Europe, therefore, became a logical continuation of microfinance. Inclusive finance complements microfinance by directly financing vulnerable groups and offering financial and non-financial products to enterprises that employ or serve them.

Inclusive Finance is the range of financial and non-financial products and services provided to unemployed people or clients from other vulnerable groups who are facing difficulties in accessing the conventional banking services, due to their socioeconomic status, and more broadly to social enterprises who provide work-integration opportunities or services to groups deemed vulnerable from a socioeconomic standpoint. Inclusive finance promotes entrepreneurship and social inclusion, by providing support to micro-enterprises and social enterprises.

In Europe, microfinance consists mainly of small loans (less than EUR 25,000) tailored to microenterprises and people who aspire to be self-employed but face difficulties in accessing the traditional banking system, while inclusive finance also serves social enterprises and provide loans up to EUR 500,000. There are many overlaps between the target groups of microfinance and inclusive finance, therefore, both groups are combined in this chapter.

²⁹ In the context of microfinance, unbanked people are considered those who have limited access to financial services: people who do not have an account with a financial institution due to insufficient funds, cost, distance or lack of necessary documentation.

6.1.2 | A support tool for business and job creation

Mapping target groups for microfinance and inclusive finance is challenging. To grasp the magnitude of the market, we look at some important indicators related to unemployment, poverty and social exclusion, entrepreneurial motivation and intentions. These indicators are particularly important to analyse the market for potential entrepreneurs, as a combination of poor labour market prospects and poverty drives people to start new businesses or even create jobs.

In the context of the Europe 2020 social inclusion targets, Eurostat published the “people at risk of poverty or social exclusion” indicator, depicted in Figure 33. The indicator corresponds to the sum of individuals who are at risk of poverty, severely materially deprived, or living in households with very low work intensity.³⁰ In 2023, more than one fifth of EU-27 citizens were at risk of poverty and social exclusion, with the highest rates recorded in some Eastern and Southern European countries (Romania, Bulgaria, Spain, Greece).

Europe 2020 aimed to ‘lift at least 20 million people out of the risk of poverty or social exclusion’ by 2020 compared to the year 2008.³¹ From 2019’s estimations, no more than 12 million managed to escape the risk of poverty and social inclusion since 2008 (Eurostat data). Achieving the target became even more impossible due to the Covid-19 crisis, which left additional 3

Definitions for Microfinance and inclusive finance

A microenterprise: an enterprise with fewer than 10 employees and a turnover below EUR 2m (as defined in the Commission Recommendation 2003/361/EC of 6 May 2003, as amended).

A social enterprise: an operator in the social economy whose main objective is to have a social impact rather than make a profit for its owners or shareholders, while operating in a market-driven environment (as defined by European Commission, 2011).

A microfinance institution (MFI): an organisation/ financial intermediary that provides microfinance services. There is a wide spectrum of different MFI business models in Europe.

Microcredit in general is defined by the European Commission as a loan or lease under EUR 25,000 to support the development of self-employment and microenterprises. It has a double impact: (1) an economic impact, as it allows the creation of income generating activities, and (2) a social impact, as it contributes to the financial inclusion and, thus, to the social inclusion of individuals.

Microenterprise lending: micro-lending to existing enterprises. MFIs focus on the upper end market of microfinance, providing loans to bankable or nearly bankable microenterprises that have difficulties accessing loans up to 25,000 EUR from commercial banks due to risk aversion or lacking liabilities.

Social inclusion lending: lending to self-employed individuals that are excluded from banking services, due to their socioeconomic status of being socially excluded or (long-term) unemployed and/or belonging to financially excluded population groups like ethnic minorities or young people. The average loan sizes are relatively low, meant to support basic income creating activities.

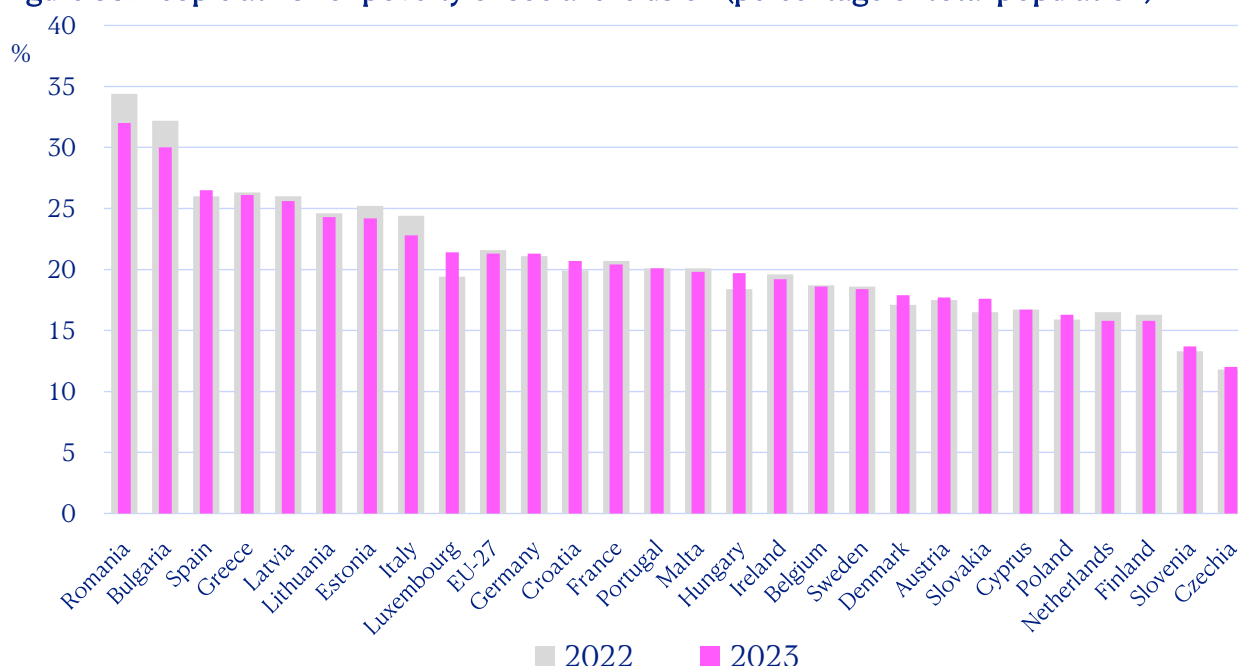
³⁰ At risk-of-poverty are persons with a normalised disposable income below the risk-of-poverty threshold, which is set at 60% of the national median normalised disposable income (after social transfers). For more information please see:

http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&plugin=1&language=en&pcode=t2020_50.

³¹ Furthermore, the indicator is part of the impact indicators of the Strategic plan 2016-2020, referring to the 10 Commission priorities, and included as main indicator in the Social Scoreboard for the European Pillar of Social Rights. It can be considered similar to the global SDG indicator 1.2.2 “Proportion of men, women and children of all ages living in poverty in all its dimensions according to national definitions”.

million people below the risk-of-poverty threshold in 2020. The consequences of the Russian aggression against Ukraine, in particular food and energy inflation further hit the poorest. Some countries managed to achieve their national targets, progressing toward greater equality. The most distinct improvements were made by Poland, Hungary, Romania and Bulgaria, mainly due to falls in material deprivation. On the other hand, Spain and Italy, but also Germany, France and the Netherlands regressed compared to 2008. Europe set a new target of reducing the number of people at risk of poverty or social exclusion by at least 15 million by 2030.

Figure 33: People at risk of poverty or social exclusion (percentage of total population)

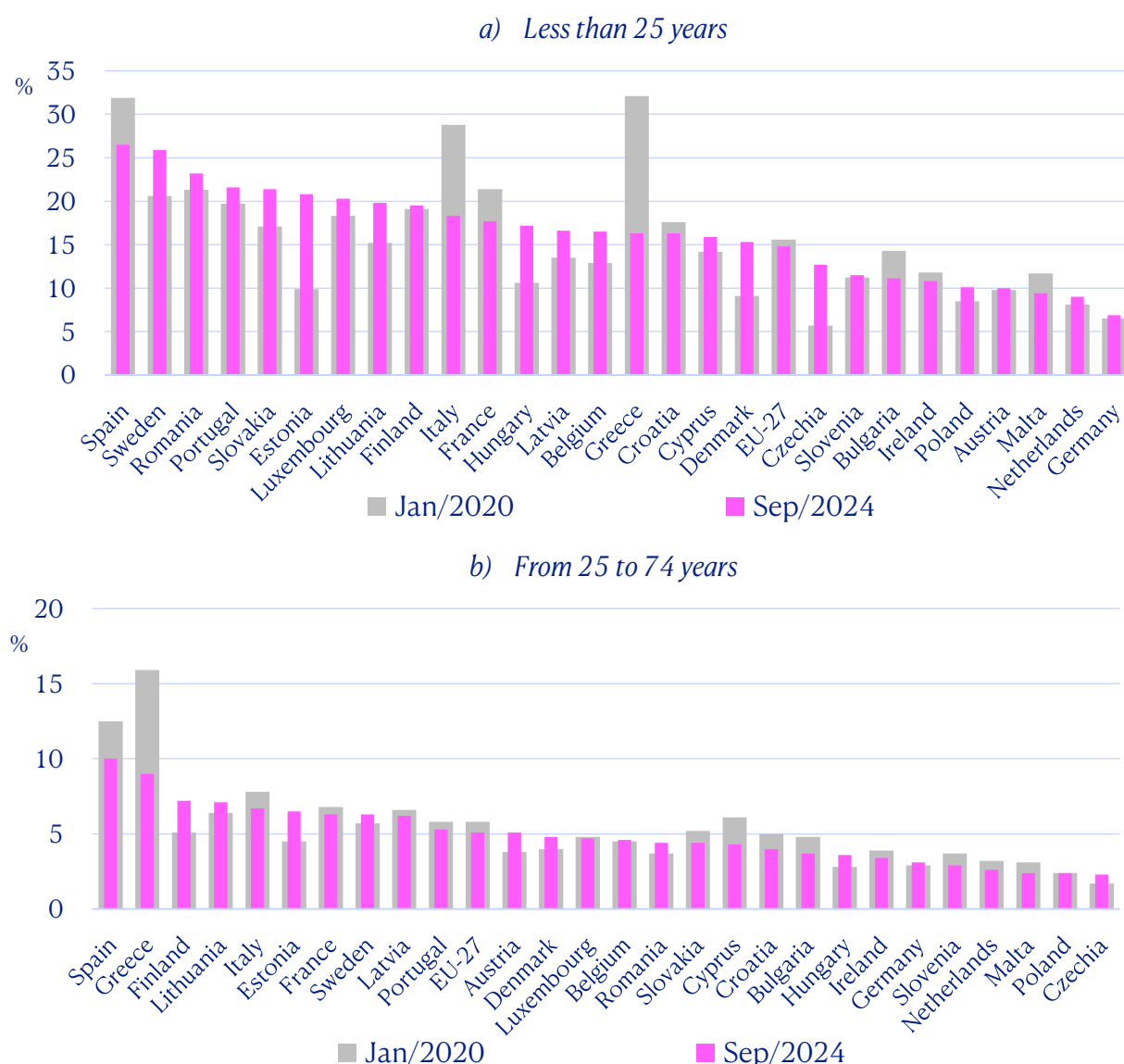


Source: Eurostat, authors' calculations

Figure 34 plots the unemployment rate for European countries. In 2022, labour market conditions improved, partly due to the easing of pandemic-related restrictions and workers transitioning out of job retention schemes. This trend continued throughout 2023, paving the way for the EU unemployment rate to reach a record low in 2024. Youth employment rebounded to pre-pandemic levels, achieving a new low of 14% in 2022, before rising slightly to 14.8% in 2024. Consequently, the employment rate gap between young individuals (under 25 years) and older cohorts has widened again in 2024, reversing some of the convergence seen since 2020.

People at risk of poverty and those unemployed are a significant group of potential business founders, as the need to start a business often arises from necessity, particularly in low-income countries. The Global Entrepreneurship Monitor (GEM) notes that a lack of jobs can push people towards starting their own businesses (Figure 35). Another common reason to embark on a business venture, especially in low-income countries, is the desire to build wealth or achieve a high income.

Figure 34: Unemployment rate by age groups (2024)



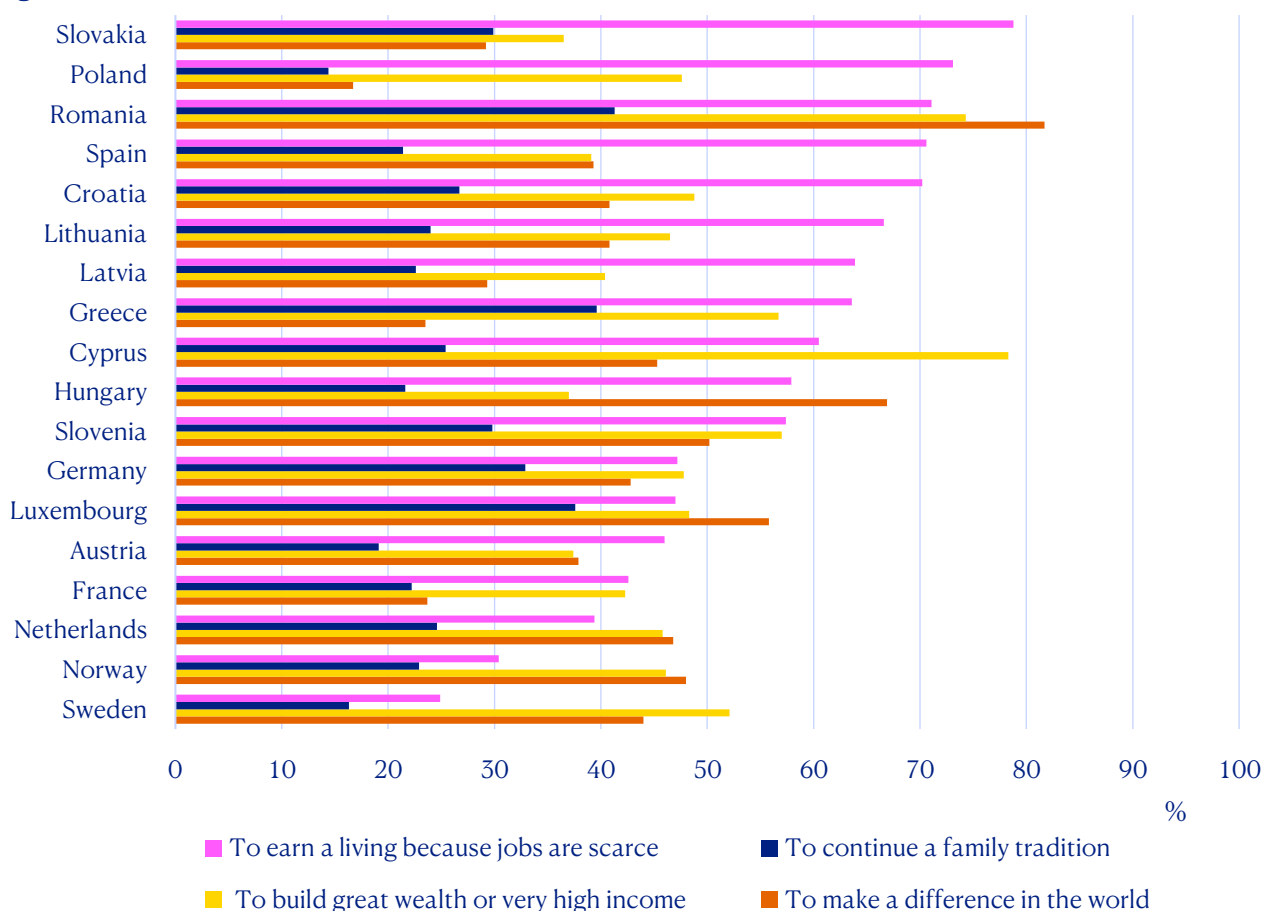
* No recent unemployment data was available for Italy (from September 2023).

Source: Eurostat, authors' calculations

In Hungary, Romania, Lithuania and Greece the drive to earn a living due to limited job opportunities is the predominant reason for starting a business, pointing to entrepreneurship born out of economic necessity in these regions. In contrast, in countries like Luxembourg, Germany and the Netherlands to make a difference in the world is a strong motivating factor.

The goal of creating significant wealth or high income, while notable in low-income countries, does not emerge as a top motivation in the European setting, implying a reduced emphasis on financial gain as the main entrepreneurial goal. Further, the aim to continue a family tradition ranks as the least common reason for starting a business in the surveyed countries, indicating a move towards more personal and socially conscious entrepreneurial motivations.

Figure 35: The motivation to start a business, 2023*



* Somewhat/strongly agree as % Total [early-stage] Entrepreneurial Activity (TEA), multiple answers are possible.

Source: GEM (2024), authors' calculations

In addition to creating employment or tackling other social challenges, many small businesses consider the environmental implications when making decisions about the future of their business. New entrepreneurs are also likely to expect to use more digital technologies in order to sell products and services in the next six months (GEM, 2024).

The impact of the Covid-19 crisis lingers, particularly affecting the most vulnerable groups in the labour market. This situation worsened due to the war in Ukraine and increasing food and energy prices. Those in unstable, low-paid, and part-time jobs were the first and most severely affected. Freelancers and self-employed individuals also experienced a significant reduction in their activities due to the lockdowns. Although self-employment has returned to pre-pandemic levels for some groups, there remains a significant number of 'missing' entrepreneurs, resulting in a loss of potential ideas, innovation, and jobs for economies (OECD, 2023). In a similar vein, social enterprises, which typically focus on social inclusion, suffered during the Covid-19 crisis with business closures, decreased sales, and challenges in reaching their target groups in person. They also faced obstacles in securing long-term financing (Dupain et al, 2022).

6.2 | The demand for microfinance

According to the ECB's SAFE survey, microenterprises use less external financing instruments than their larger peers, presumably due to difficulties in accessing finance (Figure 36). For example, bank loans are used by 15% of small companies and 22% of medium companies, while only 10% of microenterprises used bank loans. Notably, more than 43% of the microenterprises indicated that bank loans are relevant sources of financing, far exceeding the rate at which they use it. Conversely, 57% of the microenterprises considered bank loans not to be a relevant source of financing. Microenterprises indicated that too high interest rates or price were the most important reasons bank loans were considered irrelevant.

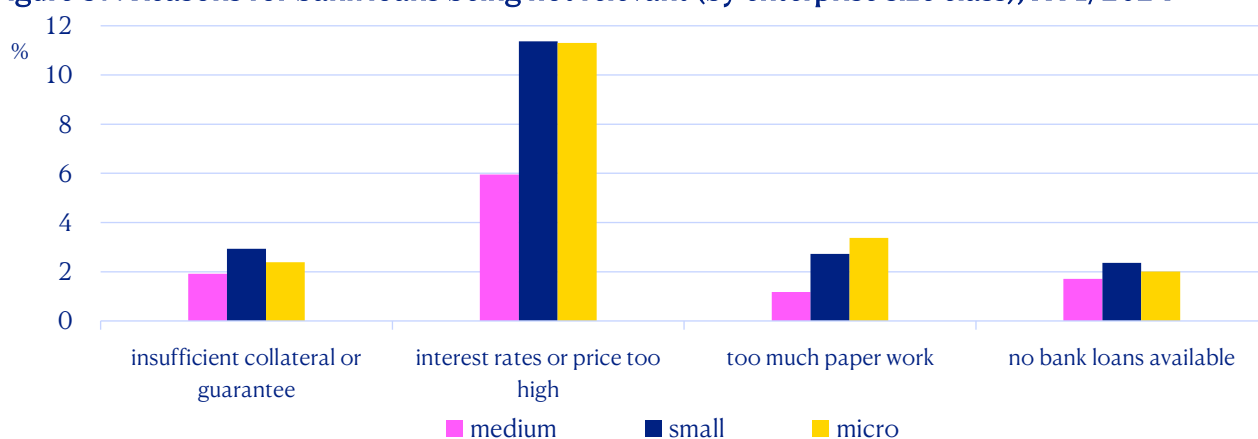
Figure 36: Relevance and use of different financing sources for microenterprises (HY1/2024)



Source: ECB SAFE (ECB, 2024), authors' calculations

The same survey states that the bank loan rejection rate reached record high in HY1/2024 at 18% (compared to 5% for small firms and 4 % for medium-sized firms). Consequently, the share of microenterprises that did not apply for a loan due to fear of rejection (discouraged borrowers) has increased to 7% (from 6% in H1/2023).

Figure 37: Reasons for bank loans being not relevant (by enterprise size class), HY1/2024



Source: ECB SAFE (ECB, 2024), authors' calculations

As microenterprises do not frequently use bank loans due to insufficient collateral, high interest rates and excessive paperwork, rejected or discouraged customers often turn to an alternative solution: microcredit from microfinance institutions (MFI). MFIs do not always charge lower interest rates than banks, but they are less demanding in terms of collateral and guarantee requirement. Clients find MFIs more personal, tailor-made and simple; MFIs “know their customers”.

6.3 | The supply of microfinance: green and digital transformation

The microfinance market in Europe is highly fragmented and diverse, with no common business model. Part of this fragmentation has geographical roots, as the role of microfinance is seen very differently across Europe. In Western Europe, microfinance is seen as a social policy tool, serving businesses that, while not commercially attractive to mainstream financiers, create social value. On the other hand, in Eastern Europe, microfinance is seen more as a business activity, which targets viable microenterprises that are financially excluded because the traditional credit market remains underdeveloped.

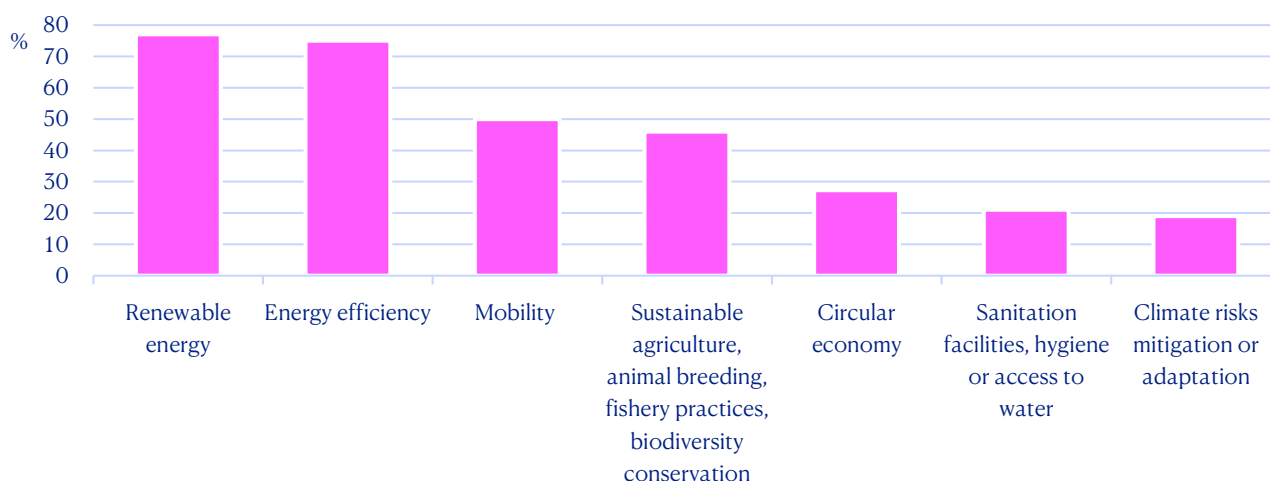
The microfinance landscape in Europe has continued to evolve and expand. The latest EMN market survey data show that by the end of 2022, the gross microloan portfolio reported by 156 microfinance institutions (MFIs) had grown to EUR 5.3 billion, serving approximately 1.3 million borrowers. The business microloan portfolio accounted for 74% of the total portfolio volume, while personal microloans represented 26%. In addition to financial products, a vast majority of MFIs (76%) also offer non-financial services.

European microfinance providers

European microfinance providers are very diverse across Europe. In addition to commercial banks that target microenterprises as part of their general SME lending activity, the spectrum of European microcredit developers includes many profit-oriented and non-profit associations: banks (both private and state-owned), non-bank financial institutions (NBFIs), microfinance associations, credit unions, cooperatives, government bodies, religious institutions and Non-Governmental Organisations (NGOs).

Green finance: In the current landscape of European microfinance, the sector has shown a commitment to contributing to the green transformation, aligning with broader initiatives in SME finance. Green finance is receiving growing interest, with 28% of MFIs offering dedicated green products and 29% providing them through standard offerings. However, 45% of MFIs still do not provide specific green microloans. Those offering green finance are focused on renewable energy and energy efficiency solutions, with 77% and 75% of MFIs engaged in these areas, respectively (see Figure 38). Other significant areas include sustainable agriculture and mobility, (EMN-MFC, 2024).

Figure 38: Purpose of green loans (2022)



Source: EMN-MFC, (2024)

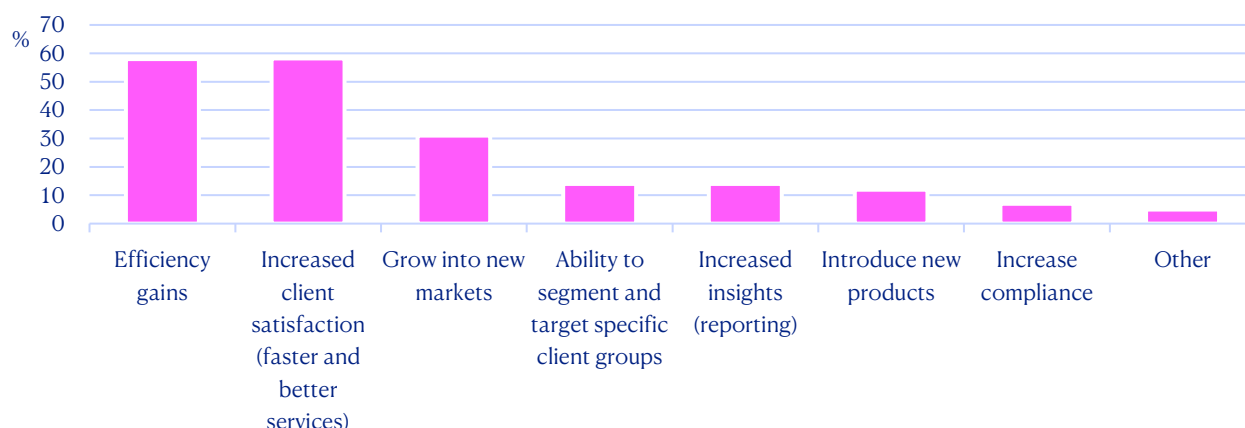
There is a significant portion of the sector engaged in training clients on green practices and connecting them with providers of green technologies. This indicates a strategic move towards not only providing financial support but also empowering clients to adopt and maintain green practices.

MFIs are encountering several key challenges in the green transition. Firstly, there's a noticeable lack of awareness among their clients about climate change vulnerability, coupled with a reluctance to adopt green technologies. Although often costly, these technologies are seen as worthwhile investments. Another major hurdle is the difficulty in developing new green financial products or adapting existing ones to be more environmentally friendly.

To address these challenges, MFIs are seeking support on multiple fronts. They primarily require technical assistance to innovate and create green financial products. Additionally, they need guarantees to broaden their reach to clients who are more vulnerable to climate risks. Further, extra funding is crucial for disbursing a greater number of green loans. Finally, MFIs are looking for grants and subsidies to enhance their provision of non-financial services, further supporting their clients in the transition to green practices (EMN-MFC, 2024).

Digitalisation: The integration of digital capabilities is a pivotal component of the strategic planning for European MFIs, with 74% of institutions considering it a critical element of their 3-to-5-year strategy. This emphasis on digitalisation is aimed at achieving significant operational improvements, specifically to enhance client satisfaction and to streamline internal processes for better efficiency (Figure 39).

Figure 39: Two key aims achieved with digitalisation



Source: EMN-MFC (2024), authors' calculations

Digitalisation strategies are not without their challenges, however. MFIs are grappling with high investment costs, cited by 66% of the institutions as a primary concern. Additionally, recruiting IT experts to lead these initiatives poses a challenge for 34% of the MFIs. Resistance to digital transition, both from clients and internal staff with limited capacity to utilise advanced systems, is another significant hurdle.

Despite the challenges, MFIs are committed to leveraging digital transformation to expand into new markets and gain deeper insights into client needs. This proactive approach is not just about keeping pace with changes, but about redefining how services are delivered and operational efficiency is achieved, aligning with the larger financial sector's push towards digital innovation. To realise these ambitions, MFIs require substantial funding for IT investment and development, given the high costs involved. Additionally, there's a need for technical assistance to develop digital strategies and to enhance the digital skills of their staff. Similar to the needs for green transformation, grants and subsidies are essential for providing non-financial services to clients, especially those with limited digital skills.

Furthermore, the funding needs of MFIs extend beyond green and digital transformations to include the provision of support to vulnerable population segments, central to the mission of microfinance. Primarily, MFIs are in search of borrowed funds, which continue to be the main source for financing their loan portfolios. The most frequently requested amount is more than EUR 10 million. When it comes to equity, MFIs generally look for smaller amounts, with the most frequently cited range being between EUR 1-5 million. This financial support, coupled with technical assistance, is key to enabling MFIs to reach and serve those most in need, thus fulfilling their fundamental objectives.

7 | Conclusion and discussion

SMEs remain central to Europe's economic resilience and growth, but persistent barriers to finance and competitiveness continue to constrain their growth and innovation potential. While some improvements in access to finance have been observed, high borrowing costs, limited equity uptake, and fragmented markets hinder their ability to compete globally. Strengthening SME competitiveness through targeted financial instruments, fostering innovation, and enhancing public-private collaboration is essential to building a resilient and inclusive SME ecosystem capable of driving sustainable economic growth in Europe.

Following several years in a row during which the *PE/VC market* activity almost continuously reached new record highs, the European PE/VC ecosystem has been come under pressure by the combined effects of the Russian war of aggression against Ukraine, the subsequent geopolitical disruptions and the difficult macroeconomic environment. EIF survey respondents reported important challenges for their investees in 2024, particularly with regard to securing equity financing. At the fund level, alongside recurring challenges, they also described a very difficult exit environment and severe fundraising issues, while expectations for the coming months have become more optimistic. Particular concerns were raised with respect to scale-up financing. Overall, this suggests a need for continuous analysis of the market requirements and for a strong policy response in support of the European PE/VC markets and its final beneficiaries, the European enterprises.

The EIF's aim is to support the European PE/VC market in order to establish a well-functioning, liquid equity environment that attracts a wide range of private sector investors. In doing so, the EIF aims at leveraging its market assistance and seizing market opportunities in all areas of the equity eco-system which are relevant to the sustainable development of the industry. EIF's role as a counter cyclical investor remains of crucial important to support the market in light of the current challenges. In the coming years, the EIF will continue to act as a cornerstone investor across the spectrum of Technology Transfer through venture capital (incl. impact investing) to the lower mid-market and mezzanine financing. This also includes the launch and extension of new/pilot initiatives.

Increased investment in equity funds, combined with co-investment initiatives or subordinated debt/quasi-equity (including first-loss provisions), can attract greater private sector capital and enhance the bankability of higher-risk projects. Some of these products can address niche or region-specific market gaps and investment needs or can act as a catalyst to enable and accelerate strategic investment and can be combined with tailored advisory support.

After the Covid-19 pandemic, guarantee instruments surged at national and European levels to address urgent corporate liquidity shortages. However, these extensive support programmes have been gradually phased out. In 2023, the total outstanding guarantee volume and the number of outstanding guarantees declined further. The volume of newly-granted guarantees for the full year of 2023 decreased by 8% compared to 2022, marking a notable improvement compared to the sharp decline in 2022, when it nearly halved relative to 2021. This, in turn,

translated into a total outstanding guarantee volume of approximately EUR 206bn in 2023, representing a 23% decrease compared to 2022. Despite this significant drop, the volume of total outstanding guarantees remains well above the pre-pandemic level.

The European *SME securitisation* market also bears the consequence of the ongoing polycrisis. Before the outbreak of Covid-19, SMESec issuance was still suffering from the after-effects of the financial crisis – and continued to suffer during the first year of the pandemic. SMESec issuance remained very weak throughout 2023 and into 2024. Despite this, synthetic SME transactions, such as unrated bilateral deals not captured in official statistics, have gained prominence as an alternative financing source. This shift indicates that while traditional SME securitisation is subdued, alternative forms of securitisation are playing an increasing role in supporting SME financing.

In the areas of credit guarantees and securitisations, the EIF cooperates with a wide range of financial intermediaries, such as banks, leasing companies, guarantee funds, mutual guarantee institutions, promotional banks, and other financial institutions that provide financing or financing guarantees to SMEs, such as debt funds. Given that SMEs have no direct access to the capital markets, banks are typically the most important source of external SME finance. Hence, funding limitations of banks have direct impact on SME lending capacity. For loans to SMEs, a standardised, transparent and quality-controlled securitisation market could transform these illiquid loans into an asset class with adequate market liquidity.

Microenterprises and social enterprises play a critical role in job creation and social innovation, particularly in European regions with high unemployment. Given the diverse landscape of inclusive finance across the EU, the EIF provides funding, guarantees, and technical assistance to a wide range of financial intermediaries, including non-bank microfinance institutions, fintech lenders, crowdlending platforms, promotional institutions, alternative lenders, cooperative banks, and, to a limited extent, commercial banks. These intermediaries, particularly microfinance institutions (MFIs), address the unique challenges faced by microenterprises and social enterprises by offering both microcredit and non-financial services. MFIs are increasingly aligning with green and digital transformation goals, focusing on renewable energy, sustainable agriculture, and operational efficiency, while overcoming challenges like high costs, limited client awareness, and capacity constraints. To expand their reach and impact, MFIs require significant funding, technical assistance, and grants to develop innovative financial products and better support vulnerable populations. Continued support from the EIF is essential to strengthening the microfinance sector and ensuring its contributions to social inclusion, sustainability, and economic resilience.

The EIF's activities are aligned with the EIB Group 2024–2027 Strategic Roadmap and the key policy objectives of the new European Commission, contributing significantly to advancing Europe's strategic priorities. Within the Strategic Roadmap framework, the EIF focuses predominantly on areas where its impact can be the greatest, such as Climate Action, digitalisation and technological innovation, cohesion, and advancing the Capital Markets Union.

Climate Action and Environmental Sustainability finance remain at the core of the EIF's strategic objectives for 2025–2027. Building on the mandates and products successfully launched during 2022 and 2023, the EIF will continue to support Europe's green transition while prioritising investments that enhance competitiveness and cleantech financing.

The EIF aims to scale up its support for innovative start-ups and scale-ups through its contributions to the EIB Group Tech-EU Programme. By leveraging its venture capital, private equity instruments, and guarantees, the EIF seeks to bridge gaps in the company and innovation growth cycle, particularly in start-up and scale-up funding, which remains a critical challenge. These efforts will not only help close the innovation gap identified in the Draghi Report³² but will also enhance productivity and the global competitiveness of European businesses.

The EIF plays a vital role under the EIB Group Capital Markets Union Action Plan, particularly in closing funding gaps throughout the company and innovation cycle. To crowd in private sector investment, the EIF will open parts of its well-diversified VC/PE portfolio to external investors through secondary sales. These sales will unlock public resources, allowing the EIF to do more with limited public funds by reinvesting proceeds into equity investments. Furthermore, the EIF will explore possibilities to engage retail investors, further enhancing the capital market ecosystem.

The EIF's strategy emphasises long-term planning to address systemic challenges and seize emerging opportunities. Beyond advancing green and digital transformation goals, the EIF prioritises improving operational efficiency, strengthening impact measurement, and fostering deeper collaboration with stakeholders. By adopting a sustainable capital management approach, the EIF ensures resources are allocated effectively to maximise impact. This integrated strategy reinforces the central role of SMEs in Europe's economic and climate transitions, ensuring they remain pivotal in building a resilient, inclusive, and climate-neutral future.

³² [EU competitiveness: Looking ahead - European Commission](#)

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