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Pilot Action 1 Summary report

P6 FhG-IMW

SUMMARY OF THE PROPOSED FINANCIAL INSTRUMENT

The basic idea of the presented innovative financial instrument (IFI) is to combine one of the three types of crowdfunding suited for business activities with one of the established forms of public funding, namely subsidies and promotional loans.

In theory, this means six possible combinations, each of which has some advantages. However, regarding our research and analysis the most suitable combination in this case is the combination of lending-based crowdfunding with a subsidy. From here on we will refer to this combination as **match lending**.

Based on our empirical assessment and desktop research, two of the major problems for small and medium-sized enterprises (SMEs) with public funding are the **complex regulations** and the **challenging conditions/ requirements** among the many current funding instruments. Finding a subsidy for a specific investment project and examining the corresponding requirements of the subsidy is often a laborious and time-consuming task, because of a large number of small-scale funding instruments. The required time and expertise are frequently not sufficiently available especially in small but also in medium-sized enterprises. Consequently, investment initiatives to implement energy efficiency measures are being nipped in the bud. An effective innovation promoting financial instrument must, therefore, be easily accessible to a wide range of different investment initiatives.

Furthermore, certain proximity of the financial instrument to the capital market is desirable. On the one hand, to make use of its **efficiency** in the **allocation of financial resources** and on the other, to be able to acquire **additional private** funds for achieving the promotional objective. These requirements are well-matched by the promoted match lending. Lending based crowdfunding is easily accessible for a wide range of different enterprises. The requested documents are not few, but similar to those required by banks and therefore mostly already available.

The problem here is that investment projects to improve energy efficiency are often not competitive on the capital markets as a financial investment and therefore aren't financed. This also applies to finance CO₂-reducing investment projects via lending-based crowdfunding. It is at this point that the advantages of the combination with a subsidy become apparent. The subsidy lowers the risk/return ratio of investment projects to improve energy efficiency which,

in addition to the economic objective, pursues the political goal of reducing CO₂. That way, the investment becomes competitive in the capital market and thus attracts additional private funds.

However, care must be taken to ensure that the risk/return level is raised to a competitive level but does not exceed the level of comparable unsubsidized investments. If this succeeds, the capital market selection process can be used to identify economically efficient and sustainable investments while preventing the funding of inefficient investments.

VALUE ADDED OF THE FINANCIAL INSTRUMENT

The main characteristics of the designed innovative financial instrument is that the crowd lending feature attracts private investments in additional to the public funds.

These private investments in most cases do not come from a few large investors, but from a large number of smaller investors. This is of great importance, since the instrument can make thereby use of the so-called "crowdsourcing". Crowdsourcing is the practice of obtaining information or input into a project by enlisting the services of a large number of people via the Internet. In this case, the service used is the evaluation of the project. Only those who come to the conclusion that their investment pays off in their personal risk/return assessment of the project will invest. Especially for out of the box projects, which are difficult to assess for the authorities, this additional information can be a decision-making aid.

Viewed in this way, match lending is not only co-investment because of the combination of subsidy and another financial source. It`s also co-investing because it stimulates a wide range of private sources to invest cooperatively. In general, but also because it stimulates especially private investments from a number of different sources.

INVOLVEMENT OF STAKEHOLDERS

By the development of the innovative financial instrument, different stakeholders were involved at the diverse stages of the development process. The stakeholder groups are listed below with a short description of their contribution and involvement:

- Regional and local authorities: survey partners as well as for specific discussions during the ex-ante assessment of the available financial instruments in Saxony, Germany, and the market gaps as well as discussion partner regarding the feasibility of the designed innovative financial instrument;
- Financial institutions (banks): interview partner during the ex-ante assessment of the available financial instruments in Saxony, Germany, and the market gaps;
- SMEs - survey partners during the ex-ante assessment of the available financial instruments in Saxony, Germany and the market gaps;
- Owners and operators of crowdfunding platforms – discussion partner by the actual development of the innovative financial instrument and its feasibility;
- NGO – discussion partner for the feasibility of the developed innovative financial instrument.

EXPECTED RESULTS OF THE FINANCIAL INSTRUMENT

The concrete expected results of the innovative financial instrument match lending is difficult to predict due to its innovative but therefore experimental character. On the one hand the market of lending based crowdfunding is still very rapidly but also differently developing in the different countries, thus all forecasts would be subject to unacceptable uncertainty

On the other hand, there aren't many real life examples of this specific combination. Thus there is no sufficient basis for robust, methodologically sound forecasts. For this reason, the expected results of the match lending will be presented as a result of its specifics and characteristics. These could lead to a certain expectation about the feasibility and impact of the innovative financial instrument.

Subsidy as risk minimizing for lending-based crowdfunding: The problem is that investment projects to improve energy efficiency are often not competitive on the capital markets as a financial investment and therefore aren't financed. This also applies to finance CO2-reducing investment projects via lending-based crowdfunding. It is at this point that the advantages of the combination with a subsidy become apparent. The subsidy lowers the risk/return ratio of investment projects to improve energy efficiency which, in addition to the economic objective, pursues the political goal of reducing CO2. That way, the investment becomes competitive in the capital market and thus attracts additional private funds.

Lending-based crowdfunding as replacement of own capital: SMEs do not always have surplus capital to invest in energy efficiency measure, especially when the measures require a high amount of investment. In the case of match lending the whole or part of the own contribution could be replaced with the financial resources from different investors. In this case, the SMEs could be more willing to invest in especially energy efficiency measures with higher financial demand even if they do not have the needed capital as surplus. Another advantage of this innovative financial instrument is that through the lending-based crowdfunding the SMEs do not have to reallocate their own financial resources, when investing in energy efficiency measures. This could stimulate the investment in energy efficiency measures and especially measures with a higher financial demand.

Lending-based crowdfunding as especially appropriate for financing energy efficiency

measures: the topics related to climate change, reduction of CO2-Emission, global warming etc. are very emotional and are gathering more and more attention recently among all the age groups and among all the countries. This fact is crucial for crowdfunding in general, because it is the moving intrinsic motivation for the (private) investors to provide financial resources. In the case of lending-based crowdfunding one more circumstance play a motivation role – the fixed-income rate, which the investors get. Those two facts and the mentioned above reduction of risk because of the subsidy as a combination for this innovative financial instrument are solid basis for on one side the attractiveness of the innovative financial instrument for the SMEs but also on the other side to raise the motivation for investments meaning the value added.

TRANSFERABILITY

From the beginning of the FIRECE-project, there are different activities contributing to the transferability of the project in general and to promote the designed innovative financial instrument (IFI). The different activities are listed below with a short description of its contribution to the transferability of the project respectively the IFI:

- **Organization of workshops and meetings** – two main goals. First, to inform about the projects and its objectives and to transfer the knowledge and project results. Second, to stimulate feedback and firsthand information from the involved and affected stakeholders;
- **Survey** – in form of questionnaires and interviews the involved and affected stakeholders were able to give their opinion on the relevant topics;
- Participation on events – different events with relevant topics and audience were used for discussion with other participants and getting insight from the presentations, on one side, but also to attract the attention to the FIRECE-projects, its goals and results;
- **Contacting other regional projects with similar topic** –there were a scan of the new and current projects with a similar topic in the region at the end of the project. The goal was to find synergies with those projects and the knowledge and results of the soon finalized FIRECE-project to be transferred and further used and developed;
- **Online activities** –relevant information about the FIRECE-project and its results were spread through different online channels, e.g, on the Fraunhofer IMW website, on the website of the group Innovative financing (Fraunhofer IMW), as blog post and sharing the survey on partner's websites as well as within our social media channels (LinkedIn). The goal is to get attention to the FIRECE-project and its results.