The Green Transformation: SMEs, Venture Capital and Investments

Discussion on EIF European Small Business Financing Outlook 2021

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Key messages

1. German SMEs: in light of the twin transformation the decrease in borrowing during the crisis due to investment restraint poses challenges.

2. German VC market still on the upswing: Business climate and deal volume extremely strong in Q3, although still smaller than benchmark markets.

3. In 2020, German SMEs invested EUR 22 billion in climate protection. Driving the volume up would require transparency about climate-relevant properties of projects and access to capital market financing.
German SMEs: in light of the twin transformation the decrease in borrowing during the crisis due to investment restraint poses challenges.
Despite tough sales losses due to COVID-19 pandemic: SMEs robust profitability contributed to rather stable equity ratios.

Wide range of economic policy measure has been effective.

**Profitability of German SME sector**
(ratio of pre-tax profit to turnover, in percent)

**SMEs’ equity ratios by firm size**
(in percent)

![Graphs showing profitability and equity ratios over time.](source: KfW SME Panel 2021)
COVID-crisis further exacerbated the trend of downward corporate investments in Germany.

Corporate investments in Germany (percentage of GDP)

SMEs investments and business expectations

- **Share of investing SMEs**
  - Pessimistic business expectations: 28%
  - Neutral: 38%
  - Optimistic business expectations: 36%

- **Share of capacity expansions**
  - Pessimistic business expectations: 28%
  - Neutral: 32%
  - Optimistic business expectations: 47%

- **Investment volume per FTE-employee (in EUR)**
  - Pessimistic business expectations: 6,355
  - Neutral: 6,989
  - Optimistic business expectations: 9,489

Source: Destatis (left), KfW SME Panel (right)
Financing conditions remained favorable, but volume of bank loans for SMEs investments decreased considerably

Strongly increasing number of smaller investments projects for crisis adaptation

Outcome of SMEs loan negotiations (in percent)

Volume of bank loans (in EUR billions, SMEs total, investments)

Source: KfW SME Panel 2021
German VC market still on the upswing: Business climate and deal volume extremely strong in Q3, although still smaller than benchmark markets.
German Venture Capital business climate sets new record in 3rd quarter – Private equity business climate stagnates after regaining positive values

Business climate with deep dive after corona outbreak: VC market has left gloom behind quickly, strain on PE sentiment more protracted

Overview of climate components shows positive picture

<table>
<thead>
<tr>
<th>Venture Capital</th>
<th>Private Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q3</td>
<td>Δ vs. Q2/21</td>
</tr>
<tr>
<td>Business climate</td>
<td>+42.2</td>
</tr>
<tr>
<td>Business situation</td>
<td>+41.5</td>
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<tr>
<td>Business expectations</td>
<td>+42.8</td>
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<tr>
<td>Fundraising</td>
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<tr>
<td>Entry evaluations</td>
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<tr>
<td>Exit opportunities</td>
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<tr>
<td>New investments</td>
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<tr>
<td>Dealflow quantity</td>
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<tr>
<td>Dealflow quality</td>
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<tr>
<td>Public support</td>
<td>+12.6</td>
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<tr>
<td>Taxation framework</td>
<td>+50.9</td>
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<tr>
<td>Write-downs</td>
<td>+23.4</td>
</tr>
</tbody>
</table>

Source: German Venture Capital Barometer and German Private Equity Barometer
Strong quarter even without megadeals: deal volume in Q3 2021 again above average

Excluding megadeals, total deals closed in Q2/21 remain roughly at the level of the (very high) previous quarter (EUR m)

Source: Preqin Pro
Due to the positive development of VC markets worldwide, the German VC market lags behind its benchmarks despite the boom.

VC deal volume in % of respective GDP

* To calculate the quotas for 2021, the first three quarters of the respective 2020 GDPs were taken as the denominator. As 2020 was a recession year in many countries and the economies have recovered, the ratios will be smaller based on the actual 2021 GDPs.

Source: Preqin Pro, own calculations
In 2020, German SMEs invested EUR 22 billion in climate protection. Driving the volume up would require transparency about climate-relevant properties of projects and access to capital market financing.
Investments in climate protection already on the agenda of SMEs

SMEs invested 22 EUR billion for projects with a contribution to climate protection

Investments with a contribution to climate protection (share in percent)

- SMEs total: 12% in 2020, 13% planned for 2021/2022
- Fewer than 5 employees: 10% in 2020, 13% planned for 2021/2022
- 5 to 9 employees: 17% in 2020, 14% planned for 2021/2022
- 10 to 49 employees: 23% in 2020, 19% planned for 2021/2022
- 50 and more employees: 36% in 2020, 19% planned for 2021/2022

Investments volume for climate protection (in EUR billions, 2020)

- SMEs total: 22 EUR billion
- Fewer than 5 employees: 5.5 EUR billion
- 5 to 9 employees: 2.0 EUR billion
- 10 to 49 employees: 6.3 EUR billion
- 50 and more employees: 8.1 EUR billion
- R&D intensive Manufacturing: 18 EUR billion
- Other manufacturing: 15 EUR billion
- Construction: 10 EUR billion
- Knowledge intensive services: 12 EUR billion
- Other services: 9 EUR billion

Source: KfW SME Panel 2021
Enabling SMEs to finance the green transition

1. Reliable climate policy
2. Transparency about climate-relevant properties and risks
3. Access to capital market financing
4. Public investment and technology promotion as leverage