



Access to smart finance

- Enhancing investors' skills in the creative industries

Center for Cultural and Experience Economy | Hersegade 20 | 4000 Roskilde | T +45 46 32 00 30 | info@cko.dk | www.cko.dk



Access to smart finance – the problem

Access to finance is often considered one of the main preconditions for industry development. Studies show that companies in the creative industries are met by the financing challenge to an even greater extent than other industries. Therefore, the *access to finance* has been high on the agenda in the creative industries.

This study approaches the problem of finance from a qualitative angle rather than the amount for money invested in the creative companies:

- How can the investment of knowledge and business skills be coupled with economic investments?
- How can we avoid thinking the creative businesses in the same terms as other /the traditional industries, and how can we allow the immaterial assets in the creative industries to be a strength rather than a weakness?
- How can we make, not only better business to be invested in but also smarter investors who understand the mechanisms in the creative industries?

Background

Why is it important to focus on smarter investors in the creative industries? The reason is that the creative industries have different characteristics from many other industries and that this difference is central asset for the creative industries.

1. Banks and other classic financing industries run a business by models of investment based on traditional industries with fixed assets and economic models based on a company's economic performance the last years. The main assets in the creative industries are often immaterial.
2. Part of what makes the creative industries innovative is the capacity to create and innovate on exactly the immaterial assets. Growth is not always linear. If we force the creative industries to abide to the classic banking and fixed asset models of finance, they will possibly lose their innovative and transformative power.

If we only attempt to make the entrepreneurs and companies in the creative industries better at being like other industries, we will risk losing some of the potential in the creative industries.

While we should still focus on developing business skills in the creative industries, we suggest that we can unleash the potential even more if we also focus on the skills of the investors. The purpose of the study is to point to ways forward and initiatives that will enhance the investors' skills in these industries with different characteristics.

Knowledge base

In 2011/12 CKO carried out a study on the characteristics of companies in the creative industries and other industries¹. The study documented differences between creative industries and other industries.

Worth noting in relation to the background is that the study *document clear differences in characteristics*.

Creative industries' companies are, to a large extent, dependent on immaterial assets and experience a higher uncertainty of future earnings.

While the creative industries are also driven by non-commercial goals, the difference between the ambitions for commercial growth is not statistically significant. This means that there is *no indication of the claim that creative industries are less ambitious for commercial growth than other industries in general*.

The study also documented the needs for business development in both the creative industries and other industries.

First of all, the needs study shows that attracting capital is not the only need for companies.

The need for capital and the need for strategy and business development are more profound in the creative industries. So is export and protection of immaterial rights.

We interpret this as an indication of the need to combine economic capital with general business development and strategy as well as specialized business development such as legal rights in the creative industries. Hence the need for smart capital.

Table 1. Self-assessment of characteristics, scale of 1-5 (5 = fully agree).

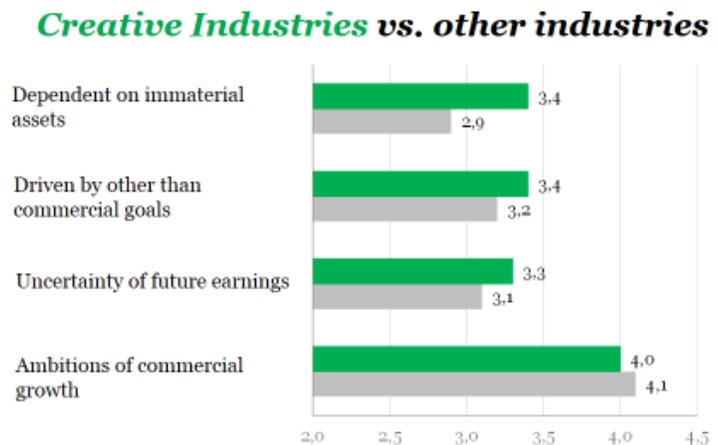
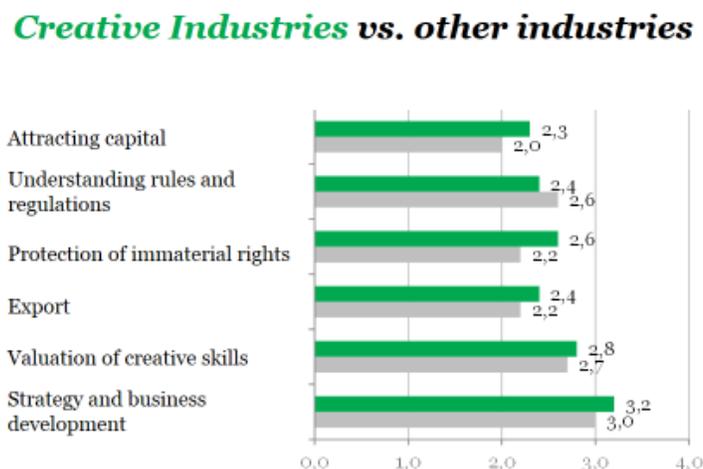


Table 2. Self-assessment of needs, scale of 1-5 (5 = high need).



¹ CKO. Behovsanalyse - Kreative erhverv i Danmark I 2011 and Behovsanalyse – Kreative erhverv i Danmark II 2012.

What is smart finance?

The term *smart finance* was proposed as a theme for the study by an investor and business developer in the creative industries in an interview with CKO.

From the start of the study, the term was loosely defined as ‘investors’ ability to primarily provide both sector specific knowledge and resources and general business skills for the companies rather than just providing economic resources’.

The problem today is that Capital is stupid. It is looking at the past and not the future. It is not key resource that companies need. But only a means to getting the right resources such as network, customer interactions, market understanding, management skills and a range of other key resources.

- Investor

The outset of this study has not been an academic task to find the most precise definition. Rather, we have used the term and the explanation above as an opening in the interviews with investors, to open their minds about investments in the creative industries.

We asked the investors in the study to use their words to describe the difference between classic investment and smart investments. Classic investments demands proven concepts focus on risk reduction by attaining a complete market and customer understanding, looks at competitors before openings in the market, society and technology and focus on long term strategy. Smart investments accepts that novelty is an asset, focus on risk reduction by small but growing scale, low costs and fast pace tests, looks at movement in consumption, culture and technology and focus on constant strategizing to reach the next step.

“Traditional investors want’s entrepreneurs to climb all the way to the top of the ladder. They believe that they can make jump as long as they can make a safety net of market analysis and foresights. The old investors are afraid to loose face when not performing a giant leap. Smart investors make the entrepreneurs jump from the low steps on the ladder and take one new step every time.”

- Investor

Methodology

The results of the study are based on qualitative and anonymous interviews with an open guide for the dialogue. We initially spoke to four investors across three countries. We recruited investors with a history of investments in the creative industries. From there we used a snowball method and as final question. We asked whom to speak to as the next investor. The study’s’ result is based on a large variety of investors from business angels to national public funds. Therefore, the validity of the findings is based on the variety of positions within the investor system rather than a high number of interviews.

The interview structure was to introduce and explain the term smart finance to the investors and ask them to describe how other investors were engaging the creative industries. By asking the investors for the lacking understanding or wrong approaches to the creative industries, we were able to avoid interviews that were self-assessments and to open.

Results of the study

Where are we now with smart financing?

During the first stage of the study we collected information about strategies for investor development in the creative industries.

In general, there is a limited focus on developing smart investors in the creative industries compared to the effort being done to make creative entrepreneurs ready for investment. Possibly this stems from an image of the investors as people with exceptional business skills and a corresponding image of the creative enterprises run by people with a total lack of business skills. The combination of these images not only can lead to very unbalanced dialogue between the two but also to a lack of effort to improve investor skills.

The study found some examples of focus on investors. These were mainly focused on awareness raising, by good examples and on providing investors with knowledge of the value- and exploitation chains of subsectors in the creative industries².

An example of initiatives with a clear focus on smart financing is Enter Europe – a project focused on the film industries using online training and cases³.

Support for highly targeted actions on the supply side for awareness raising are needed. A further core requirement of such actions is the improved provision of industry intelligence to investors about the different CI subsectors and investment opportunities, as well as examples of high growth case studies and successful investment deals, in order to increase investor confidence in making investments in this sector and to provide realistic baselines for valuations.

- Angel Capital Group

Stories from the investors

The investors interviewed for this study all agreed that there is a need of focusing on investor skills, smart or competent investment and investor readiness. According to the investors the reasons for that are:

A rapid development of the technologies underlying the creative industries. Technological development has always been an underlying factor in films, games, music, performing arts, design etc. but the pace of development is accelerating.

“We can hardly imagine the impact of the creative industries a decade or two from now. Let’s remember that Facebook and many others were nothing ten years ago.”

-Investor

“When the world was a hundred times slower, investments in tangible assets were the best investments. Today you will find some entrepreneurs who are moving the hundred times speed. If you wait for the material assets your investments will be last and worst.”

- Investor

² Creative Industries Council Access to Finance Working Group Report, 2012

³ See <http://www.enter-training.net/eu/>

The fast changes in the creative industries challenge the value chains. This leads to risks for some, but opportunities for others. Where there are opportunities there are possible good investments for those who can keep up with the change.

Social media and other new media create new ways of customer interaction and new possibilities for creative interaction and community building.

Finally, the entrepreneurs have changed. The entrepreneurs are younger and have grown up in a digital age where consumption patterns are very different from their parents' generation. Starting a business based on skills and immaterial assets is a possibility to more people today.

“Over the last ten years entrepreneurship have been much easier. Before it required money for factories. Now we have more entrepreneurs and more younger people. Many create companies in fields they know. If you are 22 what you have is pop culture as your back ground knowledge and skill base. That skill base is very different from an experienced business man in traditional industries.”

- Investor

Ways forward

Analyzing the interviews with the investors, we can identify three paths to a strengthening of smart investors in the creative industries.

Path A is a classical ‘more knowledge’ approach where the focus is on more cases and more investor learning about the value- and exploitation chains in the creative industries’ subsectors. The way to success is to learn from the few examples already in existence and to profile good cases of investments and exits and share knowledge between organization and investor communities on how to provide the investors with the knowledge and skills.

“It is long over due that we start to focus on the skills of the investors. The investors need knowledge about the value- and exploitation chains in the subsectors. And we need to show them to the investors.

...

We also need to raise the awareness that these industries are not just ‘fun’ or ‘culture’ and are not riskier than other industries – if you are smart.”

- Investor

Path B is a systemic approach where the focus lies on the life cycle of entrepreneurs, business development, investors and the different roles of these actors. Investors and especially business angels have often themselves been entrepreneurs, been drivers of a growing business and have exited from a company they have grown with. Business angels prefer to invest in sectors where they made their business because this is where they can spot the opportunities. The way to success in this approach is to catalyze investor-to-investor learning across sectors to make some investors move outside their ‘home turf’.

“There is a life cycle with investment. They start out young and make their business and then they sell it and become angles or other investors. Much of the effort that needs to be done is to wait a generation for it to happen.

...

If we had to move faster than that, I guess I would invite some specialized investors and business developers to come here from the rest of the world. We really have a lack of specialized asset valuation experts in our structural core of financing”

- Investor

Path C is a mindset approach where the focus is to make investors aware that the success parameters for business in the creative industries are vastly different from many other industries. Here the most important things are timing and team and having an awareness of the rapid change, learning and scaling business at the same time and a pursuit of step-by-step development rather than five-year plans.

If we accept the conditions of fast moving industries. Timing is essential. Let's not look at the business models of yesteryear but invite other investors into the industries as experienced co-developers of business models.

- Investor

"The barriers are more about mindset than about teaching some skills to investors."

- Investor

"Let's face it. There is often a cultural clash between the creative entrepreneurs and the investors. Let's move them a lot closer to our understanding and move ours closer to theirs."

- Investor

The three paths outlined above should be seen more as approaches to the same problem than as oppositions to each other. It is however possible that the paths will lead to different prioritizing when initiatives have to be selected and carried out.

Proposals for initiatives

The investors proposed a wide range of initiatives to strengthen the investor's skills and enable a better and smarter financing ecosystem in Europe.

Next level awareness raising

We need much more focus on investor development and investor readiness in the creative industries. Some investors suggest to:

- Continue promotion of the creative industries as not inherently risky but inherently full of opportunities.
- Share success and failures across countries – both in terms of communication channels, targeting, follow up etc.
- Form best practices and coordinate new and old initiatives across borders. Preferably in coordination or corporation with investors.

Investor academies

An academy for investors is first and foremost a learning place between investors and between investors and companies. s. Some investors suggest to form academy-like organizations to:

- Gather knowledge from the existing general and sub-sector initiatives to teach investors market skills, value- and exploitation chain mechanisms and trends.
- Identify best formats for teaching/mentoring and the best teachers/mentors. Preferably in coordination or corporation with investors.
- Recruit and deliver. Follow up with investor – entrepreneur meetings, pitching etc.

Bundling of companies as investment objects

Several of the interviewed investors pointed to the idea of having specialized CI investments experts bundle 5-10 CI companies in order to attract investor interest.

- By making a bundle of companies as one investment object, the risk of each of the companies can be reduced. The bundling also solves the problem of size. Some investors mention a gap between early funding / angel investments and large scale funding in the range of 1-5 million Euro.
- Bundles can easily be cross national and for example European. They can be subsector specific.

Produce and disseminate cases

Several of the interviewed investors pointed to the need for cases to show the potential of investments in the creative industries. According to the investors, the cases are often lacking the good exits where both the company, investor and buyer are good stories.

- Identify the already made cases and some new once. Disseminate them and follow up with new concrete opportunities to be the next case.

New pitching event design

Pitching has become the key method for matching entrepreneurs and other companies with investors. A number of the investors in the study point to the redesigning of the classic pitch session to include market intelligence, trends, investor-to-investor learning and matching.

- Engage with the investor communities and the entrepreneur communities to make new matching forms. Draw inspiration from all other formal and non-formal meetings and learning situations.
- Continue experimentation and breed new concepts. Share knowledge of best practice in this.

New valuation tool(s)

To some investors there is a strong belief that the reason for the lack of smart investments is based on the assessment tools used. Potentially it is possible to generate one or a few new valuation tools that are more suitable for the creative industries.

- The tool(s) should be made in coordination or corporation with investors.
- The new tool(s) should be supplementary to traditional valuation of the assets and potentials of a business.
- Other investors find the need for tools to be related to the presentation of the entrepreneurs and companies' business models and future plans of involvement of investors – including exits.

Grave to cradle – strengthening life cycle

There is a life cycle in some businesses where the entrepreneur sells the company and become rich. These persons often hold a lot of expertise in their own sector and a reasonable amount of general business skills. If picked up and thought how to invest smartly in the creative industries and not just their 'home turf', some of them have potentials to be smart angels.

- Identify candidates for the new generation of smart angels. Focus resources on a small number of investors.

Transfer angel subsector expertise to larger funding structures

Business angels are often funding in sectors where they have market feel, knowledge of drivers, consumer trends etc. These specialized angels can be seen as a potential advisory group or reference group by the larger trusts and funds.

- The method could also be applied to large structures such as pension funds.
- The initiative should be formed in cooperation with both angels and larger funds.
- The larger funds can use the method as recruiting.

Create a milieu – Euro Hollywood

Several of the investors point to the problem that specialized expertise is needed to invest in some of the creative subsectors.

- The suggestion from the investors is to act together across borders and form expert environments, that will have the critical mass to avoid monopolizing of investments, support a healthy competition between investors and most important support specialized investor-to-investor learning and a global cutting edge.

Move more investors into incubators

The more you have investors meet entrepreneurs and companies, the better the chances of mutual learning are.

- The investors in the study, who are also working with incubators, point to the longer lasting relations between mediators in incubators, investors and companies as a key to success.
- This is interesting to investors as a sort of talent spotting.

Final words from the investors

The investors in this study stress four points.

- **Keep supplying the creative companies with business skills.** The focus of the investment ecosystem should be balanced with skill development and learning for both entrepreneurs/companies and investors. The new focus on smart financing should not make us forget that we also need the business skills of the companies.
- **Target the initiatives.** Not all investors need the same initiative.
- **Combine with other efforts.** Good entrepreneurs are the key to sustainable and growing companies. Investments are a part of growing the creative economy.
- **Involve the investors.** Design your initiatives together with investors.

Credits and contact information

Center for Cultural and Experience Economy

Hersegade 20

DK 4000 Roskilde

P: +45 4632 0030

E: INFO@CKO.dk

www.cko.dk/eng

www.creativebusinesscup.com

www.invio-net.dk/en

Søren Würtz

Senior Consultant

P: +45 41 6060 52

E: SOW@CKO.dk

Creative Capital Conferences

<http://creative2c.info/blog/>