Study examines role of business angels during periods of austerity

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Credit: University of East Anglia

Government support for 'business angels' is essential even in times of austerity, according to research involving the University of East Anglia (UEA) and University of Glasgow.

Business angels - typically wealthy, entrepreneurial individuals who provide capital in return for a proportion of a company's equity - are recognised in both developed and emerging economies as playing a significant role in stimulating entrepreneurial activity.

With the decline in both bank lending and venture capital investment since the onset of the global economic crisis in 2008, government efforts to encourage business angel activity have become a more significant component in strategies to increase the level of entrepreneurial activity in Europe.

This new study examined the responsiveness of angels to such initiatives in so-called austerity economies - countries that were hardest hit by the financial crisis and subsequent global recession. In order to receive bail-outs from the European Union (EU), European Central Bank (ECB) and International Monetary Fund (IMF), they had to take extreme economic and fiscal measures to reduce their budget deficits

The study focused on Portugal, which suffered one of the deepest economic recessions in the EU over the crisis years following the implementation of severe austerity measures. As with other countries, such as Greece, these had adverse impacts on economic growth, investment and employment, unemployment and welfare.

The researchers, also from the Polytechnic Institute of Beja and University of Évora in Portugal, found that government intervention to support angel investing can have a positive impact. However, the impact of the various government initiatives – measured in terms of take-up rates - varied. The findings are published in the journal European Planning Studies.

Co-author Dr Tiago Botelho, of UEA's Norwich Business School, said: "Although the study confirms that government intervention to support angel investment can have a positive impact, different types of intervention appeal to different types of business angel, with implications for their effectiveness. The design of incentives also influences their effectiveness.

"Our evidence shows that the objective of expanding the number of active business angels, for example increasing the number of emerging and novice angels, requires different measures from the objective of encouraging existing and active investors to increase their investment activity.

"Other countries can learn from the Portuguese experience in relation to the types of interventions that have the highest and lowest levels of take-up, the link between the design and the take-up of incentives, and types of intervention that should be considered but have not been implemented in Portugal."

After family and friends, angel investment is the largest source of external equity financing at the start-up and early growth stages of a business. As well as the provision of capital, business angels also contribute their experience, knowledge, skills and contacts to the ventures in which they invest.

The researchers found that in Portugal, which exited from the bailout in May 2014, business angels continued to invest during the financial crisis. The typical angel made three or four investments, investing between €100,000 and €250,000 each time. Some 80 per cent also stated their intention to invest in the following 12 months, even though the process of economic adjustment was expected to continue and possibly even worsen over this period.

Fiscal incentives had a low take-up rate among business angels, suggesting the need to adjust the current eligibility conditions for tax relief on the amount invested, or replace it with tax re-investment relief, the fiscal measure most highly valued and taken-up by angels.

There was support from angels for co-investment schemes, with a preference for passive co-investment funds – as introduced by the government two years before the study - in which investment occurs automatically without investment selection filters because it eliminates uncertainty for investors. Also among the most popular measures was the elimination of the prohibition on selling shares within five years.

Portuguese business angels thought government support for business angel networks should be primarily directed at activities that improve the efficiency of the market, rather than network running costs and training for investors. However, they considered it important to support the training of young and women business angels.

Because of the role played by the networks in dissemination and supporting participation of angels in the government's co-investment fund, and increasing awareness of angel investing generally, the researchers argue that ongoing government support for these networks, preferably based on a regional model, is essential.

They add that the negative assessment by business angels of some aspects of a new legal framework is a warning that public authorities should take their needs into account when new legislation or rules are introduced, and that legitimate business angel activity should not be obstructed by legislation.

More information: José Bilau et al. Angel investing in an austerity economy – the take-up of government policies in Portugal, *European Planning Studies* (2017). DOI: 10.1080/09654313.2017.1328045

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