



Australian Private Equity & Venture Capital Association Limited

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Inquiry Secretary
Joint Standing Committee on Trade and Investment Growth
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Inquiry into Austrade's role in attracting investment in Australia

Thank you for giving the Australian Private Equity and Venture Capital Association Limited (AVCAL) an opportunity to contribute its views to the Joint Standing Committee on Trade and Investment Growth in relation to its inquiry into Austrade's role in attracting investment in Australian businesses, initiated in October 2018.

AVCAL represents the private equity (PE) and venture capital (VC) industry in Australia, which has a combined total of around \$26 billion in funds under management on behalf of both domestic and overseas investors including Australian and offshore superannuation and pension funds, sovereign wealth funds, and family offices. VC and PE firms invest billions of dollars in early stage and established businesses spanning almost every sector of our national economy. In the financial year to 30 June 2018 alone, these firms invested an estimated \$4.1 billion into Australian businesses.

Agencies such as Austrade play a critical role in attracting investment to Australian businesses both directly as well as through professional managers of capital such as PE and VC firms. We strongly support the mission of Austrade in attracting foreign capital to Australia as well as developing trade regionally and globally, and believe that further enhancements could be made to Austrade's function that would make it even more effective in meeting those objectives.

Having regard to the inquiry's terms of reference, our submission sets out to provide the views of our industry on the following topics:

- What role we believe Austrade currently has in attracting investment to Australian businesses;
- What the benefits have been from investment in Australian businesses; and
- How Austrade might better help Australian businesses to attract investment.

Our detailed comments are provided below.

1. Austrade's current role in attracting investment

AVCAL views Austrade's role in promoting investment in Australian businesses as two-fold.

Firstly, Austrade engages in generally promoting Australia as an attractive investment destination, a good place to do business, and a country that has maintained a competitive place in the region and internationally as a developed and open market economy.

One of the ways that this is achieved is by tracking and collating crucial data on Australia that is important in drawing the attention of overseas investors to the strong economic, regulatory and political/social fundamentals that exist here. International investors will inevitably look at such statistics when making their investment decisions and allocations.

A recent example would be the *Why Australia – Benchmark Report* for 2018, which sets out the reasons behind Australia's strong economic performance over the last two decades, and why the outlook for investing in businesses located in Australia remains so positive. For AVCAL, the benchmark report is a particularly useful and easily accessible tool to use when talking to large offshore investors about the merits of investing in Australia.

Secondly, it helps individual companies that are looking to export their products or services, or build a presence in offshore markets through various initiatives. For example, the Landing Pad program is designed for Australian startups and early stage companies that are ready to scale up their sales and operations (commonly referred to as 'scale-ups') with capabilities to build a presence in global innovation hubs like San Francisco, Tel Aviv, and Berlin. Program participants gain access to co-working space residency, introductions to investors, mentors and strategic partners, and business advice.

Other services provided by Austrade assist companies with information on and introductions in target markets, including:

- Market research;
- Partner and customer identification;
- Appointments during market visits;
- Follow-up to initial introductions; and
- Market promotions.

These services are all fundamental to entering and navigating through a new geographic market. Companies with limited resources, especially startups and other early stage businesses, are often unable to undertake the types of initiatives outlined above because of a lack of funding, people or expertise. In light of this, the help that is provided by Austrade can make the difference between success and failure for Australian businesses hoping to expand abroad.

In helping to build local companies into regional and global players, Austrade is enabling those companies to become larger in terms of scale and product or service offering, and become more experienced and capable in operating across multiple markets. This generates further growth in operating capacity, employment opportunities and government tax revenue, and ultimately grows the value of those companies over time.

It is also ensuring that these companies are building significant profiles with investors and business communities abroad, which potentially leads to business, partnership, or investment (both inbound and outbound) opportunities.

2. The benefits of investment into Australian businesses

Business is the key driver of economic activity in Australia. Sufficient levels of investment into business, across a variety of sources and forms of financing, are therefore necessary for our continuing economic success and the prosperity of Australia.

In our industry, businesses of all sizes rely on private capital funding, be they budding startups, small to medium-sized enterprises (SMEs) or large businesses. Some of the most promising developments for future economic growth are happening within companies that are at the early startup stage, as well high-growth companies that have graduated from the startup phase and are now expanding their workforce, increasing sales growth and investing in research and development.

Regionally, Australia already more than punches above its weight in terms of performance by such high-growth companies. A report by the Financial Times¹ included 115 Australian companies on its list of the top 1,000 high-growth companies in the Asia-Pacific region, with five of the top ten places claimed by Australian businesses in terms of percentage growth in annual revenue between 2013 and 2016. These Australian companies employed close to 42,000 people in 2016, and generated more than US\$17 billion in total revenue – which are substantial numbers in themselves for such a small cohort of businesses.

A large number of the Australian companies highlighted in the Financial Times report have benefited from VC or PE investment in order to achieve such significant growth. AVCAL believes that one of the catalysts for further employment and economic growth can be triggered by higher levels of investment into businesses by private capital providers such as PE and VC funds. The economic benefits of greater levels of private capital investment are discussed further below in this section of our submission.

Our domestic PE funds have, over the last few years, become more reliant on capital sourced from offshore. Typically, this capital is sourced from large institutional investors such as pension funds or sovereign wealth funds. Over the 3 year period of FY2015-2017, 54% of capital raised by both Australian PE and VC funds came from offshore. For PE alone, that number is even higher – for example, 83% of the total amount of capital raised by Australian PE funds came from offshore in both FY2015 and FY2016.

By raising the attractiveness of Australia as an investment destination, Austrade helps in directing flows of foreign investment – via funds managed by Australian or regional PE firms – into Australian businesses. This offshore capital then enables the PE funds to invest billions of dollars in local companies and help drive economic and employment growth.

An April 2018 study by Deloitte Access Economics provides some deeper insights into the economic contribution of PE in Australia. It highlighted some of the following key facts around how PE-backed businesses contribute to Australian economic activity, including:

- In FY2016, PE-backed businesses contributed \$43 billion in total value added to the Australian economy – equal to 2.6% of Australian GDP;
- PE-backed businesses supported 327,000 FTE jobs (172,000 directly, and 155,000 indirectly);
- In FY2016, PE-backed businesses added almost 20,000 FTE jobs, accounting for 11% of total Australian employment growth in FY2016;
- PE-backed businesses typically delivered annual revenue growth of 20%, while boosting the size of their workforce by 24%;

¹ FT 1000: High-Growth Companies Asia-Pacific, Financial Times, February 2018

- More than 85% of PE-backed businesses introduced some type of process or product innovation in FY2016, far greater than the average profile of non-PE backed businesses.

Turning now to VC, we can see the pronounced impact that foreign investment can have on our innovation sector, and the need to attract foreign investment to our innovative companies, big and small.

It is important to keep in mind that in earlier years, when VC funding was hard to find due to a lack of institutional capital in the sector, foreign VC investment was crucial to startups and scale-ups that needed large rounds of funding to continue their growth trajectory. Over the four year period of FY2011-2014, foreign VC investment accounted for 43% of all VC investment in Australian startups, scale-ups, and other early stage companies.

We are now seeing much greater levels of institutional capital coming into the local VC sector, and funding for promising startups is more available than before. But during those times of lean domestic VC funding, foreign investment continued to support the financing needs of our startups and our innovation system.

While the vast majority of domestic VC funding is currently raised from Australian investors, as the VC sector in Australia matures further and continues to grow, foreign sources of capital may become as important to the sector and to the companies that benefit from venture funding as it is for PE and other sectors of the economy.

Startups are as critical as any other business sector for providing economic and social benefits to Australia. According to the 2016 Australian Innovation System Report, startups (those businesses aged 0-2 years) are the largest contributor to job creation in Australia. From 2004 to 2011 they created more than 1.2 million jobs. This represented 90% of net positive job creation. In the same period they contributed \$164 billion to the Australian economy out of a total of \$440 billion that was added to the economy. VC investment has played a role in maintaining positive job creation in Australia, aiding the economic recovery from the global financial crisis particularly by reducing unemployment.

In more developed VC markets, venture funding provides other economic benefits. Evidence from 20 industries in the United States suggests that VC is three to four times more effective than corporate research and development at fostering innovation. Closer to home, Australian early stage life sciences companies have developed world-leading medicines and therapies, such as the bionic ear, that have improved the living standards of people here and around the world.

We have seen enormous benefits in our part of the economy from private capital investment into Australian businesses, in terms of growth in employment as well as driving more R&D and innovation. But there is no doubt that the benefits of investment in Australian business extend far wider than just the private capital sector and the Australian businesses that have benefitted from either PE or VC investment.

3. How Austrade can attract more investment into Australian businesses

Aside from providing a generic suite of tools to assist businesses in accessing new markets or sourcing investment, Austrade's role can be expanded further.

We believe that Austrade can also help larger, mature high-growth companies through a more tailor-made approach to expanding into overseas markets. Austrade's services can be customised to the specific product or service, target market, scale, and management expertise of each scale-up company. As companies grow, their capabilities and specific needs become more varied and complex. Enabling Austrade to provide a focused service approach to these companies, in terms of export know-how and investment readiness, would be one way of meeting those needs.

3.1 Lessons from overseas

It is worthwhile to turn to examples from other jurisdictions to find other effective approaches that Australia can undertake for attracting more investment into our domestic businesses. Two examples are explored further below: Scotland and Singapore.

Scotland

In early 2016, Scotland released an action plan to increase trade and investment in Scotland called “*Global Scotland: trade and investment strategy 2016-2021*”.

The Scottish action plan also identified increasing the number of high-growth businesses as especially important, “as such businesses display higher levels of innovation and productivity than average and contribute disproportionately to employment and export growth.” But these businesses face many of the same challenges that Australian SMEs confront – particularly access to appropriate capital.

Scotland's approach to improving access to finance for supporting company growth has primarily focused on business advice and support. However, the Scottish government has also established funds and bodies that are tasked with the specific goal of helping companies to fill their financing gaps. For example, the Scottish Investment Bank was set up in order to help companies identify appropriate sources of finance, engage with funders and secure the investment they need to grow their business. Over the 2017-18 annual period, the bank worked with over 35 investors based outside of Scotland, helped Scottish companies secure more than £105 million of international investment, and £275m of international sales were achieved by the bank's portfolio companies.

In 2015, Scotland also introduced the SME Holding Fund, which seeks to address the problems of access to finance specifically for SMEs with growth and export potential. The SME Holding Fund Advisory Group selects ‘delivery agents’, which are fund managers or trade bodies that manage the available capital in order to deliver on the objectives of the fund. To December 2017, the four appointed delivery agents' reported performance indicates that 330 companies had accessed £223 million under the fund, creating over 1,000 jobs in the process.

Singapore

Singapore formed one government agency in April 2018 to champion enterprise development – Enterprise Singapore. As part of its remit, it works towards growing Singapore as a hub for global trading and startups (thereby competing directly with Australia to attract startups in the Asia-Pacific region) as well as helping Singaporean companies internationalise.

Enterprise Singapore takes a business-centric approach to its services based on a company's stage of growth, the industry in which it operates, and the overseas markets of interest. The tailor-made approach to helping businesses is applied across some features of Enterprise Singapore's offering to companies that are looking to break out into new markets, such as its matching of companies with the right business partners in other markets and specialised tax advisory services.

A separate entity, the Singapore Economic Development Board, is responsible for attracting inbound investment into Singapore and for strategies that enhance Singapore's position as a global centre for business, innovation, and talent. It manages grants and tax incentives for global businesses that are seeking to establish themselves in Singapore.

4. Next steps

We would like to thank you for the opportunity to provide a submission in response to the inquiry. If you would like to discuss any aspect of this submission further, please do not hesitate to contact me or Kosta Sinelnikov, AVCAL's Policy & Research Manager, on 02 8243 7000.

Yours sincerely,

Yasser El-Ansary
Chief Executive