

Financing Europe's Startups and Scale-ups

Why Europe needs both deeper capital markets and better scaling conditions

Europe's ability to innovate, compete and grow increasingly depends on whether startups and scale-ups can access the financing they need to expand. For many of these firms, especially those with intangible assets, long development cycles and uncertain early revenues, traditional bank lending is not enough. Venture capital, growth capital and functioning public equity markets are therefore essential. However, Europe's weaker venture outcomes are not only a financial-market problem. They also reflect weak scaling conditions for the firms that demand risk-bearing capital.

The policy question should not be framed simply as how to mobilise more capital. The essential function of financial markets is to assess and price risk, helping direct capital to firms that can create value and scale. That function cannot easily be replicated by public funding.

Europe's challenge is not just a shortage of capital

Europe's weaker venture capital outcomes do not only reflect underdeveloped capital markets. They also reflect the conditions facing the firms that demand this type of capital. An active and deep capital market requires both investors and attractive investment opportunities in the form of growing companies.

If startups and scale-ups lack access to markets, specialised talent and predictable and globally competitive rules, fewer firms will have the potential to grow in ways that attract risk capital. Developing capital markets across the EU is therefore necessary, but not sufficient. Better capital markets can improve financing conditions, but they cannot on their own compensate for weak scaling conditions in the broader economy.

The following should be prioritized in order to create conditions for more fast-growing companies are founded and scaled in the EU:

1. **Improve access to risk-bearing capital across different stages of growth**, from early-stage venture funding to larger follow-on rounds.

2. **Develop credible exit routes**, since venture capital only works at scale if investors can realise returns through acquisitions, secondary sales or public listings.
3. **Improve access to specialised talent**, including through workable frameworks for employee ownership and stock options.
4. **Create predictable and globally competitive business conditions**. Cumulative compliance costs, regulatory fragmentation and burdensome rules are especially damaging for firms trying to scale rapidly.
5. **Deepen the Single Market**, reducing the cost and complexity of scaling across the EU.

What capital markets do for startups and scale-ups

While capital markets cannot create great firms on their own, they perform functions that startups and scale-ups depend on.

Venture and growth financing require investors that are able to bear illiquidity, long holding periods and risk. Pension funds and other long-term asset owners are therefore important not only because they can allocate capital directly to venture and growth funds, but also because they deepen the financial system as a whole. A broader base of long-term capital improves risk-bearing capacity, market depth and the wider financing environment for growing firms.

Deeper and more liquid public markets also strengthen price discovery, improve valuation benchmarks and support the wider ecosystem for IPOs and acquisitions. This matters even when firms are not listed. Buyers in M&A transactions also depend on financing capacity, valuation benchmarks and functioning market infrastructure. Increased retail investor participation and larger pools of institutional capital both contribute to deeper and more liquid markets.

Stronger capital markets also support capital recycling and entrepreneurial incentives. When successful firms exit, capital, experience and networks can flow into the next generation of companies. This is especially important for early-stage companies, which are often

too small and unproven to attract larger international investors.

More fundamentally, credible exit routes affect the incentives to start, finance and join high-risk companies in the first place. If founders, early employees, angel investors and venture funds believe that successful companies can eventually realise value through acquisitions, secondary transactions or public listings, the expected return to early-stage entrepreneurship increases. In this sense, functioning capital markets do not merely finance startups after they exist; they help create the conditions under which starting and backing such firms becomes worthwhile.

Relevant insights from Sweden

Experience from Sweden shows that relatively strong venture outcomes are possible within the broader EU framework when local ecosystems, institutional capital and exit opportunities reinforce each other. Strong firms can attract international capital, as startups have been able to draw substantial venture investment from abroad.

At the same time, Sweden also shows that venture investing relies heavily on local networks, soft information, local presence and active ownership, especially at early stages. Therefore, local ecosystems still matter.

Sweden benefits from strong institutional investors and comparatively developed public equity markets. This improves both direct access to finance and the wider ecosystem on which startups and scale-ups depend.

The positive outcomes are not primarily explained by public VC schemes. Instead, explanations lie in broader ecosystem quality: investable firms, local early-stage capital, institutional depth and credible exit routes.

The role of public funding in the EU

Public funding can play a role, but must not become the default response to Europe's financing challenges. The current landscape is already highly complex, with overlapping instruments and limited transparency on how support is allocated and what additionality it creates. Complexity is not just an administrative issue. It raises transaction costs, weakens accountability and makes it harder to distinguish effective interventions from relabelled activity.

To be effective, public instruments should therefore remain focused on clearly defined market failures, be designed to crowd in private investment, and be subject to strong discipline on effectiveness and additionality.

Key policy messages

Europe needs to work on both sides of the problem. Stronger capital markets and better general framework conditions for businesses are both essential.

- 1. Strengthen the investor base.** Europe needs deeper capital markets, including larger pools of long-term institutional capital and better channels for household savings into market-based investment.
- 2. Improve exit conditions.** Venture capital depends on credible exit routes. Deeper and more liquid public markets, together with stronger financing capacity for acquisitions, are essential for a functioning venture ecosystem.
- 3. Make Europe easier to scale in.** Better capital markets are necessary, but they must be matched by reforms that reduce fragmentation and make startups and scale-ups more attractive to invest in.

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