Unleashing Regional Startup Investment

Part of Startup Coalition's Funding the Underfunded Campaign

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STARTUP COALITION

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About Startup Coalition

Startup Coalition, formerly Coadec, is the policy voice of UK tech startups and scaleups. Since 2010, we have worked to engage on behalf of tech startups in public policy debates in the UK across a range of critical priority issues including access to finance, immigration and skills, and technology regulation.

We fight for a policy environment that enables early-stage British tech companies to grow, scale and compete globally. We have over 4,000 startups and investors in our network and have been instrumental in building proactive coalitions of businesses and investors on issues integral to the health of the UK's startup ecosystem. We represent the startup community on the Government's Digital Economy Council, and the UK on the board of the international organisation Allied for Startups.

Acknowledgements

Our work on the *Funding the Underfunded* campaign builds on the extensive efforts and insights of many individuals and organisations across the ecosystem. We recognize that the challenges faced by underrepresented groups in securing funding are deeply rooted and multifaceted. Addressing them requires acknowledging and learning from the lived experiences and perspectives of those directly impacted.

We are especially grateful to the founders, investors, and regional cluster stakeholders who contributed to this report. Ensuring that we reflect the diversity of experiences in starting and scaling innovative companies across the UK has been central to this work. We are committed to listening, amplifying their voices, and advocating for meaningful change. Special thanks to the Tech Cluster Group and associated partners for all of their help on our first report, *Unleashing Regional Startup Investment*.

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Our Funding the Underfunded Campaign

The UK's tech ecosystem has made incredible progress in the last decade, but the opportunities of tech have not been spread evenly. Founders from underrepresented groups – including those based outside of London, people of colour, women, and those from lower socioeconomic backgrounds – continue to face systemic barriers to accessing critical equity funding.

A 2020 report by Extend Ventures starkly illustrated the inequalities in Venture Capital (VC) funding - a critical source of equity funding for startups aiming for rapid growth. Over the previous decade, black founders received just 0.24% of VC investment and female founders secured only 11%. The disparities are even more pronounced at the intersection of these groups, with black female entrepreneurs receiving a mere 0.02% of the total funding.[1]

Similarly, the 2021 Cornerstone Report highlighted that founders based outside of London and those without degrees from elite universities also struggle to secure investment.[2] For example, founders based outside of London face entrenched barriers to accessing VC and angel funding when compared to their counterparts inside the M25.[3] Data on founders from lower socioeconomic backgrounds is harder to find, but the disproportionately high number of founders with degrees from elite institutions, and the normalization of a "friends and family" funding round before a founder is VC-ready reflect a built-in bias favouring those with elite backgrounds.

The *Funding the Underfunded* campaign is dedicated to closing the gaps in funding, working to increase funding for historically excluded groups while championing policies that foster an inclusive entrepreneurial landscape.

We must now take action to prevent the lost generations of progress in traditional elite professions from taking further hold of technology. There is perhaps no more important policy area than ensuring founders have an equal shot to secure investment, regardless of where they come from, what they look like, and who they are. And crucially, numerous studies have shown that funding the underfunded is not just a moral imperative, it is an economic one too.[4][5][6] Systematic barriers to accessing investment hold back job creation, economic growth and talent.

This campaign will form a dedicated stream of work focusing on ensuring that all founders can compete fairly for funding. **The Funding the Underfunded Campaign is an umbrella of work linked by a central goal: to make the UK's tech ecosystem fairer and ensure it benefits all.**

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1 Diversity Beyond Gender (2020)
2 The Cornerstone Report - Access to Venture Capital (2021)
3 British Business Bank (2023). *Investing in Ethnic Minority Entrepreneurs: Report and Data Analysis November 2023*
4 Alliance for Affordable Internet (2021). *The Costs of Exclusion: Economic Consequences of the Digital Gender Gap.* Web Foundation
5 McKinsey Digital (2023). *Women in tech: The best bet to solve Europe's talent shortage.* 24 January 2023.
6 World Economic Forum (2024). *This is how inclusion benefits the global economy, according to experts at Davos.* 30 January 2024.

Across the parliament, the Startup Coalition will run this campaign to look at levers the Government can pull to make progress on this agenda. This will include a series of papers, grounded in conversations with founders and investors and data from the sector, seeking to examine the state of funding. Building on the substantial work of others in the ecosystem, these papers will tackle issues faced by founders across geography, ethnicity, gender, and class.

The campaign will take the shape of several reports outlining the reality facing founders in attracting investment today and how the Government can help to erode funding disparities, widening access to investment for all startup founders, whilst growing the sector as a whole. The first is our deep dive into regional disparities below.

Introduction

Every corner of the UK is home to entrepreneurship and innovation. Grounded in decades-old industry clusters of expertise and some of the best universities in the world, entrepreneurs are building game-changing startups outside of London. From the Glasgow to Edinburgh corridor, Manchester, Leeds, Bristol, Bath and beyond, the UK boasts many established startup clusters. These regions are full of innovators, cultivating cutting-edge tech from advanced manufacturing and health tech to creative industries and green technologies.

These clusters have seen remarkable growth in recent years. For example, Birmingham and Liverpool have seen VC investment increase by over 1000% and 650% respectively in just four years.[7] This momentum has often been driven by local pioneers – building ecosystems from the ground up, transforming their cities into hubs of entrepreneurial activity, and generating new economic opportunities for their communities.

Despite this success, founding and scaling a startup outside of London continues to present unique challenges. Access to critical investment remains heavily concentrated in the capital, leaving many regional entrepreneurs struggling to secure the funding they need to grow. Data shows the disparity in how funding flows throughout the UK, and experiences from our founders highlight the frustrations with the added difficulties of founding and growing a business outside of London.

Regional startup ecosystems aren't just engines of innovation - they are the key to unlocking the UK's economic potential. Thriving clusters create jobs and drive sustainable growth in the regions. They help diversify the economy and ensure prosperity and opportunities are spread across the UK. Now, with a new mandate to drive economic growth through investment, devolution, and reform in the regions, the Government must tackle funding disparities head-on. Through this report, we have developed practical and tangible solutions to tackle barriers to funding and get cash into the hands of regional changemakers – enabling them to found businesses, scale their ideas, and drive growth in their communities.

[7] Dealroom (2024). *UK startup ecosystems on the rise outside London.* 12 January 2024.

Summary of recommendations for Government:

- **Recommendation 1: Mandate the British Business Bank to evaluate its regional programmes and align funding to local business needs.**
- **Recommendation 2: Make attendance at regional and national demo days mandatory for venture funds part of the Enterprise Capital Funds (ECF) scheme.**
- **Recommendation 3: Establish local mission-based talent investment programmes across the UK.**
- **Recommendation 4: Foster sector-specialised funds to channel capital into regional centres of expertise beyond the Golden Triangle.**
- **Recommendation 5: Work with mayoral combined authorities to issue convertible regional bonds based on the Municipal bonds model used in the US.**
- **Recommendation 6: Take steps to ensure the UK has a thriving spinout ecosystem to turn our world-leading research labs into engines of growth.**

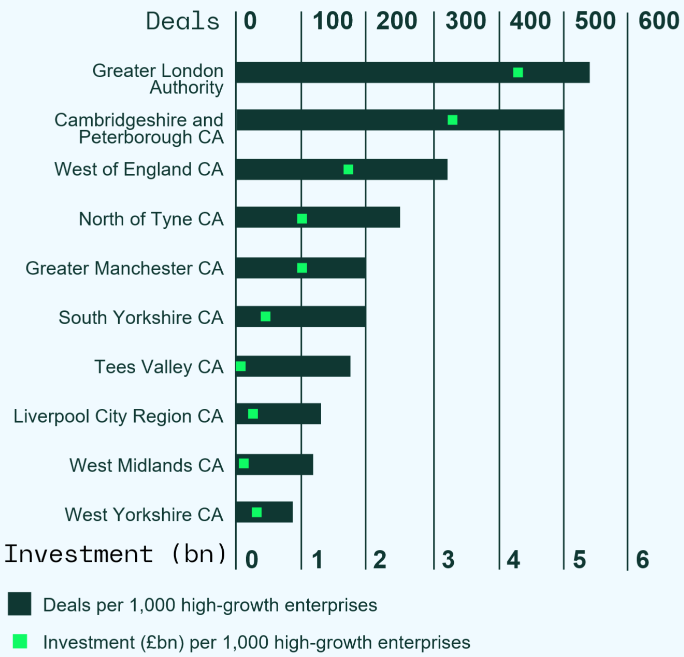
The Regional Startup Balance Sheet

To set the scene, it is first important to understand the facts on the ground. We have used Beauhurst's data to quantify and plot the regional spread of startups in the UK.

The data shows that London is by far the biggest single regional home for startups, with 47% of all firms that have raised at least £100k in VC capital based there.[8] This share increases as we look at larger amounts of funds raised: 49% of all firms that have raised more than £1m, and 53% of all firms that have raised £10m are based in London. As a share of overall funds raised, the picture is even more stark. Returning to the original sample of firms that have raised over £100k, firms in London constitute 60% of the overall investment secured. We have mapped this data in the following pages.

Equity deals and values in English Combined Authority areas per 1,000 high-growth companies

Source: British Business Bank analysis of Beauhurst data (2022); ONS Business Demography (2021)



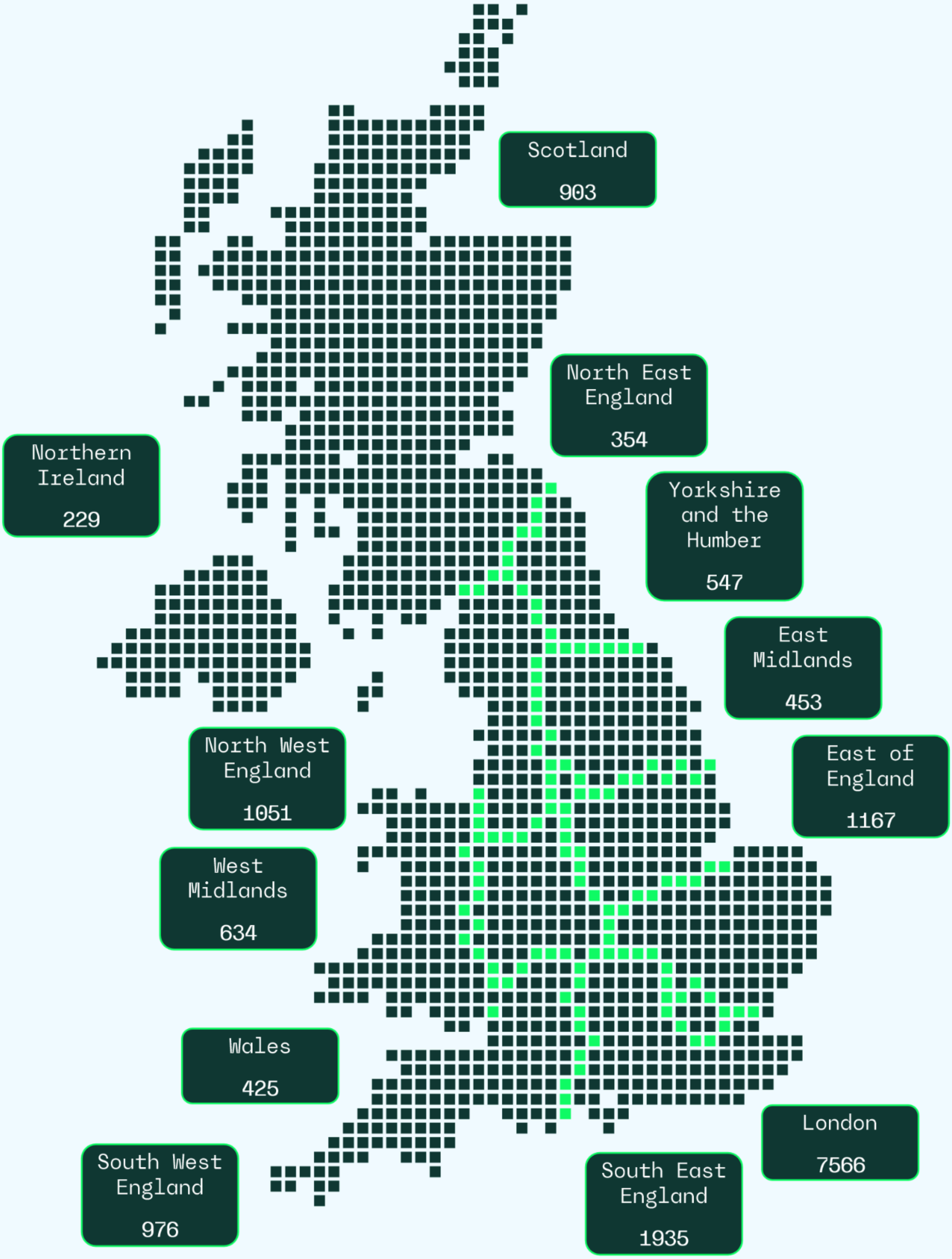
The experience of firms correlates with the data we have on where funding is flowing on the investor front. **80% of VC funds are based in London and deploy 69% of their funds to London and South East based companies.**[9] Regional startups find it harder to scale and attract follow-on funding. Outside of London, the rest of the UK represents less than 50% of the value of announced equity deals per high-growth technology company between 2021 and 2023.[10]

Almost 50% of first-time deals in 2023 were based in London, compared to the rest of the nations and regions.[11] With the deals in London equating to 63% of the total investment value for the year. London still dominates when it comes to attracting investment into high-growth businesses.

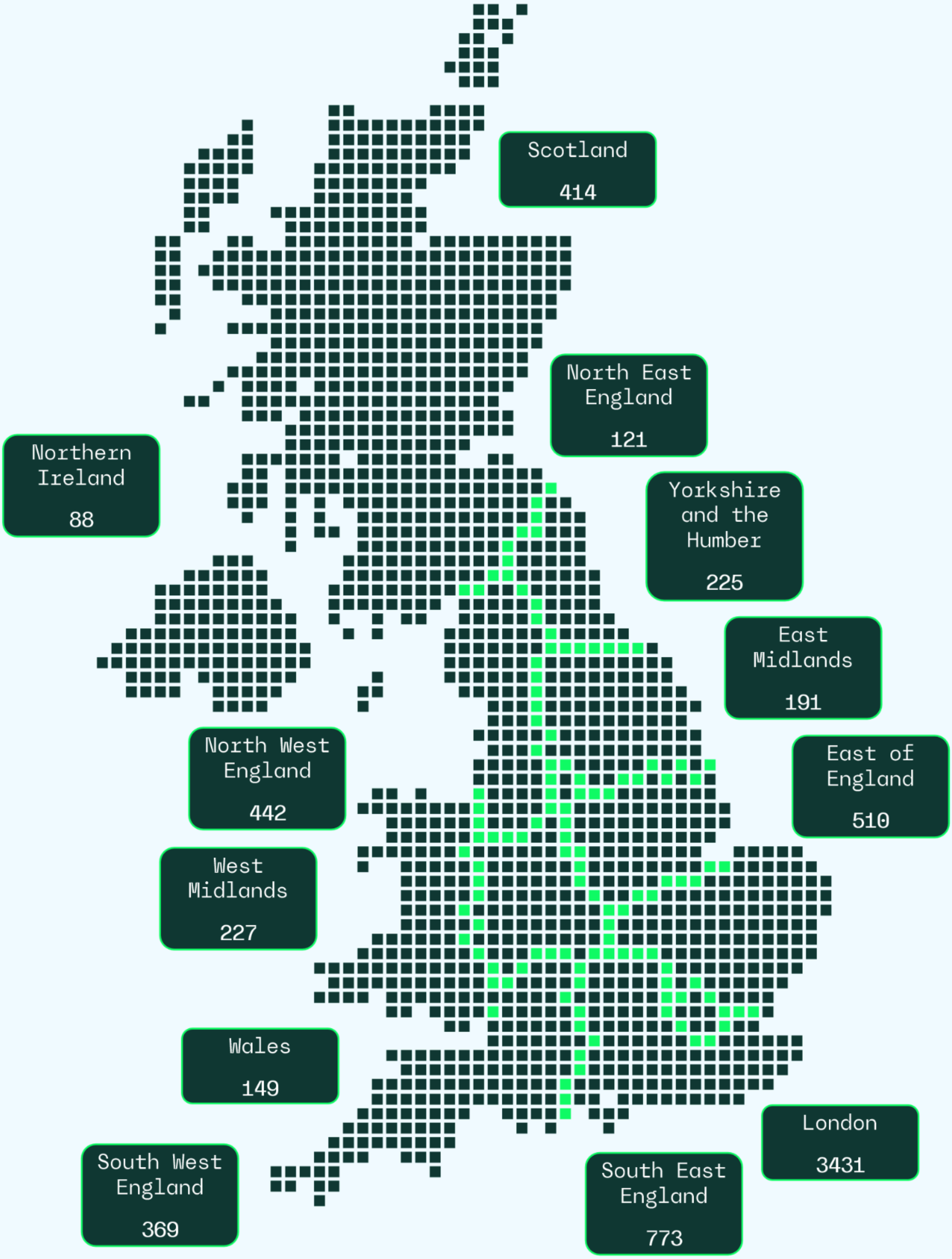
Furthermore, by other metrics, the disparity could even be increasing. 39% of firms that were founded in 2023 and 2024 and raised at least £100k were headquartered in London. **In absolute terms, their dominance is even more pronounced - of the population of startups founded in 2023 and 2024 and that have raised at least £100k, London-based firms constitute 72% of all investment secured.**

[8] Beauhurst data gathered in November 2024, using a sample of "tracked" firms under Beauhurst methodology, with a filter based on the amount of fundraising secured.
[9] Praetura Ventures (2022). *What's Powering the Powerhouse: The Story of the Northern Scale Up Landscape, Told by Those Who Built It.*
[10] The British Business Bank (2024). *Nations and Regions Tracker: Small Business Finance Markets 2024.*
[11] The British Business Bank (2024). *Nations and Regions Tracker: Small Business Finance Markets 2024.*

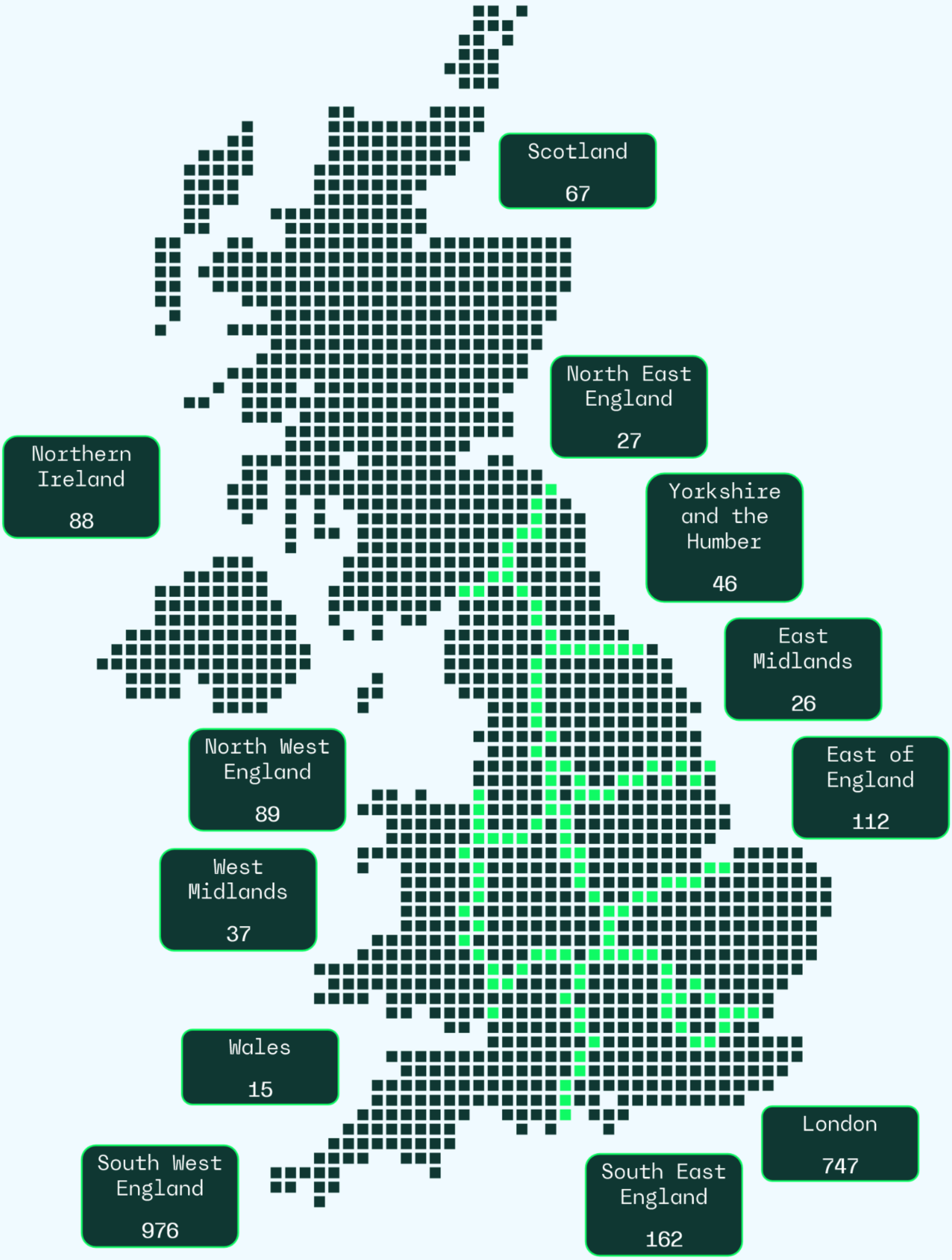
Number of firms that have raised at least £100,000:



Number of firms that have raised at least £1,000,000:



Number of firms that have raised at least £10,000,000:



While this data shows London dominates in funding, this concentration does not reflect the breadth of innovative potential across the UK. Instead, it highlights the challenge to be overcome by unlocking resources and opportunities in underfunded regions. Government intervention is critical to enabling businesses inside and outside these clusters to attract talent and funding.

The British Business Bank

The BBB was launched in 2014 as an independent, state-owned development bank, stepping in, "where the business finance market doesn't provide favourable conditions for success."[12] It is the largest domestic backer of VC funds in the UK and a key lever the Government can use to tackle regional disparities in access to finance. As such, below we will be deep-diving into some of the ways in which the BBB is unlocking growth for startups as well as providing recommendations for how it can accelerate that growth in the regions.

The BBB operates a series of programmes to deliver equity finance for startups through co-investment funds and delivery by private VC firms. Its formal objectives include, "unlocking growth by ensuring entrepreneurs can access the finance they need regardless of where and who they are."

In practice, the BBB has many tacit goals and functions: from crowding in private capital to solving regional, ethnic and gender-based barriers to funding; creating national tech champions and unicorns; and delivering a commercial return for the taxpayer – all whilst creating a generation of fund managers that can attract institutional capital.

In November 2024, the Chancellor launched the British Growth Partnership which will allow the BBB to reinvest its returns. It is positive to see this update of the BBB's remit and the extra flexibility granted to reinvest, alongside the Government's policy to create a UK National Wealth Fund, which presents a great opportunity to implement positive change to the existing public financing regime.

We believe the BBB can go further to better tackle regional disparities in accessing finance and support the development of high-growth specialist technology clusters across the UK.

[12] What we do | British Business Bank (british-business-bank.co.uk)

The Investment Challenges

"The further away from London you are, the harder fundraising gets."
Regional Startup Founder

To help define solutions to this challenge, Startup Coalition has engaged extensively with regional players. We also convened a roundtable of founders based outside of London, including from across the developed nations, alongside colleagues from the UK Tech Cluster Group, an umbrella organisation including the regional startup networks and incubators across the country. Combined, they gave us rich insight into the reality of attracting investment outside London. These conversations have helped to discern the following selection of foundational challenges facing entrepreneurs outside of London.

Our conversations with founders revealed issues with risk aversion among funders and flaws in the BBB's funding models. When allocating funding, startups feel that the BBB doesn't conduct sufficient analysis on the sectoral clusters or tailor its approach to the specific sectoral and regional funding needs.

For example, a small tech startup that can be tested using no-code tools may not benefit from regional funds like the Northern Powerhouse Investment Fund, as these are often geared towards businesses targeting larger market sizes. Similarly, such startups may not align with the return expectations of the Regional Angels Programme. In the devolved nations too, where national investment banks dominate the landscape, startups face additional challenges.

Risk-taking and Specialisation

When it comes to backing regional founders, there is no substitute for hard capital. Difficulty attracting investors, struggling with lower valuations, and accessing Government-funded programmes were consistently the top investment issues discussed in our founder roundtables and interviews. On the one hand, we heard that there is a foundational challenge in the UK around how the investor culture is more risk-averse, particularly in contrast to the US. This is not a new challenge, and the government frequently hears this from founders across the economy. For instance, at a Business and Trade Select Committee evidence session on industrial policy in April 2024, Josh Western, CEO and Co-Founder of Space Forge shared how he "had 30-minute calls with the first 50 employees at Uber and at the end of the call they've said put 'me in for half a million', whereas the UK angel ecosystem is very much about how do I preserve my SEIS or EIS tax allowance."

For startups outside of London, however, this conservative culture is exacerbated due to the general lack of specialism across the investor population in the UK. In contrast, founders we spoke to felt that startup clusters outside of London tended to be highly specialist: for example, Lancashire is a hub for defence tech, given its proximity to BAE Systems, while Leeds is home to many innovative fintech platforms.

Our sample of founders felt that the majority of the VCs they interacted with were generalists who ignored these specialist clusters. Many founders we interviewed also felt that many VCs had a "London mindset" and were more used to investing in B2B software, with its predictable economy of scale and return on investment pathway.

Overconcentration of Funding

We also heard from founders that, while there are deep investment pools in the UK, most are concentrated in London, with unfortunately only shallow local investment pools outside the M25. With a handful of funds controlling the majority of local funding, regional founders can quickly find themselves boxed out of existing funding opportunities if they fail to appeal to these groups. This perpetuates a dependence on London-based investors, which comes with a host of problems for founders - from the time and expense of travel to larger issues like poor infrastructure and high childcare costs. We have heard that this is felt acutely by founders who face additional systemic barriers to accessing investment.

Consequently, at the heart of the investment challenge for many founders outside of London and the South East is the fact that their ecosystems are often trapped into relying on one source of funding. This comes with the added risk of stifling the natural evolution of startup ecosystems, which traditionally benefit from competing VC perspectives and approaches.

This is, in part, because Government programmes, including those led by the BBB, have created an over-reliance on a single source of funding, resulting in an excessive concentration of investment in specific funding pools and failing to effectively address regional disparities. In this way, the UK Government has identified a problem that needs addressing, but their interventions have been suboptimal. This is experienced at two distinct stages for startups - Angel and Venture Capital funding - as well as at the National level.

Angel Investors

Angel funding - typically injected before a startup's product is ready to go to market and before many VC investors are willing to talk - is critical. As the startup ecosystem matures, more Angel syndicates are burgeoning all over the UK. These syndicates, where multiple equity investors pool their funds to support startups, play a vital role in funding innovation. However, because the BBB funnels so much capital into startups outside of London through Angel syndicates - £185m into 13 syndicates through the Regional Angels Programme[13] - they have been given an outsized amount of power in the regions.

According to the founders, there are limited high-net-worth (HNW) angel investors in regional clusters outside of London. Regional angels are also less familiar with the foundational investment incentives designed to drive them towards investment in startups, such as the Seed Enterprise Investment Scheme (SEIS) and the Enterprise Investment Scheme (EIS). Recent analysis from the BBB shows that London and the South East consistently make up around 65% of EIS investment.[14] Without using these schemes, angel investors outside of London may be less inclined to take the risks associated with early-stage startup investments

As a result, founders reported feeling "stuck" when they were unable to secure funding from local angel syndicates. If a state-backed local syndicate leader does not support their company, it can create a perception that something is fundamentally wrong with the company. This creates a snowball effect, where one missed opportunity hinders their ability to attract investment elsewhere.

[13] British Business Investments Regional Angels Programme (accessed 2 Dec 2024)
[14] Enterprise Investment Scheme, Seed Enterprise Investment Scheme and Social Investment Tax Relief statistics: 2024 - GOV.UK

Venture Capital

An over-concentration can also be seen in the VC funding landscape. The BBB targets regions for equity funding through their Nations and Regions Investment Funds. These include one fund for each of the devolved nations, and funds supporting startups in the North, South West, and Midlands. Each fund is managed by a private firm and offers equity finance up to £5 million through that firm - meaning startups only have one fund to pitch to if they want to benefit from the BBB's regional investment offering.

This is done by design. Part of the BBB's remit is to deliver value to the taxpayer, and it does so in part by managing funds efficiently – which has led to this tendency to concentrate capital into one venture fund to reduce multiple management fees. However, in practice, this may have the opposite effect, instead creating a less resilient and less diverse startup funding environment.

With limited private venture capital operating outside of London, this concentration of state-backed funding makes a single fund's investment philosophy the de facto gatekeeper for an entire region's innovation. If founders are unsuccessful in appealing to this one fund, they have nowhere else to turn. As a result, promising startups that don't fit the specific criteria of the dominant fund may be forced to relocate or abandon their ventures entirely, despite their potential value to the local economy.

Devolved Investment Banks

Like in the regions, startups in the devolved nations face significant challenges in securing early-stage funding compared to their London-based counterparts because of their limited access to local equity funding. Travelling to meet London VCs is not only time-consuming but also often prohibitively expensive, especially since building relationships with investors takes time.

National development banks have been designed to fill this gap in the market, and are used to deliver some of the BBB's funds to the devolved nations. The Development Bank of Wales (DBW) and the Scottish National Investment Bank (SNIB) provide a significant proportion of the financial support for startups in their respective nations. For example, in previous research, we found that 80% of venture investment into startups in Wales between 2011-2020 came from the Welsh Development Bank.[15]

While these banks play a critical role in their respective ecosystems, founders expressed concerns that this overconcentration acts as a barrier to private investment. Founders have told us that they worry that the dominance of these banks risks fostering a culture of "grant dependency," where startups design ideas to fit grant criteria rather than market demands or innovation potential.

We have also heard from founders who told us that the concentration of funding within these institutions has added layers of bureaucracy, making it challenging to navigate funding processes. It can also be costly, with one founder spending £500k on legal fees to take money from the SNIB due to extensive red tape.

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[15] Coadec (2023). *Startup Wales The Welsh Tech ecosystem, its challenges and opportunities March 2023*

The Role of Corporates

Corporate Venture Capital (CVC) has also been identified as an emerging driver of innovation, as corporations increasingly recognise the value of investing in startups. CVCs can leverage their industry expertise and resources to provide not only growth capital, but also strategic guidance, access to markets, and credibility to startups.

Since 2011, CVC investment in the UK has grown significantly, with £5.55bn deployed across 429 deals. CVC investment in the UK peaked at £1.5bn in 2019, mirroring global trends as corporate venture investment reached a record $73.1bn in 2020. In the UK, prominent CVCs include Google Ventures, Channel 4's Indie Growth Fund and Unilever Ventures. These CVCs fund a broad spectrum of sectors - from advanced technologies to sustainable consumer goods.

A notable CVC is the Sheffield-based UK Steel Enterprise (UKSE), a subsidiary of Tata Steel which was set up in 1975 to support communities impacted by the closure of the steel factories across the UK. Their focus is on supporting businesses in steel areas, providing investments, loans, and workspaces. Their role in reinvigorating regional economies, especially in areas that have experienced economic decline, illustrates the potential for CVCs to drive economic growth in the regions.

However, despite this progress, regional disparities remain evident, as most CVC activity continues to be concentrated in London and the South East.

Recommendations for Regional Growth

We have several recommendations on how the BBB could better support the development of regional startup clusters. To complement these levers available through the BBB, the Government should also collaborate with Mayoral Combined Authorities (or Combined Authorities) to help integrate technology and startup development into their regional economic strategies and take the necessary steps to boost the pipeline of startups spinning out from our country's leading universities.

Scale up the British Business Bank

Recommendation 1: Mandate the British Business Bank to evaluate its regional programmes and align funding to local business needs.

As part of the multi-year spending review, the BBB should assess the effectiveness of its current regionally focused programmes. Rather than asking the beneficiaries of existing programmes about their effectiveness, the BBB should instead assess the programmes on their merit and as part of the wider investment challenges within regions.[16]

As part of this, the BBB should be mandated to conduct detailed research into the funding journeys and specific needs of businesses within each regional cluster. This analysis would tailor funding schemes to local conditions, providing a more strategic, data-driven approach to regional economic growth instead of the current one-size-fits-all approach.

For example, Leeds may have lots of financial services startups creating back-office automation platforms that need seed venture funding, whereas Sheffield may have lots of legal tech businesses that can be started by solo entrepreneurs off a small cheque size that doesn't necessarily need to be straight equity.

These insights are critical to enabling targeted interventions that align with local industry strengths and development needs and could significantly enhance regional Gross Value Added (GVA) and support the government's wider strategy. The research should be conducted on a clear timeline so it can support the creation and delivery of Local Growth Plans, which the government has committed to and are discussed in greater detail in the following section.

Recommendation 2: Make attendance at regional and national demo days mandatory for venture funds that are part of the Enterprise Capital Funds (ECF) scheme.

[16] Chalmers, Alex (2024). *A bridge fund to nowhere? The UK government, venture capital, and 23 years of bad public policy*

The ECF scheme is a UK-wide programme which aims to bolster the availability of venture capital for promising early-stage businesses with high-growth potential. This programme gives capital directly to private funds to invest. Most of these funds are London-based.[17]

Firms in this scheme are subject to several conditions, such as limitations on the round size, investment timing, and what types and sizes of companies can receive investment. Currently, the ECF Programme is agnostic to geography and sector of investment as long as the requirements around being a British company are met. However, the BBB is entitled to add conditions to how it gives out money to firms.

To provide regional founders with greater access to funding, VC firms that accept BBB money through the ECF scheme should have to attend regional demo days arranged in partnership with local cluster groups.

Get Local Growth Plans Right

The government has committed to power up every corner of the UK and make further progress on devolution. In several areas, including Greater Manchester, the West Midlands, and Tees Valley, this means established combined authorities will be led by directly elected mayors. Recent devolution deals have begun granting combined authorities greater control over localised taxes (e.g., business rates retention), some budgetary flexibility, and have consolidated funding streams into "single pots" enabling regional governments to allocate resources more effectively across different sectors.

It has also asked every place to develop a Local Growth Plan to guide the delivery of local industrial strategies. These must not hark back to the industries of the past but set out a clear vision for how clusters can be formed around emerging technologies and drive new industrial growth in the coming decades.

This is only possible if startups can access the funding they need to grow in every region of the UK.

Local Growth Plans represent a unique opportunity for places to support their regional startup ecosystems by bringing together existing programmes under a local strategy. However, many places already have well-developed plans for regional economic growth - the government should not make them replicate this with the addition of their stamp of approval unless they have something new to offer them. This could include additional data, synergies with the national industrial strategy, and policy that encourages investment into areas.

Recommendation 3: Establish local mission-based talent investment programmes across the UK.

Government should create programmes that can unlock regional investment by leveraging talent across the UK and encouraging them to build the technology companies of the future. Programmes could be focused on the sectoral strengths identified in Local Growth Plans to tie them to regional industrial strategies. They should provide successful applicants with the resources and networks to grow successful high-growth companies in their areas.

[17] Funds we have invested in | British Business Bank

What is talent investing?

Talent investing identifies extraordinary talent and supports them in developing ambitious business ventures by offering them the support, space, time and resources to build out ideas. At the end of the process, there are opportunities to access capital investment from the organisation running the programme. Unlike accelerators or incubators, which support pre-existing startups, talent investors actively create new ventures, making them particularly effective at de-risking the initial entrepreneurial steps.

Examples from Entrepreneur First and Antler showcase the model's success, where selected entrepreneurs receive a stipend, structured guidance, and expert validation, allowing them to focus on building robust ventures without the distractions often associated with bootstrapping or navigating accelerator programs.

The Government should work with local partners who understand their regions. They could choose to invest alongside other Limited Partners (LPs) in established funds on their terms. Alternatively, via the BBB, they could work with local partners to establish funds with more flexible terms. The latter approach would be extremely beneficial since the Government would be able to stipulate that the funding and/or companies created must have a regional impact or address specific diversity metrics. This could be where the programs are located, or where the companies are located after completing the program, etc.

Recommendation 4: Foster sector-specialised funds to channel capital into regional centres of expertise beyond the Golden Triangle.

The BBB's British Patient Capital (BPC) Programmes - which was created to address the late-stage funding for high-growth companies - plays a critical role in helping startups scale. For example, Northern Gritstone - a fund designed to support high-growth businesses in the North - has benefitted from BPC funding that has enabled it to provide critical funds to Northern startups as they scale.

However, despite its objectives, BPC funding remains disproportionately concentrated in London. A 2023 Interim Evaluation of British Patient Capital by the BBB showed that companies backed by BPC are more heavily concentrated in London than the general private market: 45.7% of all equity-backed businesses were based in London, while 72.9% of companies backed by BPC were London-based.[18]

Additionally, there are pockets of wealth across the country in corporate industrial businesses. However, these people may be reluctant to invest in non-cash flow generating startups, due to a lack of familiarity with the trajectory of a modern tech business. The Government could encourage such investors to deploy capital through SEIS/EIS. However, a better option would be to club investors into a corporate venture capital fund, investing in climate, industrial and deeptech businesses that are closer to their expertise. This could be based on regional sectoral strengths, including those set out in the Local Growth Plans.

Recommendation 5: Work with mayoral combined authorities to issue convertible regional bonds based on the Municipal bonds model used in the US.

[18] British Business Bank (2023). *Interim Evaluation of British Patient Capital*. p 152-3

The UK Government has already encouraged Local Government Pension (LGP) funds to channel more investment into venture capital, as demonstrated by initiatives like the Mansion House Compact. To build on this momentum, Combined Authorities could be supported to issue convertible regional bonds, a novel hybrid instrument designed to fund both infrastructure and high-potential startups.

What are municipal bonds?

Municipal bonds are debt securities issued by states and local governments to fund public projects or meet operational needs. Investors purchase these bonds, effectively lending money to the issuer, and receive regular interest payments until the bond matures. At maturity, the principal is repaid.

How would this work?

Building on this model, convertible regional bonds could offer a fixed-income investment to fund a mix of infrastructure projects, startups, and scaleups. The bonds would be repaid using revenue generated by these investments, with additional flexibility for bondholders to forgo interest payments and convert their bonds into startup equity.

LGPs have already started to deploy capital into assets within their boundaries. Convertible regional bonds would align with the fiduciary duty of LGPs to deliver returns while benefiting the local economy. Deploying pension capital into startups and infrastructure supports regeneration and enhances the quality of life for pensioners. This approach would be a win-win, allowing Combined Authorities to drive regional growth while creating new avenues for investment.

In contrast to US municipal bonds, the interest income from UK local government bonds is subject to taxation, as the UK does not provide the same level of tax-exemption benefits as in the US. Like in the US, the UK local government bonds are repaid with interest over a fixed period. However, local authorities in the UK are subject to stricter regulations and borrowing limits, which affects their bond issuance practices. The Treasury should explore whether changes to either of these areas could create a more attractive market for municipal bonds.

Get Serious About Spin-Outs

Spin-outs are innovative companies that are created based on research, most often undertaken at universities or public sector research labs – or a mixture of both, which is “spun out” into a commercial product. With world-leading academic and public sector research institutions in every corner of the country, ensuring innovators can capitalise on this research in the regions is critical to driving growth in clusters beyond the “Golden Triangle” of Oxford, Cambridge, and London.

Often, a key barrier to accessing private funding for startups is tied to equity stakes their institutions have retained in their companies. Currently, spinning out a company can be an uphill battle for founders. As the research institutions themselves own the Intellectual Property (IP), researchers have to negotiate with their university’s Technology Transfer Office (TTO) or the Public Sector Body (PSB) to commercialise their product, typically with the TTO or PSB retaining stakes in the startup.

Often, these negotiations are weighted against founders, with TTOs and PSBs having significantly stronger negotiating power. TTOs and PSBs are emboldened to set terms that hurt founders and take high stakes in their spinouts - which acts as a major barrier to private equity investment. In the case of public sector spinouts, a 2024 study of public sector founder equity found that, while the data was more obscured, PSBs typically took a higher median founding equity stake in their spinouts compared with universities - with more PSBs taking over 40% stakes than universities.[19]

In 2023, the Government undertook an independent review of university spin-out companies, which included 11 recommendations for making the UK a world-class destination for spinning out research.[20] By November 2024, 49 universities - less than half of all UK universities - had adopted different standards, promising to take less from spinouts to address some of the challenges founders face. However, both the report and this step taken by universities fall short of what's needed.

Those that have signed on still allow university Technology Transfer Offices (TTOs) to take up to 25% of certain types of businesses. The percentage of stakes taken is still too high, even with these changes, and the terms that come with these agreements continue to be swayed in the university's favour. Notable Russell Group universities Leeds University and Queen's University Belfast, as well as non-Russell Group universities like the University of St Andrews, haven't adopted these new standards.[21] According to Spinout.fyi - an open database for university spinouts - one founder who spun out their research from Leeds University said the university took 55% in equity of their startup upon founding and before investment was raised.[22]

Coupled with other interventions to expand funding pools, improving how research is spun out from these institutions can be key for retaining local talent. We have also heard from founders that, in areas with less entrenched startup ecosystems, university innovation can be siloed from the local startup community. Young entrepreneurs have told us that it can make remaining in the local area less appealing once they max out the funding available to them through their universities. Ensuring that these startups have a fair chance at private equity funding and can capitalise on existing networks in their local communities is critical for retaining talent.

Recommendation 6: Take steps to ensure the UK has a thriving spinout ecosystem to turn our world-leading research labs into engines of growth.

The Government must bring the parties to the table and deliver on making sure that founders can spin out innovative companies from British institutions fairly and openly. Increased standardisation of equity frameworks would be a step in the right direction - giving founders more negotiating power through clear, transparent terms, and preventing TTOs and PSBs from taking more than their fair share in equity through lower caps on equity stakes.

[19] Public Sector Founder Equity & Rewards to Innovators Study - GOV.UK

[20] Eggington, E., Kinsman, L., Lasek, M., Ulrichsen, T. C., & Roupakia, Z. (2024). *Public sector founder equity & rewards to innovators study.* Government Office for Technology Transfer.

[21] https://www.ukri.org/publications/spin-outs-review-implementation-best-practices-adoption-list/spin-outs-best-practice-adoption-list/ Accessed 4 Dec 2024

[22] https://www.spinout.fyi/data Accessed 3 Dec 2024

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