

# 2012 trends in VC/PE country attractiveness

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## **For the third year running, IESE's Global Venture Capital and Private Equity Country Attractiveness Index measures the investment attractiveness of countries in the volatile VC/PE fields.**

For the third consecutive year, IESE's Center for International Finance, in conjunction with Ernst & Young, has published its [Global Venture Capital and Private Equity Country Attractiveness Index](#).

In 2011, the index expanded from 66 to 80 countries. In 2012, the research team -- led again by IESE Prof. [Heinrich Liechtenstein](#), Prof. Alexander Groh of EMLYON Business School (France) and Karsten Lieser, a research associate at IESE -- have profiled 116 countries.

The expansion reflects the growing importance of emerging economies. Africa is prominent among the newcomers, with a total of 31 countries represented, compared with last year's eight.

Many of the new candidates are not yet mature enough for VC/PE investment. Instead, the expansion is driven by "investors' desire to put additional emerging markets on the world map of potential countries for allocation."

## **King of the hill**

This year, the United States again tops the rankings, with Canada and the United Kingdom swapping their 2011 places for second and third. Japan and Singapore follow in fourth and fifth.

The six key drivers of VC/PE attractiveness were again used: economic activity; depth of capital market; taxation; investor protection and corporate governance; human and social environment; and entrepreneurial culture and deal opportunities.

The apparent simplicity marks a complexity, though: Many factors are summarized to reach a single composite VC/PE measure. For a country to have a high rank, it needs to achieve a high score on all of the criteria.

The United States usually ranks ahead, especially in its capital market. This was the most decisive factor for other highly ranked countries' lower scores, even when they did well in entrepreneurial culture and deal opportunities.

Investor protection and corporate governance were also important in developing strong VC/PE conditions, with the strongest performers all scoring highly in these categories.

Until the big emerging economies can challenge the United States across the board, they will continue to lag, even as they become more attractive.

The expansion has affected the rankings, stretching them at the lower end and narrowing the gaps at the top.

The index does not compare directly with 2011, but calculates changes over a five-year period (2008-2012) with the enlarged country sample.

Such a change is beneficial in examining the shift from traditional mature markets toward emerging regions.

## **Making way for emerging economies**

The five-year comparison underlines the increasing attractiveness of even the smaller emerging economies. Countries in the Middle East, in particular, registered a strong performance, with Tunisia, Morocco, Saudi Arabia, Egypt and Kuwait all rising at least 10 places, despite the turmoil of the Arab Spring.

The change in many mature economies is no less stark. Greece, Iceland and Ireland all dropped on the back of the sovereign debt crisis. Ireland, for example, fell eight places over five years.

Invariably, it is the big emerging economies -- the BRICS of Brazil, Russia, India, China and South Africa -- they are making way for, as investors seek to capitalize on these fast-growing

economies, large populations and catch-up potential.

China, in particular, has enjoyed spectacular success, with sound economic conditions, deep capital market liquidity and a strong performance in stock market trading and public issues.

India follows closely behind, while Brazil, too, has seen substantially improved investment conditions.

South Africa is also on the march, thanks to its ties with the United Kingdom and the "establishment of a similar legal and capital market-oriented culture."

However, the survey also reveals reservations about the BRICS.

Corporate governance levels and investor protection remain concerns, while bribery and corruption levels remain high, and innovation and corporate R&D low. These factors particularly affect Russia, a relative laggard among the BRICS.

Most worrisome, growth and wealth creation in the BRICS are often confined to certain regions and small elites. Until growth benefits are more widespread, the BRICS are unlikely to improve across the board.

Should growth slow -- a clear possibility, with even China experiencing a relative slowdown recently -- their VC/PE attractiveness rankings are likely to drop.

## **Performance anxiety**

Overall, the shift toward big emerging markets is clear, and investors are more and more inclined to consider the potential of even small emerging economies.

But unless some of the key driving forces improve, the interest could just as easily fade. As Ireland vividly demonstrates, the ground can shift very quickly in response to events.

With investors ever more willing to consider taking risks, the expansion of the index is particularly valuable. But this brings challenges as well, as the team's testing of the index's tracking power revealed.

This process involves calculating data on VC/PE transactions in countries to work out their averages. As a rule, this correlated with countries' index rankings, demonstrating its effectiveness in tracking VC/PE activity.

Yet measuring performance figures, "still one of the best-kept secrets in the VC and PE industry," proved problematic, primarily due to the entrenched principle of non-disclosure.

This is accentuated in developing countries by the comparative immaturity and low activity of their markets.

Compiling the index is an evolving process. But the team is game for the challenge, urging users to contribute feedback and knowledge. The 2012 expansion is a direct result of that.

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