

Actors and contribution mechanisms for financing innovation

Innovation requires resources to develop it, so access to finance is a crucial requirement for many forms of innovation activity (even if not for all of them).

Stages in the innovation process

In order to understand how finance impacts the development of innovation activity, it is useful to consider three broad stages:

- Develop inventions and conduct research
- Develop prototypes and commercialize inventions
- Technology diffusion and adoption

The funding needs are different across each of them, and so is the willingness of financiers to provide funds (see [Contribution mechanisms for financial innovation](#) [1]).

Key actors for financing innovation

There are multiple types of investors, beyond family and friends, who can provide finance to innovative firms at different stages of the innovation and firm development process, if their internal resources are not sufficient. The main categories include banks, stock and bond markets as well as public institutions, venture capitalists and business angels. Other types of actors play an important role in funding innovation in firms, such as foundations, which often fund R&D but also commercialization or alternative financial intermediaries, including providers of asset-backed finance or crowd-funding platforms (see [Key actors for financing innovation](#) [2]).

Finance mismatch

“Finance mismatch” occurs when the supply of finance does not meet demand. One of the main reasons for this capital market imperfection is information asymmetries between lenders/investors and borrowers which lead to adverse selection and moral hazard. Finance mismatch may particularly affect innovative projects because the outcome of an innovation investment is generally more uncertain than the outcomes of other kinds of investments. Also, since the returns on innovation investments are not perfectly appropriable, firms may be more reluctant to disclose information on innovative projects than on other types of projects. This will render negotiations with potential funders more difficult (see [Finance mismatch](#) [3]).

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[1] <https://www.innovationpolicyplatform.org/content/contribution-mechanisms-financing-innovation?topic-filters=12273>

[2] <https://www.innovationpolicyplatform.org/content/key-actors-financing-innovation?topic-filters=12104>

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