

Funding Options for Early Stage Companies

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26th January 2016

Funding Landscape

- Recap – recent history
- Current trends – moving on from the Great Financial Crash
- Managing without grants?

‘Banking is necessary, banks are not.’ - *Bill Gates*....in
1994

'The Second-hand Mortgages Department'

- 'Financial innovation was critical to the creation of an industrial society; it does not follow that every modern financial innovation contributes to economic growth. Many good ideas become bad ideas when pursued to excess.'
 - *John Kay Other People's Money (2015)*
- 'How many other innovations can you tell me that have been as important to the individual as the automatic teller machine, which is in fact more of a mechanical innovation than a financial one?'
 - *Paul Volcker, Former Chairman, Federal Reserve, WSJ 14/12/2009*
- 'If banks don't change, let's change the banks.'
 - *Jack Ma, founder of Alibaba (2009)*

Was This Familiar?

Why We Are Needed

The UK has the lowest level of business investment of all the OECD countries. The ratio of UK business investment to GDP is 8% compared to over 10% for the USA, Germany and France.

*British Business Bank
Strategic Plan – June 2014*

FINANCIAL TIMES TUESDAY FEBRUARY 14 2012

Small businesses suffer as lending falls £1bn short

Project Merlin

With RBS focusing on other activity, many companies are struggling to access finance, reports
Brian Groom

Access to bank finance

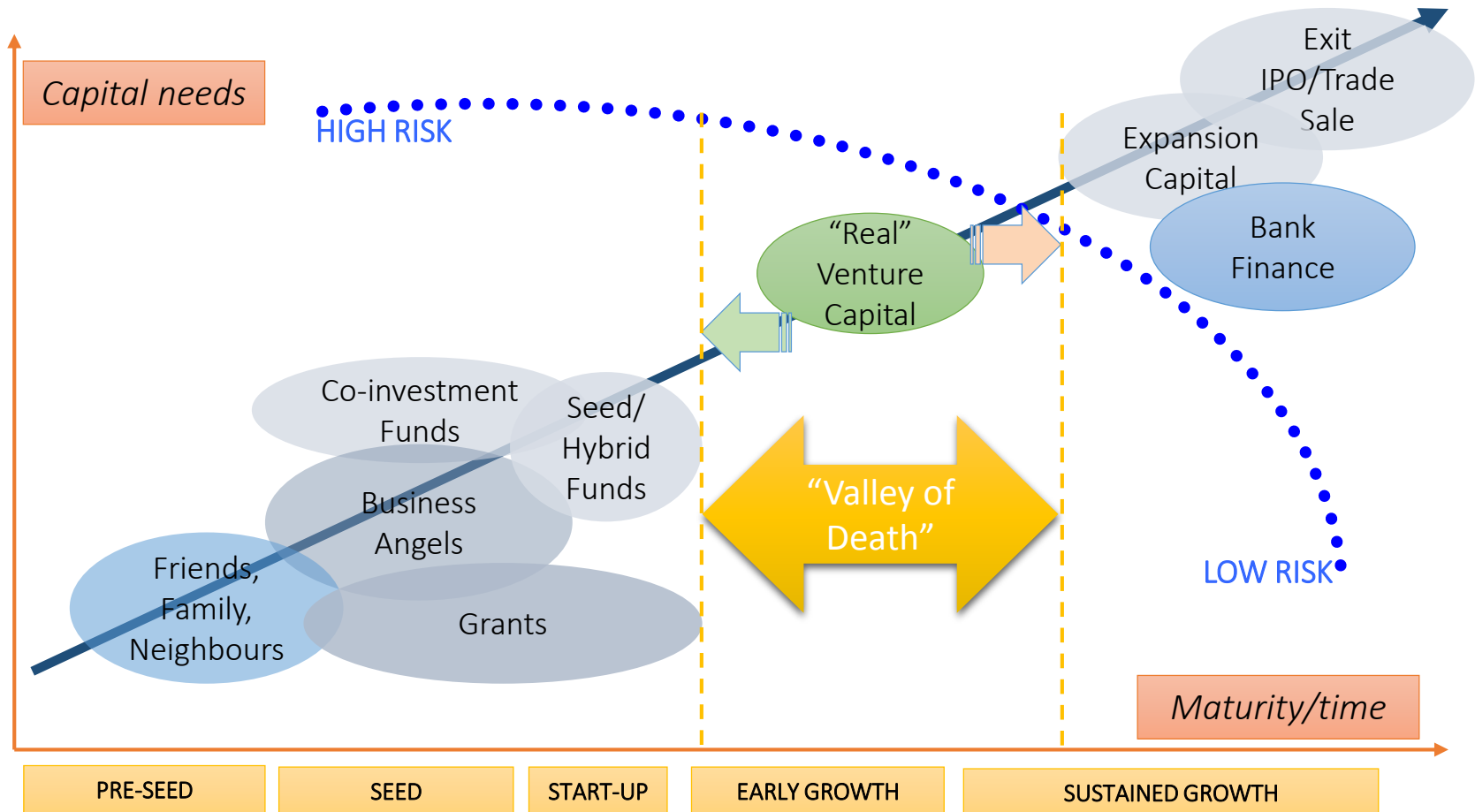
is not being repeated this year. Instead, George Osborne, the chancellor, is negotiating with the banks on a "credit easing" deal to cut the cost of borrowing through a £20bn national loan guarantee scheme over the next two years.

The banks exceeded their overall government-agreed commitments with gross new loans of £214.9bn

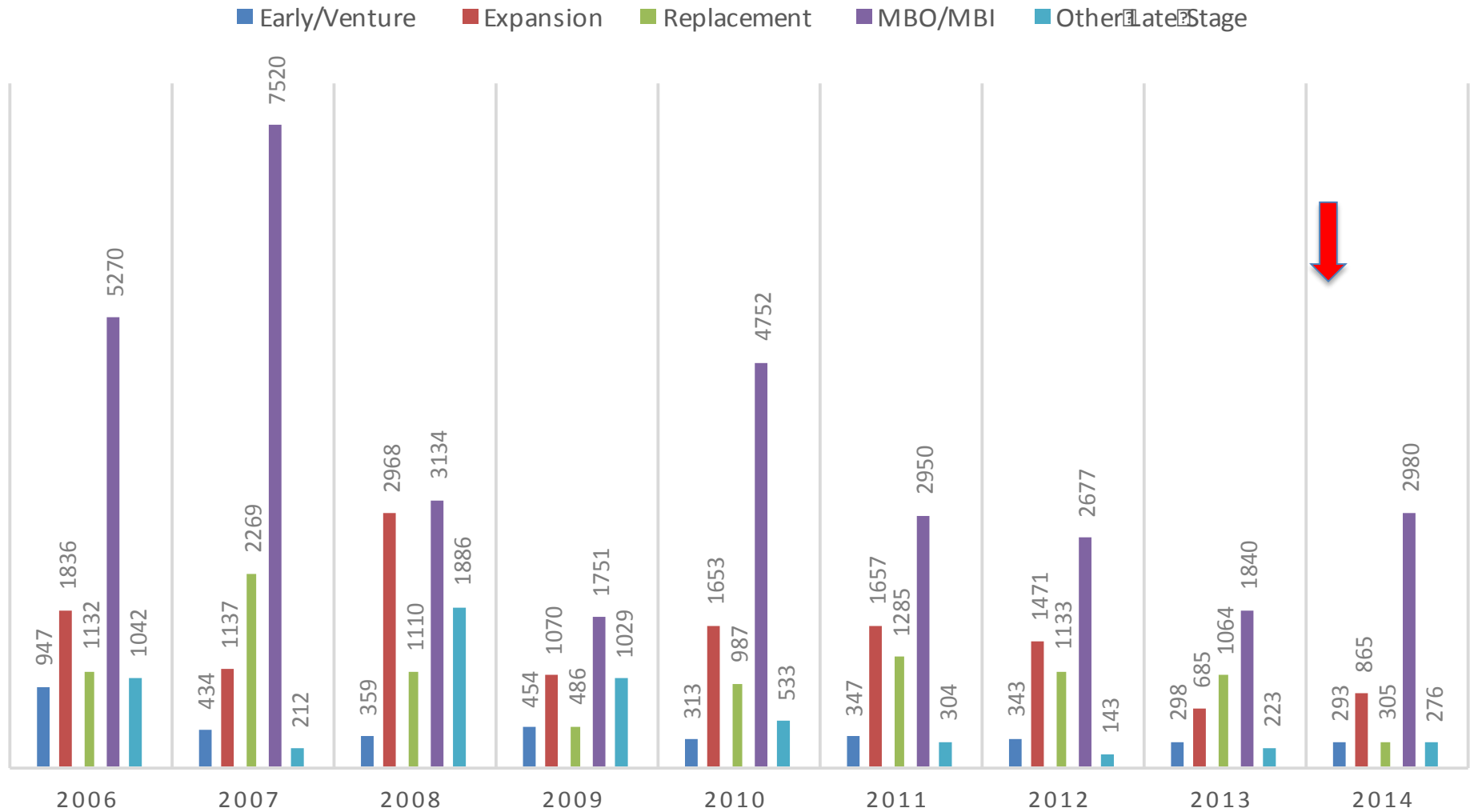
many having to use other sources such as credit cards or borrowing from friends and family.

"This is still a burning issue for many SMEs," said Phil Orford, the forum's chief executive. "Our helpline receives complaints from members every week over increasing costs associated with bank products and the removal of over-

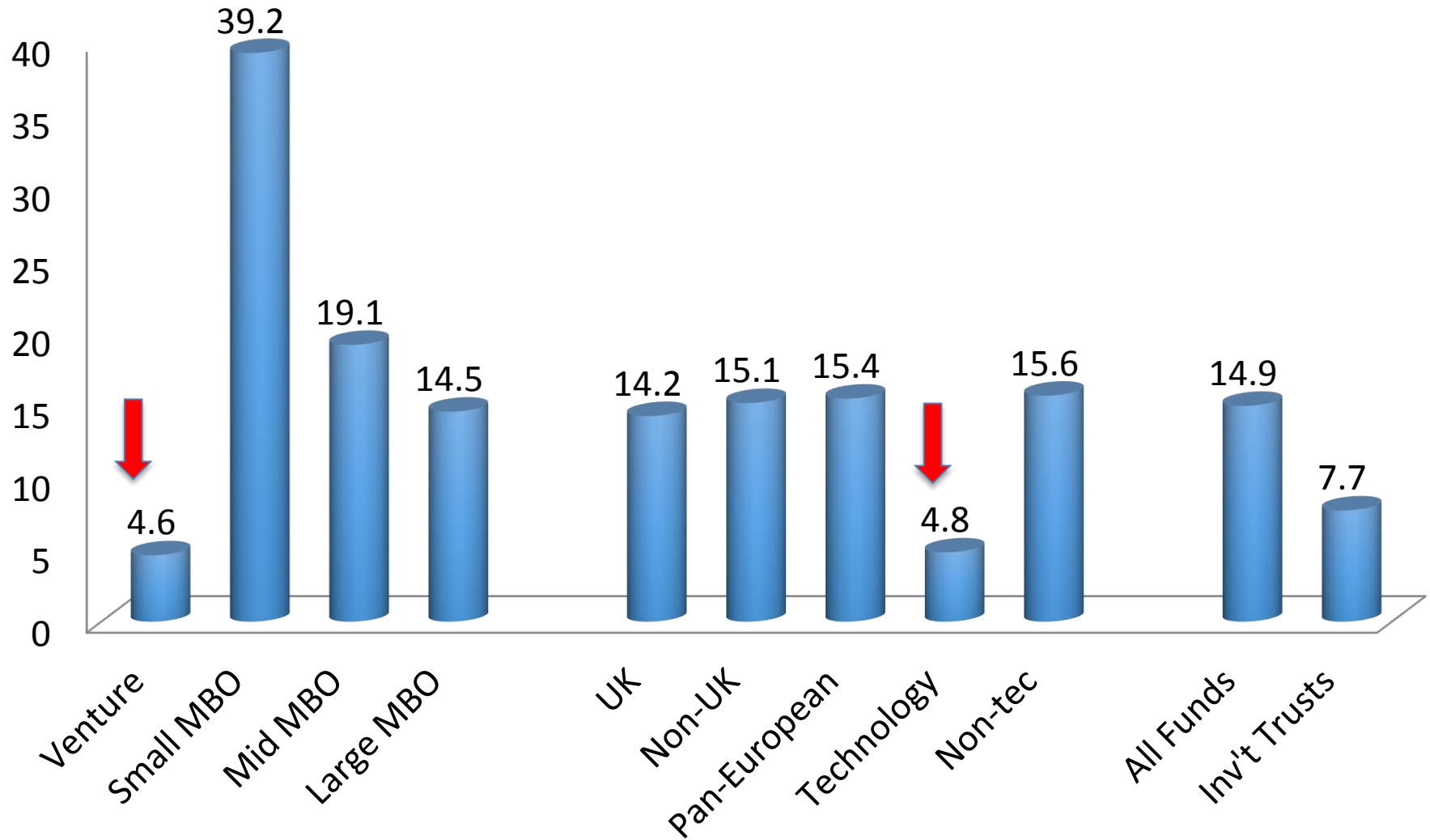
The Funding 'Ladder'



UK VC Investment by Stage – 2006-14 (£M) [BVCA]



10-year Returns to End 2014 (IRR%) [BVCA]



Nesta...



UNIVERSITY OF
CAMBRIDGE

.....

UNDERSTANDING ALTERNATIVE FINANCE

The UK Alternative Finance Industry Report 2014

.....

Peter Baeck, Liam Collins and Bryan Zhang
November 2014



Some Failure Inevitable, but:

“The failure of a single crowdfunding project or even of a peer-to-peer lending platform will be bad news for some investors, but it will be a drop in the ocean compared to the fall-out and systemic shock from the failures we’ve seen in the last decade in the mainstream financial sector.”

Stian Westlake

www.nesta.org.uk/news/2015-predictions/bust-funded-crowd#sthash.BEZcU0S4.dpuf

Angel Tax Breaks

- Seed (50%)/Enterprise (30%) Investment Scheme
- Set investment against income tax liability and provide capital gains incentives
- Trade off uncertainty for tax benefit
- UK experience:
 - Angels = 3x venture funding at early stage
 - 82% of angels used tax schemes
 - 57% of investments made under tax schemes

R&D Tax Credits

Not a grant scheme but corporation tax relief

- For all companies with qualifying R&D revenue expenditure
- Allows 225% (SMEs) or 130% (large companies) of R&D expenditure to be deducted from profits for tax purposes
- For capital R&D expenditure, 100% capital allowance possible
- Some SMEs not in profit can surrender R&D tax losses for cash
- BUT: grants can reduce the amount of eligible R&D expenditure or deduction percentage, sometimes to zero

Patent Box

Favourable company tax regime for Intellectual Property

- Tax rate 10%, phased in over 5 years to 2018
- Company must own/have exclusive rights to IP
 - ...be exploiting the IP commercially
 - Complex, multistage calculations
 - For new and existing patents
- Includes profits up to 6 years before grant
- Must have robust accounting systems
- EU restrictions to 'home' country profits only

See Also: Corporate Investment

Many large corporations have investment funds

- Act like VCs; ring-fenced activity, strong sector focus
- Unlikely to create conflicts of interest
- Will have a clear process and ‘rules’

Some SMEs may act like private investors

- Directors/shareholders interested in opportunities they understand
- Have synergy with their own business

Finding corporate funds is easy, finding strategic fit takes initiative

Better: Enterprise Capital Funds

- Public-private vehicle from 2006, 18 to date, £620M
- Min 33.3% private funding, eg £13.33M of £40M fund
 - Priority govt return \pm interest charged on drawn capital
 - Then capital repaid to all investors
 - Then profits to private investors, with govt 'override'
 - No additional tax breaks
 - Rules focus on funding-gap investment
- Some ECFs have 'active angel investor' participants

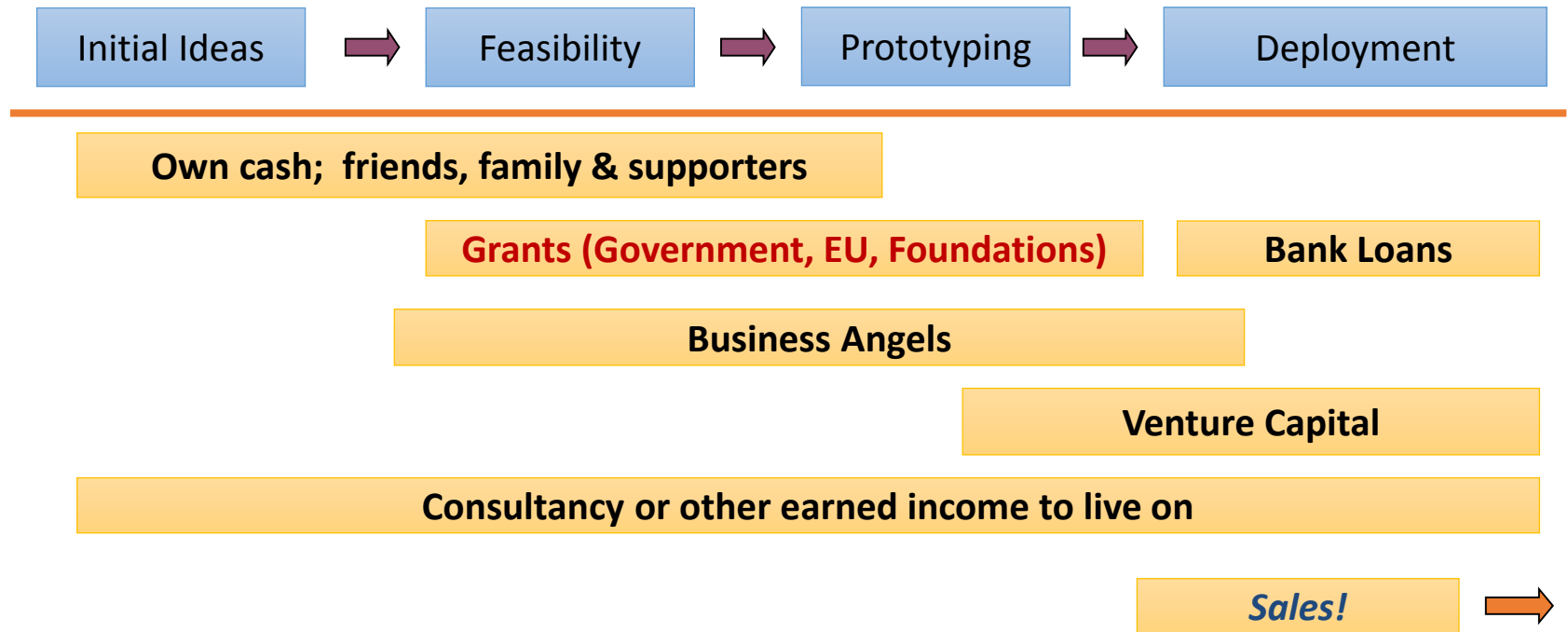
Worse: Comprehensive Spending Review

‘Innovate UK to convert £165 million of its grants into loans or other new financial products by 2019/20.’

25/11/2015

- Details lacking...like student loans?
- Grants as means of making investment go further
- Grants as validation
- A step removed from the funding ladder?

Development Stages & Funding



Enterprise Europe Network Services

We help ambitious businesses to innovate and grow internationally:

Partnering: Finding commercial, technology development and research partners

Access to Finance: Helping business to access funding through Innovate UK competitions and European finance programmes including Horizon 2020

Innovate2Succeed: Bespoke programme of coaching

Networking events: Focused around accessing finance

European Information: eg. VAT, EU Policies and Directives, EU Legislation

Public Procurement: Public procurement rules, tenders alerting service

Your voice in Europe: EU consultations, feedback mechanism relating to EU policies