

**Enterprise M3 Board**

**30 November 2017**

**Enterprise M3 Fund Management Service – Item 7**

The Enterprise M3 Board is asked to:

**AGREE** that the draft fund specification and level of funding set out in this paper are approved.

**1. Background**

- 1.1 The findings of the evaluation of the Funding Escalator in May 2017 demonstrated the ongoing need to support early stage, high growth businesses through the Enterprise M3 Fund Management Service to help meet a gap in funding available to these types of businesses. In May 2017 the Board agreed that work should be undertaken to procure a replacement loan and equity fund to operate across the Enterprise M3 area to avoid a ‘gap’ being left in the market from June 2018 when the current Funding Escalator programme comes to an end.
- 1.2 The procurement process will help provide Enterprise M3 LEP with a cost effective, high quality and flexible provider who can manage the future Fund Management Service. It will also assist in delivering a value for money compliant Contract and demonstrate best practice through a competitive open procurement process.
- 1.3 In September 2017 the Board agreed a proposed funding envelope for this new fund of between £8.5m and £12.5m, noting that sign-off to the approach, level of funding and detailed specification would be sought at the Board Meeting in November 2017. There is available Local Growth Fund and Growing Enterprise Fund available to support this programme at the maximum level and on 16 November, the PMG agreed a recommendation that the fund should be supported with £10m of LGF/GEF.
- 1.4 A procurement of this scale for a replacement loan and equity fund needs to be carried out through an OJEU process. This process is however a fairly lengthy and detailed process and typically takes approximately 9 months to complete. To support this work, a Steering Group consisting of representatives from the Enterprise M3 team and our Accountable Body’s Legal and Procurement teams was formed with consultancy support to help develop the specification.
- 1.5 The main changes to the new fund, recommended by the Steering Group are that it should operate on a revolving basis, with the available funding being re-invested as it is repaid therefore allowing for more businesses to benefit from the funds. A larger fund was also proposed to enable greater economic benefits to be achieved and to support a higher number of businesses. It was also felt that this larger fund would encourage a number of fund managers to bid for the new contract.

**2. Process update**

- 2.1 A stakeholder engagement and information gathering event was held on the 19 October 2017 to help inform the thinking around the new fund. At this event we presented outline fund proposals which received a positive response from participants. There were also a number of helpful suggestions, in particular around how partners can assist in finding and referring businesses to the funds.
- 2.2 Following the stakeholder event, the Steering Group has now produced a finalised Fund Management Procurement Strategy, as required by Hampshire County Council as our

Accountable Body, and is at an advanced stage with the draft Fund Management Service Specification (outlined below).

- 2.3 The Specification is being influenced by a number of strategic documents which are still in the process of being finalised. In particular, these include the Enterprise M3 Strategic Economic Plan (SEP) and work is continuing with the SEP Steering Group to ensure the fund specification aligns with and reflects the aspirations of our new SEP. Additionally, the Specification is likely to need to respond to any significant funding and business support proposals emerging from the Autumn Budget on 22<sup>nd</sup> November 2017. The final version will not be produced until early December to take account of these factors and will be made available to PMG and Board Members once finalised.

### **3. Proposed Enterprise M3 Fund Management specification**

- 3.1 The main proposed terms of the new Enterprise M3 Fund Management Service specification are summarised below.
- 3.2 The Fund Management Service will operate from June 2018 for a period of 10 years with no extensions (with break clauses at 3, 5 and 7 years) to achieve value for money and continuity of financial provision supporting the Enterprise M3 Strategic Economic Plan, Industrial Strategy and Science & Innovation Audit.
- 3.3 The total value of the fund is proposed to be £10m, covering £8.6m for business investment and a value of the contract to the provider of £1.4 million over 10 years. This level of contract value (14% of total) is in line with industry norms and is commercially viable for the provider. This funding will come from the proposed single capital pot being established by Enterprise M3 sourced from both Local Growth Fund and Growing Enterprise Funds.
- 3.4 The Fund Management Service will comprise three financial products: a debt/loan fund, an equity fund and the introduction of a new short-term trade finance fund in response to market need. These will be split on a 60:30:10 funding ratio basis initially although we wish to retain flexibility with these ratios to respond to changing market conditions and will ensure this flexibility is built into the Specification. The ratios are based on our previous experience with the FSE Group and market intelligence and PMG were highly supportive of the need to maintain as much flexibility within the fund as possible.
- 3.5 The new fund will operate on a revolving basis, with the available funding being re-invested as it is repaid therefore allowing for a greater volume of funds to be made available to more businesses on a longer-term basis. This is similar to access to finance arrangements in other areas (e.g. Manchester, Cornwall).
- 3.6 The funds will be targeted at SMEs, comprising start-ups, scale ups and established technology businesses in the broadest sense. Businesses operating in the Enterprise M3 key and niche sectors will also be of importance. These businesses should be early stage SMEs with high growth potential. High growth businesses in non-priority sectors will be considered where there is a compelling case to do so.
- 3.7 Investment from the fund should be for business expansion activities that will deliver significant economic impacts that contribute specific and measurable impacts on the Enterprise M3 strategic targets. However, it is important that the programme is not driven purely by numbers, but also on creating the right investment infrastructure to promote sustainable economic growth across the Enterprise M3 area.
- 3.8 To qualify for a loan/equity funding, the business borrower must:
- Have existing sales and customers (or a clear order book for such) and thus have a proven business concept which has achieved some commercial traction (the fund is designed to support expansion and scaling up of existing businesses)
  - Have clear commercial potential based on either intellectual property rights (IPR) ownership or appropriate licence arrangements where sustainable market penetration is in prospect or other sustainable competitive advantage

- Have a management team that is capable and ambitious with commercial expertise to drive the business forward and achieve projected business growth
- Be a separate private company limited by shares incorporated in the United Kingdom and not an individual or sole trader or partnership of a subsidiary of another entity
- Have legal capacity to enter into all relevant financing and related security documents
- Not be a not-for-profit organisation
- Have a material part of its operations in the Enterprise M3 area
- Require finance to implement expansion activities that will deliver growth impact within the Enterprise M3 area
- Be able to match the investment provided by way of funding from private investors (for equity funding only)

3.9 Higher risk levels of 10 – 12% in line with industry norms are anticipated. The previous Funding Escalator target risk level was 10% but in reality, due to the nature of investments and “good luck”, a default level of only 6% was reported. A priority for the new fund will be to demonstrate higher returns on higher risk investments.

3.10 In terms of outputs and outcomes, the minimum job creation target for the Fund Management Service over the 10-year period is as follows. Other outputs are currently being considered (number of enquiries, number of loans/investments drawn down) and will be included in the final Specification. These targets are in line with current achievement of the existing schemes and provide a cost per job (typically high value) of £23k.

Output indicator	Debt/loan fund target	Equity fund target	Short-term trade fund target
Jobs created/safeguarded	200	100	60

3.11 Investment terms will be proposed by the bidder. Loan pricing is expected to comprise interest on loans, arrangement fees, monitoring fees and legal fees. It is anticipated that each equity investment will be matched by at least an equal amount of private investment.

3.12 The upper limit on loan funding will be increased to £300k per business (from £250k). The investment may be made in stages contingent on achievement of specified milestones and equity finance can be provided more than once per business.

3.13 The involvement of the Enterprise M3 Growth Hub team will be an integral part of the Fund Management Service and delivery, in particular in relation to business referrals and awareness raising. Similarly, the use of a wide range of partners nationally, regionally and locally to help with promotion and awareness raising of the programme is crucial.

3.14 A Fund Investment Committee to review applications and make investment decisions will be established and the Fund Management Service provider must be regulated by the Financial Conduct Authority.

3.15 The Fund Management Service will be aligned with other parts of the local business support network (also national initiatives delivered locally), with particular emphasis on providing SMEs with investment readiness and post-investment support.

3.16 A key consideration for the specification will be ensuring sufficient flexibility so that it can respond to current market and economic needs.

3.17 Appropriate management information needs to be provided to Enterprise M3 to allow them to contract manage the overall performance of the service. This will include reporting to and attending quarterly meetings of the Enterprise M3 Fund Management Service Steering Group which will be represented on a day to day basis by the Enterprise M3 Head of Programmes.

#### 4. Proposed bidding and evaluation process

- 4.1 We are currently working with our Accountable Body Procurement team to finalise the contract bidding and evaluation process. Tenders will be evaluated using a two-stage process. Stage 1 will be a set of pass/fail questions all of which must receive a “pass” to be eligible for the stage two tender evaluation. Stage 2 will evaluate the Quality of bids based on 5 criteria which are summarised:
- 1) **Operations:** Bidders must describe how they will deliver the services and outputs and outcomes for the Fund, and its component three products, as outlined in the specification, including details of staffing and management arrangements
  - 2) **Finance:** A detailed financial plan setting out capital (loan and equity fund) and revenue expenditures and income must be provided. This needs to include the reinvestment of revolving funds.
  - 3) **Outputs and outcomes:** A detailed plan of target outputs and outcomes to be achieved over the three-year period from June 2018 must be set out. Bidders must demonstrate how these will be achieved and when. They also need to state what additional outputs and outcomes will be achieved over and above those stated as a minimum in the specification.
  - 4) **Partnership:** A list of the key partners to be involved in the development and delivery of the service has to be provided, setting out their roles, responsibilities and capacity to deliver.
  - 5) **Quality assurance:** Bidders must demonstrate how quality assurance issues will be managed and how the Investment Committee will operate to ensure the highest levels of scrutiny and that the funding is being allocated appropriately and without prejudice.
- 4.2 Bids will be evaluated against these 5 criteria and we will be asking shortlisted bidders to present their proposals to our evaluation panel. It is intended that representatives of the Enterprise M3 Board will be represented on the panel. The evaluation ratio of the quality of the criteria responses to presentation will be 80:20. Price is not included as part of the evaluation as a fixed contract price applies.

#### 5. Next steps

- 5.1 We are currently working with our Accountable Body to publish an OJEU notice in January 2018. The timescale for the procurement process is as follow:

Date	Event
December	Finalise specification
19/01/2018	Place OJEU Advertisement
20/02/2018	Clarification period ends
05/03/2018	ITT Return – closing date for receipt of tenders
15/03/2018	Presentations by bidders
09/04/2018	Evaluation complete
16/04/2018	Preparation of Standstill Letters complete
26/04/2018	Mandatory Standstill expires
17/05/2018	Contract Award
16/06/2018	Mobilisation
18/06/2018	Contract Commencement

Rachel Barker  
20 November 2017