

Enterprise M3 Board Meeting

28 January 2021

Enterprise M3 Funding Escalator - Item 8

1. Recommendation

- 1.1. The Board is asked to approve the extension of the contract with FSE to continue to manage the EM3 Funding Escalator for a further 2 years, with the option to extend for up to a maximum of a further 5 years in 2023.

2. Overview

- 2.1. The Enterprise M3 Funding Escalator comprises three financial products: medium term loans, trade finance loans and equity investment. The funds address the funding gap identified in the Enterprise M3 area, to scale up fast growing businesses particularly those that are too young to have a credit history. The fund is focused on supporting Enterprise M3's strategic priorities as described in previous Strategic Economic Plans, Local Industrial Strategy, Science and Innovation Audit and most recently the Revive and Renew recovery plan.
- 2.2. The original EM3 Funding Escalator was a £5.5 million fund launched in July 2014. This fund is in portfolio management realisation phase and has begun repayments back to the LEP. Its successor, the Enterprise M3 II Funding Escalator, is a £10 million commitment from Enterprise M3 LEP launched in July 2018 for an initial term of 3 years with the option to extend up to a maximum of 10 years. This fund is making new investments and loans.
- 2.3. Both funds are managed by FSE C.I.C. (FSE), an FCA regulated Fund Manager that specialises in the particular funding needs of SMEs, with the latest contract secured after a public tender process. The FSE Group have been funding scaleup enterprises since 2002 and manage debt and equity funds across the South East, London, Midlands, East of England and Cornwall.
- 2.4. The initial term for the EM3 II fund comes to an end on June 18th 2021. We are required to notify FSE by March 18th 2021 as to whether we wish to extend the term further.

3. Main issues

- 3.1. The fund is generally performing well, especially during recent testing circumstances. There is no performance issue that would motivate seeking a new provider, which would also create significant extra work in carrying out a complex procurement exercise at a time when the core LEP team capacity is already stretched.
- 3.2. The FSE Group has circa £200m under management and works with investors from both the private and public sectors. This includes managing funds on behalf of The British Business Bank, Funding London in conjunction with The Mayor of London, as well as working with 18 Local Enterprise Partnerships across the country. They are a reputable partner with an impressive range of clients.
- 3.3. Since inception the LEP has **invested £9.1m** into the fund escalator of which **£1.5m has so far been repaid to the LEP.**

- 3.4. The combined funds have so far **assisted 107 businesses**, resulting in **deployment of £9.7m via 80 loans / investments and leveraged additional matched private capital into the LEP area of £26.3m**, effectively multiplying the impact of the LEP's funds by a factor of four. The deployment is greater than drawings due to recycling of debt interest / repayments and equity realisations. In the same period, the schemes have **created or sustained 643 jobs**, allowing for a recent reduction due to CV19.

Fund position as at 31/12/20:

Fund	Start Date	Total LEP commitment £m	Net Drawn* £m	Value of portfolio + cash
EM3 I	20/07/15	5.5	2.5	2.1
EM3 II	20/07/18	10.0	5.1	4.9
Total		15.5	7.6	7.0

*Less £1.5m repayments to LEP

- 3.5. The current portfolio valuation plus cash held in transit stands today at 92% of total cash invested. Given the early stage in the investment cycle and current economic conditions the fund is on track to repay at least the capital invested to the LEP and, depending on share sale values later in the fund's life, may provide a surplus return.
- 3.6. At least the first half of 2021 is likely to pose further challenges to the portfolio. However, it is encouraging that so far there has been no material impact to provision levels. Across the two portfolios the total provisions as at 31/12/20 are 3%. Only 7 capital holidays remain out of a total of 15 original requests. The low provision rate is reflective of the relationship lending approach. The equity portfolio across both funds is valued at a gross multiple of 1.03x investment, which is a good performance given some investments are relatively recent. One equity exit has been made so far at a multiple of 1.5x investment. Further exits are in prospect.
- 3.7. Further detail on the performance of the fund is included in the Appendix.
- 3.8. The relationship between the EM3 LEP and FSE has been consistently very good with quarterly steering groups, chaired by Mike Short and more recently Julie Baker, EM3 Board members, used to monitor performance. The fund will provide essential access to finance to many businesses looking to recover or grow following the pandemic.

4. Next Steps

- 4.1. Taking into account the good performance of the fund, the strong relationship with FSE, current economic uncertainty and the capacity challenges within the core LEP team at this current time, it is recommended that the Board approve extending the term with FSE for a further two years to July 2023. This will take us to 5 years and half of the maximum 10 years available under the current OJEU procurement arrangement.
- 4.2. It is proposed that the LEP will undertake an independent review of the fund in late 2022 to provide the LEP Board with a full assessment of performance with a view to taking a decision on the remaining 5 years available at the January 2023 Board meeting.

Rob Dunford
Director, Business Delivery
21 January 2021