FIN(4)FW018
Finance Wales Inquiry
Response from Simon Thelwall-Jones

I write following the invitation to comment on the recent publication of the Access To Finance Review Stage 2 Review ("the Report").

As a "Big 4" trained Member of The Institute Of Chartered Accountants Corporate Finance Faculty, with over 20 years Corporate Finance experience, and having been an Investment Director for one of the EU supported English Regional Venture Capital Institutions, who now provides advice to similar UK Government & EU supported Regional Venture Capital institutions, I feel I am well qualified to comment on the issue of whether Finance Wales was charging higher Interest rates than it needed to.

First and foremost, Investment success is about correctly pricing the risk associated with the underlying dynamics of the business concerned. Most companies financed by Finance Wales and other Regional Venture Capital Institutions are small, often under-capitalised/under-invested, companies with extremely high risk characteristics:-

- Weak market positions (e.g. facing bigger competitors, buying from a small number of larger more powerful suppliers, few barriers to entry and few, if any, true "USPs")
- Management Teams lacking ["blue-chip"] business experience
- Offering little by way of tangible assets for security collateral purposes

Consequently, in the context of the European Commission Guidelines on Loan Margins ("the Guidelines"), set out on page 36 of the Report, I personally would characterise the vast majority of companies backed by Finance Wales as having a rating between a "B" and "CCC" Rating and offering low levels of collateral.

Based on the Guidelines I would suggest that an interest rate of 10.00% + would be most appropriate.

In addition, if one over-lays the economic climate since mid-2008, when as a practitioner who is involved in turning around companies, it was virtually impossible to obtain any finance for a period of 12 months, or to forecast with any degree of certainty the likely levels of demand for the products and services of a number of SME clients, then it is actually arguable whether Finance Wales were in fact charging a high enough interest rate to reflect the risk that they were taking.

In fact, it is my considered opinion, that in a number of instances Finance Wales were, and in some cases continue to, take risks much more akin to Equity risks, despite offering companies Loan products. These Equity risks would ordinarily necessitate business owners giving up a percentage share of the ownership of their businesses. In my experience, the need to give up a percentage share of the ownership of ones business is by far a bigger reason why SME owners do not take on finance, rather than high interest rates.

In summary, therefore, I do not believe, based on my 20 years of experience, that the interest rates charged by Finance Wales have in any way been excessive, as they have been fairly priced given the risk characteristics of the businesses that have been supported, and have, in fact, stimulated economic activity amongst Welsh SME businesses which would not have taken on Equity investment had this been offered.

Furthermore, based on my personal experiences of trying to raise finance for SMEs all over the UK, I believe that since mid 2008 Finance Wales has been the primary supporter of Welsh SME businesses.

I cannot, therefore agree that “Finance Wales should be scrapped”, as suggested by one recent BBC on-line headline.

As an organisation, Finance Wales has done a great deal for Welsh SMEs, and such a suggestion is, to my mind, pure folly.

Finally, I would like to make two further points.

Firstly, as the economic climate improves, it will be possible for Welsh SME businesses to re-finance their Loans from Finance Wales with more mainstream Bank finance at lower interest rates. The cost to most businesses of re-financing Finance Wales’s investment will, therefore, be a very modest 1-2% early repayment fee.

Finance Wales will therefore have done an excellent job of supporting Welsh SME businesses through a prolonged period of illiquidity in the mainstream Banking market and if the interest rates that it seeks to charge are no longer competitive, because of market forces, they will come down if Finance Wales is to continue to lend.

Secondly, what would have been the assessment of Finance Wales if the organisation had simply “given” money to Welsh SMEs, which had then been lost due to inappropriate risk and reward pricing? There are a plethora of under-performing Regional VC companies which will not return money to the UK Government or to the EU.

Is it not better to have a self-sustaining Regional Financial Institution, capable of continual re-investment, rather than one that squanders £100-£200m of UK and EU Taxpayers money?

Please feel free to contact me should you want any further input.

Best regards

Yours faithfully

Simon

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