

The MJ Achievement Awards 2017

Innovation in Finance Submission:

Venture Capital Fund to help deliver
business growth and return a profit within
County Durham



Business B
Durham D

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Summary

- 1 Finance Durham Fund (FD), is a newly established £20m venture capital fund to help deliver business growth and return a profit within County Durham. Developed and managed by Business Durham (BD), which delivers financially sustainable economic development activities, FD may take direct equity stakes in businesses ranging from £200,000 to £700,000 rather than distribute grants. As part of a drive for greater commercialisation, this innovative approach to providing finance for businesses is boosting inward investment and business growth within the county by taking a more patient view to investment and providing an evergreen fund.

Background

- 2 Durham County Council (DCC) became a unitary authority in 2009 as part of Local Government Reorganisation (LGR). The number one priority for the new council is the economy, to help businesses create wealth, more and better jobs and attract greater levels of economic investment into the area. Therefore, it set up a new and bespoke service to focus on this area: Business Durham.

What is the council doing through Business Durham?

- 3 BD, whilst still part of the council, operates under an independent brand and identity. Its aim is to create an environment that attracts and supports businesses to create wealth and jobs in County Durham, whilst at the same time becoming increasingly financially self-sufficient from profitably letting commercial property.

- 4 BD operates DCC's industrial and office property portfolio. In total, this equates to 50,938m² split across industrial units (30,725m²), offices (11,962m²) and North East England's only science park NETPark (8,701m²). The portfolio is 87% full, an increase from 72% three years ago and is funding the delivery of £1 million worth of economic development and business engagement.
- 5 Operating as the economic development company for County Durham, BD supports start-ups and SME expansion, inward investment and raising the profile of the area. It provides a business engagement programme that covers a range of areas from starting up, upscaling ideas, relocating, and securing property and funding. Against a backdrop of a wide geographical area with a very dispersed population and settlement pattern, it also helps to facilitate networking between businesses. Operating as a commercial entity enables BD to develop stronger relationships with its client base and the businesses it engages. The model allows BD to take a real gauge of the economy, as most of its tenants are SMEs and thus act as an early warning regarding changes in the economy.
- 6 Through the engagements and approach led by BD, DCC has helped to attract and retain businesses by investing directly in them. One example is Atom Bank, a start-up full service digital bank accessed by mobile phones and tablets. In 2014 the founders of Atom were looking for funding, and a preferred location to base themselves while they developed their business model, secured Prudential Regulatory Authority approval and built their team. DCC moved several of its teams, including BD out of a building to provide Atom with a base and to enable them to build their business in Durham City. Recognising they were a start-up and still raising funding, DCC took equity shares in lieu of rent, charged at a market rental level with no further incentives.



Atom Bank, a start-up full service digital bank

- 7 To date, Atom has created over 300 jobs and commenced trading in mid 2016. In addition, they have acquired a number of technology businesses, locating them in Durham to integrate with their technology platform.
- 8 PolyPhotonix is another technology business in which DCC has invested money for equity. PolyPhotonix has developed a new non-invasive light based technology to treat and prevent diabetic retinopathy and diabetic macular oedema. The business is a tenant at DCC's science park, NETPark and are in the final stages of getting their Noctura 400 Sleep Mask adopted by health services in the UK, EU and wider afield. They needed the investment to help them achieve this growth ambition. In making the investment in PolyPhotonix, DCC has helped the company to grow, will help to influence its future development plans and will in time provide a financial return on the investment, generating income for DCC via dividend or share sale.



The Noctura 400 Sleep Mask Developed by PolyPhotonix

Developing a new innovative approach to finance for business: Finance Durham

9 In part informed by the experience of investing in Atom and PolyPhotonyx, and recognising the austerity pressures on local authorities, BD sought to develop innovative solutions to developing businesses and attracting investment. It recognised that whilst businesses will accept grants, what they really want is access to finance and to develop partnerships. The council's Cabinet approved the establishment of a £20 million venture capital fund in June 2016, titled Finance Durham Fund (FD). The provision of this commercial finance will also enhance the already attractive proposition that Durham provides to both new and existing businesses. The key features of the fund are as follows:

- The Finance Durham fund will be operated for a commercial return, and able to invest in business located in Durham.

Therefore, FD will support inward investment as well as growth in existing Durham based businesses.

- The investment range is aimed at seed and round A investments with typical amounts between £200,000 and £700,000.
- A range of investment instruments will be used covering debt, equity, and mezzanine.
- The fund is aimed at high growth businesses irrespective of sector.
- The fund will be established as an evergreen fund, meaning that the majority of the monies generated by the investments will be recycled into new investments. Therefore, FD will be able to take a more patient view of investments and thus support a wider range of businesses to grow and exit at a higher value.
- FD will be operated as limited partnership to enable easier expansion and a focus on commercial returns.

- 10 In addition to the direct fund activity, two other elements will be undertaken: the establishment of an access to finance business support (soft side) programme and the creation of a new FCA authorised fund manager as an arms length company of DCC.

Maximising the impact of Finance Durham:

Access to Finance Business Support (Soft Side) Programme

- 11 One of the biggest challenges facing north east business relating to accessing alternative forms of investment, is the awareness of the monies and the skills to be able to realise the benefits from such investments, how to secure the investment and how to use the money once invested, e.g. governance. Therefore, as part of the project, the procured fund management partner will be expected to set up a programme of support to help businesses with these issues. As the fund

is evergreen, this provision will be in place for many years and will not add any additional cost to the public.

Creation of a new Fund Management Company (newco)

- 12 As part of the establishment of FD, DCC will be creating its own fund management company, which will secure Financial Conduct Authority (FCA) authorisation and take over the operation of the commercial fund. In the medium term, the new company will then be able to raise additional monies to invest further into Durham businesses and perhaps deliver funds for others.

Why are we establishing Finance Durham: Key benefits and results

- Tackles the access to finance needs, skills and competencies of our businesses.
- Recognises the pressures of austerity on the council and the need to move away from grants towards investment. A far greater return is achieved, along with a more sustainable model, by partnering with businesses rather than providing grants.
- Over a ten year modelling period the £20 million fund is anticipated to return £6 million after fund management costs have been accounted for.
- Revenue comes back into the council, creating public value. Over the next 10 years, this is expected to be over £550,000.
- Building on equity investment, successes like Atom Bank, the planned modelling for FD is based on a 10 year period - 5 years for investment and 5 years for managing the portfolio and estimated to support more than 500 companies, make investment in 70 and create over 2,000 jobs by 2027.
- Financial modelling and sound business planning are key, as are having people with the right capabilities in place. The legal structure provides appropriate governance to protect DCC investment whilst ensuring the fund is operated commercially.

An OJEU procurement was undertaken, completing in March 2017 to identify the fund management partner. The full launch of Finance Durham is planned for May 2017.

- Represents council support for innovation and a mature approach to risk that will allow us to take advantage of unique opportunities.
- Businesses receive a higher level of support and advice than they would through a traditional grant, as both parties have a vested interest in their success.
- There is a greater intermediary community active in Durham, facilitating wider growth opportunities for Durham businesses.
- County Durham benefits from a thriving and diverse economy that continues to attract inward investment.
- Further enhancing County Durham as an attractive place to do business continues to provide local jobs.