gambit CORPORATE FINANCE

Covid-19 – Business Support

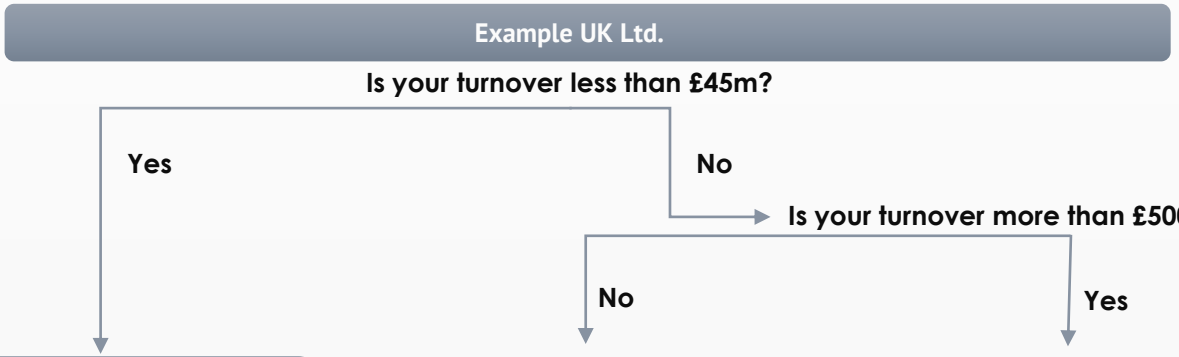
Gambit Update

6th April 2020

Notice to reader – the contents of this circular are subject to frequent changes and interpretations by government and the private sector.

Key Funding Schemes - Update

The UK government updated the Covid-19 funding schemes available to UK businesses on 3rd April 2020. The Chancellor has sought to address one of the key systematic constraints by dropping the requirement for viable companies to have initially attempted to obtain a commercial loan from their banks, now they can apply for CBILS from the outset. In addition, banks will now also be restricted from requesting personal guarantees for facilities below £250,000, although for amounts higher than this, personal guarantees may be required at the lender's discretion. Below is a chart detailing the latest options available to UK businesses experiencing Covid-19 related disruption:



Coronavirus Business Interruption Loan Scheme ("CBILS")

- CBILS is a business financial support scheme established for businesses with turnover of up to £45m
- Lenders benefit from a government-backed guarantee against 80% of the new outstanding facility balance
- Facilities of up to £5m are available and are interest free for the first 12 months
- Businesses must evidence signs of Covid-19 disruption and prove a viable business case in the longer term, with viability based on 2019 debt capacity
- The scheme is being coordinated by the British Business Bank and is supported by 40 lenders
- The 80% guarantee from the UK government seeks to ensure that marginal business cases are supported
- Flexible lending terms should provide businesses with the liquidity to trade through Covid-19

Coronavirus Large Business Interruption Loan Scheme ("CLBILS")

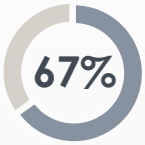
- CLBILS was announced on 3rd April in response to the lack of support for those caught between CBILS and CCFF, the 'squeezed middle'
- Latest information from UK Finance suggests that interest may be payable by the business from 'day one', unlike the CBILS scheme, where the government will pay the interest costs for the first 12 months
- Further details of the scheme will be announced later this month
- The new initiative will allow companies with turnover of between £45m and £500m to borrow amounts up to £25m
- As with CBILS, 80% of the new outstanding facility balance is expected to be guaranteed by the UK government
- Loans backed by a guarantee under CLBILS will be offered at commercial rates of interest
- It is hoped that CLBILS will assist some of the c.5,000 businesses which fall into this category

Covid Commercial Financing Facility ("CCFF")

- CCFF is a scheme launched by the Bank of England ("BoE") to ensure that large firms have sufficient liquidity to bridge the disruption caused by Covid-19
- The funding consists of the purchase of commercial paper (a short-term bond) of up to one-year maturity from firms making a material contribution to the UK economy
- To be eligible, the business must have had, prior to being affected by Covid-19, a short or long-term investment grade rating, although the eligibility criteria may be broadened
- It is hoped that CCFF will support corporate finance markets overall and ease the supply of credit to all firms by reducing the risk of a 'torpedo insolvency'
- CCFF aims to support Britain's largest employers and it is hoped that the scheme will help to safeguard the UK jobs market, taking the strain away from other schemes for those hardest hit by Covid-19

Key Funding Schemes – The Reality

Despite the best intentions of the UK government, businesses are likely to continue their struggle in prising the billions in relief that has been pledged to those in distress as a direct result of Covid-19. The heart of the problem remains the same; delivery of cashflow through an uncomplicated and efficient process. This requires a change in mindset on behalf of the nominated financial partners which, as institutions, are prone to process and excessive collateral requests. Below is a snapshot of how this mindset continues to contribute to a combination of issues which need to be bridged in order to mitigate the effects that Covid-19 is inflicting on the UK economy:



Of SMEs believe that CBILS funds will not reach them before Easter (April 12)

Source: MarketFinance (25/03/20)

£90m

Of loans have been approved by CBILS since its launch on 23rd March

Source: Financial Times (02/04/20)

130,000

Applications from companies for business interruption loans

Source: UK Finance (03/04/20)

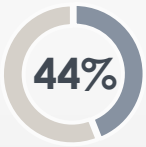
983

Businesses have managed to obtain a loan through CBILS

Source: The Independent (03/04/20)

Of SMEs reported a fall in revenues of between 40-50% in March

Source: MarketFinance (25/03/20)



Of businesses expect to furlough at least 50% of their workforce

Source: British Chamber of Commerce (02/04/20)

950,000

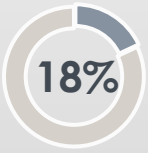
Have applied for universal credit in the last fortnight

Source: The Guardian (01/04/20)

15%

Forecasted fall in UK economic output for the period from April to June

Source: Capital Economics (03/04/20)



Of businesses have less than a month's worth of cash in reserve

Source: British Chamber of Commerce (02/04/20)

44%

Of businesses have between one and three months of cash in reserve

Source: British Chamber of Commerce (02/04/20)

36.0

UK PMI data for March (readings below 50 indicate contraction)

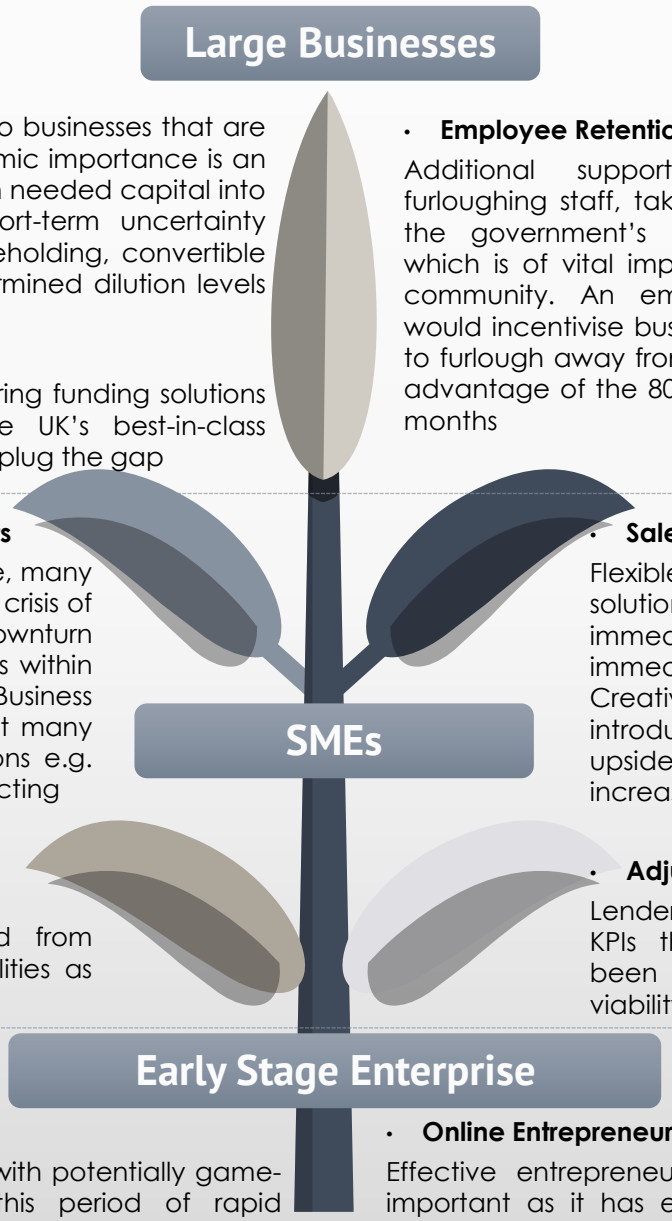
Source: BBC News

The peak of Covid-19 in the UK is expected in June and July

Source: Imperial College London

The Solutions Spectrum

There is a requirement for both the Public and Private sector to look beyond the existing measures and seek to provide a spectrum of solutions that caters to a wide range of businesses. A more collaborative approach is needed. The recent feat of converting London's Excel Centre into the World's largest critical care unit was done through existing synergies between both public and private resources. Further proof that a collaborative effort often yields the most effective results. Below we have outlined some solutions that could be introduced at every stage of business, through a cohesive approach by both the Public and Private sectors.



Large Businesses

- **Equity stakes**

Introducing equity stakes into businesses that are of critical social and economic importance is an effective way to inject much needed capital into businesses experiencing short-term uncertainty though direct minority shareholding, convertible bonds or grants at predetermined dilution levels

- **Use of FinTechs**

As the efficiencies of delivering funding solutions is brought into focus, the UK's best-in-class FinTech industry can help to plug the gap

- **Employee Retention Grant**

Additional support for businesses not furloughing staff, taking the strain away from the government's Job Retention Scheme, which is of vital importance to the UK's SME community. An employee retention grant would incentivise businesses who do not need to furlough away from doing so simply to take advantage of the 80% salary subsidy for three months

SMEs

- **Business Reinvention Grants**

In this period of rapid change, many businesses face an existential crisis of sorts. For many, the current downturn simply amplifies existing issues within their organisation. A Business Reinvention grant could assist many in making important transitions e.g. from physical to online transacting

- **Enhance Existing Facilities**

Further flexibility is required from funders through existing facilities as well as new advances

- **Sale & Leaseback Solutions**

Flexible sale and leaseback solutions would allow for an immediate cash injection, easing immediate cashflow pressures. Creative structures could be introduced, such as potential upside from any onward sale or increase in market value

- **Adjusted Metrics**

Lenders need to look beyond the KPIs that have been historically been used to assess business viability and creditworthiness

Early Stage Enterprise

- **Entrepreneurship Grants**

Support for entrepreneurs with potentially game-changing inventions in this period of rapid change. The grant would provide vital financial resource to set up a website, begin production and deliver their product/service to market. An emphasis would be placed on those businesses with a scientific/digital focus given the nature of the current environment. Such support will assist sustainability upon an economic rebound

- **Online Entrepreneur Incubators**

Effective entrepreneurial activity is perhaps as important as it has ever been. The solutions to assist in managing this period of heightened disruption may come from world-class entrepreneurial incubator systems. These initiatives should not be put aside. Instead, existing "acceleration programmes" should continue to attract significant private and public sector investment, continuing online

Solutions in Focus - Update

We would welcome the opportunity to engage with key stakeholders and ensure that all potential avenues are explored as we look to mitigate the effects of Covid-19 on the UK economy. Further to the ideas outlined, we have re-assessed four areas that could yield short-term benefits:

Enhance Existing Facilities

- At large, banks are dealing with existing customers and, therefore, have the benefit of a track record, positive KYC checks and management information
- Existing facilities should be reviewed, with relaxed repayment terms for loans (i.e. capital repayment holidays) and ignoring covenants with an immediate impact
- Rather than expose businesses to the rigour of introducing a new loan, enhancements could be made to existing facilities, such as:
    - Increasing the advanced rate from an invoice discounting facility from c.75% to 90% and extending the 'allowable period' by 30 days
    - Automatic overdraft increases of 10-15%
    - Extension of proactive supply chain finance facilities to SMEs which allow for faster payment
    - More efficient and deliverable bond facilities
    - Topping up property mortgages

Use FinTechs

- The UK is the leading global FinTech hub with a thriving ecosystem and international talent pool spanning the whole country
- Mainstream lenders are struggling to process the large number of applications for CBILS, potentially jeopardising the financial security of SMEs
- FinTechs are already working with the UK government to diversify the source of funding to SMEs and they want to continue to help
- A taskforce has been established which includes FinTechs 'Wisefunding', 'Nimbla' and 'NorthRow'
- Even before the Covid-19 crisis, SMEs were struggling to access enough credit, with over £59bn in unmet lending needs (*Source: The Fintech Times*)
- FinTechs should be used to facilitate improved access to the schemes through turnkey lending platforms, risk assessment support and KYC checks to expedite the allocation of funding

Adjust Metrics

- The vast majority of lenders' financial performance metrics have limited use in the current environment
- Increased collaboration between lenders to identify transparent, achievable KPIs to assess struggling businesses is vitally important
- Greater emphasis could be placed on averages or run rates of key measures such as EBITDA to assess debt capacity
- In addition, multiples of expenses such as utility bills or wages could be used to gauge a clearer picture of funding requirements
- Protections via quick review of overdrawn director's accounts, dividend strips, CCJs and HMRC liabilities

Introduce Equity Stakes

- By taking an equity stake in firms in distress, the government could shore up balance sheets over the current period of disruption and assist those with insufficient debt capacity
- An equity stake would add a layer of protection to the taxpayer, ensuring that there is an upside benefit upon economic recovery
- Equity stakes could also provide a convertible position to banks or government, which could subsequently be bought out
- Locally, the Development Bank of Wales can assist by managing these cases within their investment portfolio team
- Upon an economic rebound, companies would have a sense of impetus to buy-out their position, returning shares to private ownership

Economic Resilience Fund

- A £500m Economic Resilience Fund ("ERF") has been announced by Welsh Assembly Government, aiming to plug the gaps in the UK government's support schemes
- A new £100m Development Bank of Wales fund has also been made available for companies experiencing cashflow issues as a result of Covid-19
- Grants of £10,000 for micro-businesses and of up to £100,000 for SMEs are also available, as is support for larger Welsh companies of critical social or economic importance (to be determined on a case-by-case basis)
- In collaboration with Welsh Assembly Government, the solutions outlined in this document could be introduced through the ERF

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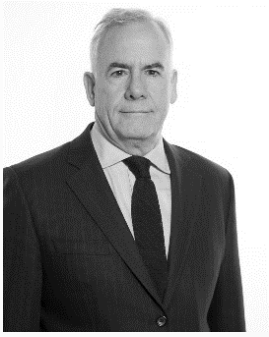

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Gambit Corporate Finance

Established in 1992, Gambit is an independent corporate finance advisory firm specialising in advising private and public companies on mid-market transactions in the UK and overseas. With offices in London and Cardiff, Gambit is widely recognised as a market leader in M&A advice having built up detailed industry knowledge and an enviable track record in deal origination and execution.

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