

Commercial Finance Opportunities

Alternative Fixed Income Opportunities



Prestige Funds - OpenTalks
SME Lending in a post Coronavirus World

Interview with Craig Reeves - Founder, Prestige Capital Management

Mark Goldman - Director, Nucleus Commercial Finance

What is Prestige Funds - OpenTalks?

Prestige Funds - OpenTalks is a periodic publication by Prestige Asset Management, in which we interview key members of the Prestige Funds investment management team and dedicated, specialist Finance Arrangers which provide vital funding to Small and Medium Size Enterprises (SMEs).

We hope this provides a useful and somewhat unique insight into how specific areas of the economy and Prestige operate. The idea is to share with existing and future clients the challenges and opportunities that members of our team see in their field and beyond.

The Topic

The growth of SME sectors and the Coronavirus challenge

How important is the SME sector to the overall economy, including as a source of employment and an engine of productivity? What is going to happen to this sector during the year of the Coronavirus? How do lending firms manage their risk in such a vast and diverse environment?



Introduction

The UK has approximately 5.7 million SMEs and they remain an extremely important part of the economy, accounting for over three quarters of its economic activity and most jobs. But, as a sector, it remains harder to access, including via public markets.

SMEs are turning to non-traditional sources of finance for their capital requirements, a trend that has been occurring over the past decade. This has included lending from peer-to-peer platforms, equity finance and specialist lending organisations like those that are part of the Prestige group of companies.

The SME market in the UK has remained robust and has continued to grow in importance since the 2016 Brexit vote. It includes many world-leading sectors, including the UK's much-admired alternative energy and information technology expertise.

SOURCES:

<https://developmenteconomics.co.uk/wp-content/uploads/2018/11/sme-santander-devecon-summary-nov18.pdf>

<https://bionic.co.uk/business-essentials/guides/the-role-of-small-businesses-in-the-UK-economy/>

Macro Environment

The Carbon Economy

The United Kingdom has signed into law that it will become a 'carbon neutral' economy by 2050. This includes banning all diesel and petrol powered cars as well as burning coal to generate electricity. This requires many industries, businesses and consumers to change how they operate. It also means that both the government and the private sector must increase spending on upgrading infrastructure and modernisation.

- The UK is aiming to stop burning coal to generate electricity within the next 10 years
- The UK is aiming to source up to 20% of its gas from natural / renewable sources in the next 10 years
- The UK is aiming to stop allowing waste to be buried in landfill sites in the next 15 years
- The UK is aiming to ban the sale of both diesel and petrol vehicles by 2050
- The UK is aiming to be a zero-carbon emission economy by 2050

Both energy and food 'security' are likely to remain top priorities for both UK and European governments and significant 'climate change' initiatives will almost certainly continue to grow in both the public and private sectors, resulting in considerable investment / lending opportunities which exist across a range of strategic sectors.

SOURCES:

<https://www.gov.uk/government/news/uk-becomes-first-major-economy-to-pass-net-zero-emissions-law>

<https://greengb.campaign.gov.uk/>



Macro Environment

The Infrastructure Economy

Investors should take some comfort from the widespread expectation that extensive UK Government financial support will be provided in certain core sectors, including infrastructure, and this sector is key to the continuity and recovery of the economy post-Coronavirus. Most infrastructure assets play an essential role in our society and will be vital in assisting the global economy to get back on its feet. Government policy in this area is likely to be supportive.

With London being the largest city in Europe, demand for more housing and modernised infrastructure continues to grow. The UK Government recently announced over GBP 600 billion of new infrastructure projects in its March 2020 budget. However, while large projects such as London's Cross Rail, Heathrow's Third Runway, Hinkley Point Nuclear Power Station and High-Speed Rail 2 have previously dominated the headlines and consumed much public money and resource, there remain many smaller, regional projects that continue to be announced requiring contractors, specialist services and funding to be provided.

Despite the fact approximately 92% of British companies do not work outside the UK and Services represent approximately 80% of the UK economy, the country exports more Services than any other country in the world other than the USA.

Rising Population

The United Kingdom has a population of approximately 64 million people, of whom 8 million were born overseas and net immigration has been running at around 1,000 people per day. Some estimates suggest it is also the most densely populated country in Europe.

SOURCES:

National Infrastructure Delivery Plan 2016-2021
Infrastructure and Projects Authority Reporting to HM Treasury and Cabinet Office
https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/520086/2904569_nidp_deliveryplan.pdf

NOTE: All figures are approximate and subject to change without notice.

Prestige & Nucleus

Established in 2007, Prestige consists of several companies under common ownership and control. Prestige Funds specialises in lending to UK and US SMEs across a range of sectors and has its own dedicated, Finance Arrangers. The collective in-house skills and expertise both within the Prestige Fund team and its dedicated, specialist Finance Arrangers have accumulated over many years, and the business has expanded with the addition of new personnel from the commercial banking sector and other areas of the specialist finance industry.

One of these dedicated, specialist Finance Arrangers is London based Nucleus Commercial Finance, which oversees generic lending activity in the UK SME market. Established in 2011, it employs over 70 people and has lent over GBP 1.4 billion to several thousand small and medium enterprises. Among the lending products it uses are:

- Construction / infrastructure finance
- Asset-based lending
- Property finance
- Cash flow finance
- Business cash advances
- Invoice finance

It should be emphasised that commercial lending to SMEs requires a highly sophisticated operation, able to accurately assess the credit risk of opportunities while possessing excellent knowledge of the dynamics of specific SME sectors.

At the time of writing the SME sector in the UK - and the wider global economy - is addressing the social and economic challenges of the COVID-19 Coronavirus. This research document also considers how smaller companies may weather some of the challenges posed by this issue.

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Q. What does the SME sector look like in the UK?

At the start of 2019 there were more than 5.7 million private businesses in the UK. SMEs, which are defined as companies with less than 250 employees, make up 60% of the private sector jobs in the UK. Some 99.9% of private sector businesses in the UK are SMEs and, according to the SME Finance Monitor, over 80% of them are profitable.

Going into the start of 2020, 37% of SMEs reported that they had grown over the last year. While we do not expect this can be replicated in 2020, it still points to a sector that was able to enjoy profitable growth at a time when the UK economy was under considerable pressure during the Brexit debate.

The centre of gravity for SMEs lies in the south of England, with a large concentration in London and the surrounding counties. London alone has 1,544 businesses for every 10,000 adult residents. Since 2010 London has also seen the fastest increase in the number of new SMEs, with a rise of 52%, and it remains an area of focus for us at Prestige.

Q. Why do UK SMEs deal with your lending companies rather than going to banks?

The growth in the importance of the SME sector in the UK has been paralleled by the withdrawal of top tier bank funding from the sector, especially after the Great Financial Crisis of 2008-09. The number of businesses in the country has increased every year since 2000, except for a small contraction over the period 2017-2018.

This has created a demand for private finance within the UK SME sector, which has been filling the gap left by commercial banks in the period since 2010. This demand has originated from both government and non-government sources, including peer-to-peer frameworks and dedicated private lending operations like Prestige Funds.

Approximately a quarter of the UK Bank branch network has closed over the past five years and prior to Coronavirus, one in ten small companies could get a loan from a traditional bank lender.

**“AT PRESTIGE WE
HAVE BEEN INVOLVED
IN SME LENDING FOR
OVER 12 YEARS”**

SOURCES:

<https://publications.parliament.uk/pa/cm201719/cmselect/cmbeis/807/807.pdf>

http://www.bva-bdrc.com/wp-content/uploads/2020/03/BVABDRC_SME_Finance_Monitor_Q4_2019_FINAL.pdf

BBC / The Economist

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Q. Which areas of the large SME economy do you focus on at Prestige?

At Prestige we have been involved in SME lending for over 12 years. During that time, we have developed a wide awareness of the dynamics of sub-sectors within SME that we understand and where we see good prospects. We are not a universal SME lender, and since the Brexit vote and the onset of the Coronavirus we have focused on businesses that distinguish themselves with robust characteristics and little international exposure. This includes areas of the economy now designated as essential by the UK government, including the groceries sector, pharmacies and food delivery. We have avoided or scaled back exposure in hotels and the wider tourism sector.

We have been increasing our exposure within the IT space as it assumes more importance, but we don't fund technology or startups. It should be noted that the UK has one of the biggest tech sectors in the world and, if anything, the latest crisis has demonstrated how we as a civilisation are becoming more reliant on the digital sphere, depending on companies in the SME market for integrated logistics and e-commerce.

“THE LATEST CRISIS HAS DEMONSTRATED HOW WE AS A CIVILISATION ARE BECOMING MORE RELIANT ON THE DIGITAL SPHERE”

SOURCE: <https://www.ons.gov.uk/businessindustryandtrade/business/activitysizeandlocation>



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Q. Are there any areas you seek to avoid?

We have always avoided lending in vice sectors like pornography, defence, the legal sector and the financial services industry. These are either businesses that we do not want to be associated with or that we feel would be difficult or risky to lend to.

We constantly review the market and, as the situation changes, we will add or remove sectors. This might be across our entire range of corporate lending products or just as it relates to one particular product.

TRADE EXAMPLES

www.prestigefunds.marketing/wp-content/uploads/CFO-Finance-Trade-Examples.pdf

www.prestigefunds.marketing/wp-content/uploads/CFO-Finance-Trade-Examples-Q2-2020.pdf

Q. How is the COVID-19 virus impacting the market?

The SME sector is critically important to the UK: the government is taking unprecedented steps to preserve it and support employers in the market. There had already been some concerns about how the departure of the UK from the EU would impact on SMEs. The companies we lend to were very well prepared for this, with most having little to no exposure to cross-border trade (indeed, only 11% of UK SMEs trade internationally, according to the SME Monitor). Not only that, but strategic level preparations for Brexit have meant that many SMEs were already taking steps to protect themselves against a period of anticipated economic uncertainty before the virus struck.

The UK economy remains heavily dependent on its SME sector, as we have seen from the government's reaction to the onset of the COVID-19 virus in the country. This has included a wide range of support measures including cash grants and business rates reductions. These initiatives represent an unprecedented range of support measures for smaller companies and also reveal how much the UK values this segment of its economy.

SOURCE:

<https://www.gov.uk/government/news/billion-pound-support-package-for-innovative-firms-hit-by-Coronavirus>

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Q. Are SMEs prepared to meet this kind of operational challenge?

Of course, the Coronavirus pandemic represents an even more severe challenge than Brexit. But looking at 2019 figures from Merchant Savvy, for example, we can see that many SMEs have either a partial or fully remote workforce. Even before the pandemic, a large slice of this sector was already functioning in such a way that a lockdown by the government could be shrugged off. This is in line with a flexible working trend which sees the UK above the median, with 68% of UK companies now offering flexible working terms. This compares with a global average of around 62%; by contrast 59% of Italian companies offer flexible working practices.

Such high levels of adaptability are going to be essential if the sector is going to survive these challenges and emerge strongly on the other side.

Q. What sort of steps are you taking to manage risk during this period?

At Prestige, we have necessarily tightened our lending criteria and are managing new underwriting very tightly, as we must do during periods of economic uncertainty. Our traditional asset-backed lending business is evaluated daily, so we can maintain a very strict process of verifications and approvals with applications. We are also working closely with borrowers to help their businesses access government funding programmes. We are confident that the vast bulk of our lending clients will emerge from the current crisis and continue to grow their businesses successfully in the future.

On top of this, Prestige has invested heavily in its technological resources in the past few years, with an automatic underwriting capability which allows its financing firms to gather information more quickly and with less scope for input errors. This lets the firm review a much wider array of credit metrics, increasing the speed of analysis and removing some companies from the underwriting queue before they go in front of an analyst.

Prestige's financing companies have been able to seamlessly integrate their risk teams with their finance and collections teams, delivering better risk management and reporting, and giving its internal lending committees a much better overview of the total risk in the portfolio.

SOURCE: <https://www.merchantsavvy.co.uk/uk-sme-data-stats-charts/>

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Q. Where do you get your funding from?

Our dedicated, specialist SME Finance Arranger - Nucleus - is currently funded by three groups which include a dedicated, listed Prestige fund and two large UK-based Banks/Financial Institutions. Currently Nucleus is in advanced discussions with a large banking group to establish a debt finance portfolio and become a fourth debt funder to the group.

Q. Why do these groups give you debt to lend?

We believe, going forward in some areas, we have identified opportunities to lend money at premium rates to quality borrowers who are willing to put even better assets as collateral, given the lack of funding opportunities elsewhere. We believe in some cases we can take advantage of this situation by further improving the quality of our investments, without having to sacrifice returns. Indeed, some areas have probably never been more attractive.

This is perhaps exemplified by the fact that both our dedicated, specialist Finance Arrangers are in discussions with other larger financial institutions which wish to establish their own significant debt finance facilities (managed accounts). They are looking at this situation from the perspective of 3, 6 and 12 months forward from now when some greater levels of normality and stability will be in place.

What the world will be left with is many cuts, bruises and scars, but also USD 8 trillion of monetary and fiscal stimulus underpinning getting people back to work. Spending on government-led infrastructure in the UK, USA and Europe will potentially be at record levels over the next two to three years.

Q. What is your lending capacity?

Given the size of the marketplace and the general lack of funding provided by traditional banks to SMEs, we believe we can responsibly lend GBP 10-30 million per month across our different funding sectors, although this is not linear, and some will be seasonal and cyclical.

Q. How big is your team?

The Prestige Funds team consists of approximately 40 people based in two main locations (UK and Malta) and two satellite locations (Luxembourg and Cayman).

Our dedicated, specialist Finance Arranger (Nucleus) operates with a team of approximately 70 people in two main locations (UK and India).

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SOURCE: The Economist / Prestige

NOTE: All figures are approximate and subject to change without notice.

Prestige Funds - OpenTalks

Q. How much have you lent?

Our dedicated, specialist Finance Arranger Nucleus has lent approximately GBP 1.4 billion / USD 1.75 billion over the last decade.

Q. Where do you get loan customers from?

Our dedicated, specialist Finance Arranger Nucleus has been in business for almost 10 years. It has a large existing customer base, sales team, website, local/sector brand recognition and a network of intermediaries who, between them, introduce hundreds of transactions a year.

Q. How do you select loan customers?

Our dedicated, specialist Finance Arranger Nucleus operates with sophisticated loan origination and underwriting processes. Extensive customer / sector profiling, filtering and evaluation are undertaken before even reaching a credit committee or specialist underwriting team, resulting in up to 90 loan requests out of 100 being rejected.

Q. Do you only lend to companies or individuals as well?

Both Prestige Funds and our dedicated, specialist Finance Arranger Nucleus only lend to private companies.

Q. Do you buy existing loans from other banks?

We do not buy loans from other groups, and we do not operate as a loan platform or exchange although we have sold loans from time to time. All our loans are a result of our origination and underwriting.



Mark Goldman

Mark joined Nucleus as a Director in 2012 after a career spanning over 30 years in global fixed income markets. In 2005, he joined Mitsubishi UFJ Securities International in London as Managing Director and Head of Fixed Income. He created the Strategic Trading Group, which focused on short and long-term proprietary trading as well as the Quantitative Analysis Group and introduced a new risk and settlement system for the Fixed Income group. Previously a Managing Director for BNP Paribas and a member of the European Executive Committee and, prior to BNP, he spent six years at Nomura International, where he was again a member of the European Executive Committee responsible for European Fixed Income Sales. He was instrumental in capital-raising for Nomura's direct European investments through structured vehicles. His career commenced in New York in 1981 in Merrill Lynch's International Fixed Income Department. After five years in New York, he transferred to Europe to run the German Fixed Income Sales business in Frankfurt, where he was responsible for building Merrill's sales, trading and origination effort. In 1992, he moved to London as the Head of European Fixed Income Sales and became a member of Merrill's European Executive Committee.

He has a Bachelor of Arts degree in History and German from Harpur College, SUNY Binghamton, a Master's in Comparative Literature from SUNY Binghamton and a Master's in International Business Management from Thunderbird, the American Graduate School of International Business in Glendale, Arizona.



Craig Reeves

Craig is a Director and Founder of Prestige Capital Management Limited, Prestige Fund Management Limited, Prestige Asset Distribution Limited and Prestige International Marketing Services Limited and is a Board Director of various international Prestige Funds. He is also a Director of Nucleus Holdings Limited and is a co-founder and nonexecutive director of OpenFunds Investment Services AG. Formerly Managing Director and co-founder of Platinum Capital Management Limited (an international asset management group). Formerly Head of Portfolio Management and Asset Allocation at Titan Capital Management Limited (an international asset management group). Prior experience as a Proprietary Trader at Gaiacorp Trading Limited (an international asset management group), Proprietary Trader at London Currency Exchange Limited (a private client / proprietary trading house) and an internship at Bank of America (London). He has also previously provided retained consultancy services to a large London-based international family office, a large London-based international stock broker, a London-based pension consulting group and a London-based international real estate investment group.

He has over 25 years' experience in financial services as a professional investment manager, trader and investor of alternative investments, hedge funds, capital markets and real estate and has written several articles for various financial publications journals including the AIMA Journal. He has served as a Board Director on over 20 international Funds. He graduated with a BA (Hons) in Business Administration from Huddersfield University and a Higher National Diploma in Business and Finance from University of Greenwich (London). He also attended the New York Institute of Finance (NYIF) where he studied various financial markets and derivative trading courses and is also a member of the Chartered Institute for Securities and Investment (CISI).

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About Prestige

Founded in 2007, Prestige consists of several companies under common ownership and control focusing on investment management / operation / administration / marketing and direct lending businesses with offices in UK, Malta, Luxembourg and Cayman.

Prestige specialises in direct lending to small businesses primarily in the United Kingdom and United States. It owns equity stakes in several dedicated, specialist “Finance Arrangers”, amongst these Nucleus Commercial Finance, which has existed since 2011, and has lent approximately GBP 1.4 billion to over 6,000 customers, representing thousands of transactions.

Financing areas include asset finance, project finance, invoice finance and specialist commercial finance. Prestige currently manages approximately USD 1 billion of assets for approximately 300 international financial advisory and institutional investor groups.



Prestige celebrated its 10 year anniversary in 2017 and has raised USD 2 billion from a diverse range of international investors.



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