



Economic Affairs Scrutiny Panel Innovation Fund Review hearing with Jersey Business

WEDNESDAY, 6th FEBRUARY 2013

Panel:

Deputy S.G. Luce of St. Martin (Chairman)
Connétable S.W. Pallett of St. Brelade (Vice-Chairman)
Connétable M.J. Paddock of St. Ouen

Witnesses:

Chairman, Jersey Business
Chief Executive, Jersey Business

[10:01]

Deputy S.G. Luce of St. Martin (Chairman):

Welcome everybody to the second hearing this morning on the review of the Jersey Innovation Fund. For the benefit of the tape we will just whizz round the table, if we may again, and introduce ourselves. My name is Deputy Steve Luce, Chairman of the Economic Affairs Scrutiny Panel.

The Deputy of St. Martin:

Okay, thank you very much for that. Just for those members of the public who are here, if you are leaving please do quietly and obviously all mobile phones and electronic devices to be switched to silent or off please. Gentlemen, thanks for coming in this morning. The topic, as you well know, is the proposed Innovation Fund, which is a new initiative from E.D. (Economic Development) and we are speaking this morning to three sections of people who are outside or at arm's length from government to try and get a view from the other side of the fence, so to speak. This morning we

have already spoken to David Warr from the Chamber of Commerce and later on this morning we are talking to Digital Jersey. We felt it important to talk to you, gentlemen, especially Andy with his experience with Jersey Business Venture because the Innovation Fund by definition is hopefully to innovate new business and create more jobs and stimulate the economy here in Jersey. I suppose the first question is: we presume that you are in favour of this, you see it as a good idea and you see it as a way of moving forward and stimulating the economy.

Chairman, Jersey Business:

Maybe it would be helpful, Mr Chairman, if we just gave you a little bit of background on Jersey Business and how we were established and where we stand now and how we feel that our objectives fit with the Innovation Fund. I mean, as you know, Jersey Business was set up in November 2011 and it was set up to combine the functions of Jersey Enterprise, which was an organisation within Economic Development, along with the activities of Jersey Business Ventures, which was funded by an E.D.D. grant but whose main purpose, as you know, was to support local business. Our board was formed in February 2012 following an Appointment Commission process. We have 6 independent directors, all of them are what I would call very successful local entrepreneurs and, as I said to them often, they are probably the best board I have ever served on in terms of the breadth of experience and also their youth, I might add. The successful entrepreneurs are all locally based. Andy Cook joined us as our chief executive in September 2012. Andy, as you know by background, is a qualified accountant and has very extensive background in local business. And, as you mentioned earlier, Mr Chairman, is the founding and first chief executive of Jersey Business Venture set up many years ago. We have since last April/May been recruiting staff and setting ourselves up. We will shortly have 6 executives on our staff along with Mr Cook. We have opened offices at 31 The Parade, which we share with Digital Jersey. We are funded by Economic Development, by an annual grant of approximately £700,000 per year. We have a partnership agreement with E.D.D. and our goals and objectives I would say are absolutely aligned with the States growth and diversification strategy, in other words proposition P.55. Our role then is to support the creation and development of enterprise for the social and economic benefit of Jersey. Our objectives are, again, very much in line with the objectives of the Innovation Fund. We are to encourage innovation and improve Jersey's international competitiveness. We are to grow and diversify the financial services sector capacity and profitability. We are to create new businesses in employment in high value sectors and to raise the productivity of the whole economy and reduce reliance on inward migration. In answer to your question, Mr Chairman, we support the Minister for Treasury and Resources' proposition, P.124, that is the Jersey Innovation Fund.

The Deputy of St. Martin:

If I can just pick up on one particular point you raised there towards the end of that short presentation. You mentioned high value and the need for Jersey or Jersey Business' view moving towards creating high value jobs and stuff like that. Could I ask Andy how he sees that in light of innovation? Are we going to have to target our innovation, if you like, specifically the high value? Is there not a need to say we have to be more general when it comes to innovation?

Chief Executive, Jersey Business:

I think the point about innovation for me and where you get this high value bit is twofold. One is in terms of its relative potential because it does not always work out, but potential ability to contribute to the economy for the amount of resources that it consumes. So if you take a small retail shop, it has a relatively low value in terms of the economy relative to the amount of resources that it consumes locally. If you took a highly dynamic digital business that has the potential of a global market place, what it consumes locally is relatively small in proportion to the return that you get. So for me one part is the high value in terms of how the business sits within the economic environment. The other one, where the word "high value" is attributed, is to people. The bit about innovation, and I do not believe this is an absolute rule, but I think, and people have different views, but what I believe happens in reality is that you do need a level of very creative entrepreneurial wealth generators. They might be the business owners, they might be the business holders of the idea but by supporting their endeavours what you then get is that wider spread because they are not doing all the work down below and we need to create jobs across our overall economy. But how do you get to that? Do you get that really by having those innovators that are able to stimulate a business model, the needs and resource to do something, and that is where you get in terms of our - particularly in terms of recruitment - recruitment locally may be at a lower level but that suits our economy so I think the Innovation Fund is right to focus on high value and I think the economic strategy overall is right to focus on that because you can almost ask yourself the other way round: why would you not? So I think from the Island's economy point of view that is right. That does not set aside the need to support and develop businesses, if I can put it this way, in the ordinary walk of life.

The Deputy of St. Martin:

If I understand what you are saying here is that you see the Innovation Fund being targeted towards rather established and larger business as opposed to start-ups and one or two-man bands because you feel that to generate the high value side of it the business already needs to exist and the entrepreneur is at a different level.

Chief Executive, Jersey Business:

No, it is not a matter that the business needs to exist. I do not go with that because an awful lot of new business and innovative things are going to be new businesses. What I think is it needs a certain type of entrepreneurial culture to create those businesses and by doing so it then draws in people across the wider economy. In terms of start-up, it is an often used expression that has such a breadth of meaning that start up is everything from what we will see ... 80 per cent of what we will do is guys who want to come, it is a one-man band, it is what we call a microbusiness, 2 or three people. It could also be someone who is looking at a start-up of a £10 million capitalised business. That is a start-up. So just the start-up is, I think, a bit of a loose term. What we are talking about perhaps in terms of the Innovation Fund, as I understand it, and that I have it all nailed down, I do not, is that they are really looking for the businesses that can create the opportunity to give a greater return more than a standard ... more than the average, perhaps that is the way to put it.

The Connétable of St. Brelade:

The comment made by the Minister that he is expecting 70 per cent of businesses that innovation money is given to to fail, which suggests to me that this money is not going to be going to existing businesses because you do not want existing businesses to fail. What would be your comment on his statement?

Chairman, Jersey Business:

I think the question is how much risk is the Innovation Fund going to take on? If we take, and Andy knows very well the cross-section of the people who come to Jersey Business for advice, as Andy has indicated, 70 per cent of them are fairly small businesses. Some of them have some good ideas, some of them have some awful ideas. Part of our job is to encourage the people with awful ideas to perhaps seek a job. There are an increasing number of larger businesses, and I would say the turnover is £500,000, £1 million, £2 million, who come to us for advice, mainly seeking money. Mainly seeking investment of one sort or another. Can we put them in touch with someone who might be able to fund them? Our role at the moment, because we do not have the ability to make grants or to arrange loans or whatever, is to assist them with their business planning, their documentation and to help them meet potential investors. Would the Innovation Fund be part of that process? It could very well be. I think the Innovation Fund, the first threshold question is, is the States prepared to put up funding to invest in innovation, as described in the proposition, and then how would that be executed? Would it be executed with the assistance organisations like ours or Digital Jersey or through its own board, or whatever? There are many ways that those funds could be earmarked and invested and there are many existing organisations that can take part in determining the confidence with which an investment could be made.

The Connétable of St. Brelade:

You say businesses are coming to you looking for investment, which obviously a lot of businesses do need investment, but is the Innovation Fund the right port of call for businesses that are just looking for extra investment? Basically what I am saying to you is, is that what you would term “innovative”. All they are looking for is money to ...

Chairman, Jersey Business:

No, we are generalising here and I think with any investment process if you say funding is available, and this is the criteria under which we will entertain making loans or grants for investment, you are going to get a huge variety of people coming, and you are unable at this stage to predict exactly what the form of that variety will be. You can shape it by saying: “We are looking for businesses that are in the biomedical field or in the environmental field or in the digital field” or whatever. Then you can further shave it by saying: “We are only interested in brand new businesses that are starting up or businesses that exist that are extending into a new area, or larger scale businesses that are looking for further support.” There is a wide range of potential funding requirements here but the starting point is: is the States prepared to stimulate innovation through the establishment of a fund as proposed? And our starting point is yes. We think it should.

[10:15]

The Connétable of St. Brelade:

What you are saying is you see innovation as a very wide-ranging issue, it is not just, for example, a lot of people have looked at the digital industry where a lot of these potential new ideas may come from. But you see it as wide-ranging. It could be a local company involved in the tourism industry.

Chairman, Jersey Business:

What I am saying is that it is difficult to predict. There are a number of companies here that we have come across who have ideas ranging from the mundane to what I would call the innovative to the highly innovative, and there are degrees of risk associated with all of them and so on.

The Deputy of St. Martin:

In hindsight, do you think the word “innovation” was the wrong one to choose for the name of the fund? Would we have been better using the word “stimulus”?

Chairman, Jersey Business:

No, I think “innovation” is a good description of what we, as a community, are trying to accomplish.

Chief Executive, Jersey Business:

Can I come back to the Constable's point? I would invite people, you keep hearing this expression "new business" and you ask: "Is this about new business or does that exclude local business?" I would invite you to perhaps consider it like this. For me these things are about new ventures so if we had a long established finance firm that got together with a long established retailer and decided that between the 2 of them they are going to come up with a new way in which they are going to make payments. A typical thing at the moment, I suspect you even heard it this morning, payments through your phone. If those 2 came together, they are both existing businesses, and I suspect they would have a separate entity they might do this under, but they would be creating a new venture. I do not believe for one second it is one or the other. It is not all about new businesses. It is not all about established businesses. It could be an established business that has nothing to do with anyone else and what it is going to do is quite simply radically different and innovative. As far as I know there is no preclusion on one thing to another. I think that it is quite likely that the larger proposals will tend to come off the back of some more robust base. That could be a joint venture, that could be it happens to be a larger organisation. That is sort of where the reality lies. So new ventures would tend to be a more meaningful way of looking at it.

The Connétable of St. Brelade:

That is an interesting point because I think there has been some misunderstanding of what people understand to be innovation, which is why we are asking what you consider "innovation" to be. You use the word there several times, "venture". Is that not really a truer reflection of what this is? This is venture capital rather than innovative capital? I think we need to distinguish between the 2.

Chief Executive, Jersey Business:

You ask the comment about: "Is this established businesses or just new businesses?" and for me it is the principle of doing something new regardless of where the baseline is. The second one is the Deputy asked whether "innovation", is that the right sort of expression. I am a great believer, things are horses for courses. So in this particular circumstance the proposal is a fund that will support the development of frankly new ideas, not the repeat of existing ideas. The distinction would be a retailer that is here, a retailer that is there, to me would in itself not be an innovative move. It might be a business move or it could be a new venture. But does it hit the criteria of what we are doing is trying to develop something that has a greater potential for return in its wider sense, be that financial, be that employment but for the economic benefit of the Island, that to me was really what this particular fund is about.

The Connétable of St. Brelade:

Are some of those businesses that you mentioned could possibly be local businesses, will that investment generate the sort of return on the fund that would allow that fund to be replenishing

because if we are looking at, and I am only repeating what the Minister said, a possible 70% failure rate, you are going to need some of these businesses to give you a fairly high return.

Chairman, Jersey Business:

There is another aspect of that and, as we read the Innovation Fund proposition, there is a phase one which is the fund will make loans or grants and phase two, subject to States approval, it will make an equity investment. If you make a loan to someone and you put a rate of interest on it, your return is pretty well defined. If 70 per cent of those loans fail where you are going to end up is also pretty well defined. If, on the other hand, those loans are attached to performance related bonuses or participation and it has been noted that a number of funds do invest on that basis, in other words they either accept royalties or some sort of performance-related reward then there is an enhanced return perhaps. But ultimately the fund in order to be self-sustaining is going to have to make equity investments. It is going to have to make investments in which it participates in the success to the degree that the people who are running the business participate and the others they all must participate.

The Connétable of St. Brelade:

So really what you are saying there is in terms of the first tranche of money and how it is going to work, in terms of this being a replenishing fund, it will not be replenishing under a loan scheme. What you are saying is it will only survive if it is equity based.

Chairman, Jersey Business:

Banks make loans based on security. The reason they make loans based on security is it does not take very long to figure out that if you loan a bunch of people £1 million at 5 per cent interest you are making £20,000, if one of them happens to lose £200,000 and you cannot recover it, it is going to take you in excess of five years to get that money back, so there is a very natural caution as to how you lend money and the security against which you secure your investment. This Innovation Fund is not looking to be a bank, as we understand it, in the sense it is looking for collateral. It is looking for as much certainty as it can obtain as to the outcome of the investment but ultimately it is going to be shaped more or less like what we see as a venture capital fund down the stream. It will be a combination of loans, it will be a combination of subordinated debt. It will be a combination of preference debt, it will be a combination of equity and the question is: what is the return on that investment?

The Connétable of St. Brelade:

Is the outcome, in terms of success, not reliant on what financial return is going to be to that fund? And I think of some of the comments the Minister for Treasury and Resources made; is the outcome more important that we create a large amount of jobs or jobs rather than you are going to

get a good financial return on it? Is that something you see as being ... because the other comment the Minister for Treasury and Resources made, which I think is important, is he did not see this as a first tranche of money, there could be other money available and he used the phrase ...

The Deputy of St. Martin:

Another shot of capital.

The Connétable of St. Brelade:

If it does not work.

Chairman, Jersey Business:

You can create jobs by subsidising them. It is done in many economies. There certainly are some very prime examples of that. The question is are they sustainable, are those jobs sustainable? If you give X amount of money to the economy and want the businesses in the economy to hire people will those jobs remain if that subsidy is withdrawn? In other words, will the jobs become productive and become a part of the businesses to which the subsidy is directed? We do not view this as a subsidy; a subsidising process just to create jobs. We view this as an opportunity for investment to be made which will create jobs.

The Deputy of St. Martin:

Can I go straight on to another point then? The first part of this Innovation Fund is for loans and grants. On the basis of what you just said, how do you feel about granting money as opposed to loaning money?

Chief Executive, Jersey Business:

These are personal views rather than necessarily representative of the full board of J.B.L. (Jersey Business Limited). I believe there is a place for both but it should be defined and understood why you are doing it. So, for me, for example, I hope that later in this year to bring forward proposals where we would have the capacity to make very small sums available for local start-ups and we are talking the £500 whatever, putting a great deal of administration around that to get people going. You can picture where I am coming at from here. I am talking about locals trying to do something there. Putting a great deal and making it into a loan and we are going to go in and take their TV back or whatever. That to me is an appropriate place where, subject to the right due diligence, and I want to come back to that, that a grant is appropriate. If someone is looking at a business model and they want to develop whatever it is, and for me, and this is not a view held everywhere, they need an open mind, whether it is in the agricultural industry and the tourism industry, the digital sector or anywhere else. They should have a business proposal that you are

funding into that as an investment panel you believe on the basis of probability that it will work, because if you do not believe that why are you investing in it, be it grant, be it loan, be it equity, at which point that business must be able to withstand taking on a loan. I think that is the bit for me about this fund, and I accept if I have it wrong I have it wrong, but if you are capable of going to the bank and meeting all of the bank's and the investment house's criteria then why are you not? What the difference for me is, is that there are scenarios and I would say we see them - I will not say daily - weekly where there are potentially very good commercial ideas that would add real value. Our role perhaps is to try and shape those ideas around the business plan that might be considerably better than what comes in the first time round, but there are things lacking in terms of borrowing. Generally, speaking that is exactly what Peter has just said, which is the collateral criteria. In days gone past the banks might lend on collateral or they might lend against earnings, today, make absolutely no mistake, yes, you need those earnings and a business plan that says this is a viable business, but on top of that you need the collateral. For a lot of particularly younger business or young entrepreneurs and new ventures that collateral is not here. You have to get past it.

The Connétable of St. Brelade:

What you were saying, is the lending criteria for banks over the last five or 6 years has tightened. I presume the same will be for private investors as well.

Chief Executive, Jersey Business:

Yes.

The Connétable of St. Brelade:

I think what you are saying is rather than this being a - I hate the phrase - "fund of last resort". It is not really a fund of last resort. It is a fund of last hope.

Chief Executive, Jersey Business:

No. Sorry, I would rather pull that around and say that this is the fund that recognises the opportunities that cannot be serviced elsewhere.

The Connétable of St. Brelade:

So you do not like the "last resort" bit?

Chief Executive, Jersey Business:

No, I do not.

Chairman, Jersey Business:

No.

The Connétable of St. Brelade:

No, I do not either.

Chief Executive, Jersey Business:

Because for me if you can get your funding through the ordinary supply of finance I do not understand why you would not be.

The Connétable of St. Ouen:

What, in your experience, does the success rate of what you have experienced, can you put a ...?

Chief Executive, Jersey Business:

Yes, I can. There were lots of figures bandied round and I have just heard you refer to the Minister for Economic Development saying that perhaps there could be a 70 per cent failure rate. Peter would know better than I but if a venture capital fund had a 70 per cent failure rate it would not be around very long. It seems exceptionally high. I think that is a pessimistic figure. This would be my personal view. I believe that is a pessimistic figure. The why is because it is about the criteria to invest. It is all about the due diligence you start with. If you had some sort of automatic right to the fund, in other words: "I have an idea, I have written a few things down on paper, now I am eligible for the money", I suspect 70 per cent will be very low. But that is not how it works. Nothing in here suggests to me that is how it is proposed whatsoever.

[10:30]

The reality is, and I will just slip in where I see how Jersey Business fits into this, organisations that make an application to the Innovation Fund must do so in exactly the same way as if they were going for any other robust application, as though they were going for any other type of funding. The panel that sits as part of the Innovation Fund must review it in exactly that way. They may have a preference towards digital, for example, a bias to that because they want to stimulate that side of the economy. As long as you have that mechanism in place and you are judging it ... only investing into something that you fundamentally believe is going to work, I can tell you that my understanding of the bank failure rate, in other words where they have to make a claim against equity, is 15 per cent. In the banking sector commercial lending, the amount of lending that they have to do, where they effectively land up going and doing some kind of repossession to get the assets back, to get the capital back, my understanding is that figure is around 15 per cent, I would

encourage you to take a more accurate from someone in the banking sector, but that is my understanding.

The Deputy of St. Martin:

Can I just come back at you then and say, I understand where you are coming from and the need for the people who want to access this fund to come up with the same sort of information as they would do if they went to the bank and what have you. But is Jersey Business the conduit, if you like, for the person with the great idea but no business experience?

Chairman, Jersey Business:

It could be. It could be very well. That is pretty much what we do day in and day out, is to assist people, as I said in my opening remarks, with their business plans and with the development of their business. We are advisers. Some of our advice is pretty sharp and short but we typically work with companies over many weeks and months to try and help them develop their plan. This could be part of the process. There is, in terms of the proposed workings of the review panel, that process as well. In other words they are obligated, as I read it, to review business plans and that is the kind of thing that we could assist with presentation or we could be a conduit for that funding, it all depends.

The Connétable of St. Brelade:

Presumably somebody has applied to the fund and they have received money and their business is up and running, what role do you see Jersey Business playing in monitoring that business once it is set up?

Chief Executive, Jersey Business:

I must start by saying we have not had a specific conversation with Economic Development in relation to a specific role for Jersey Business Limited under the Innovation Fund. There has not been a formal conversation. We have had some various comments that have gone in the general terms and in the general makeup of Jersey Business Limited. For me there are 2 parts. One is in this run up to how you make an application. In terms of the fund, I am a great believer in the concrete ceiling. I think we have a role internally, particularly at the executive level within Jersey Business, where we should work thoroughly with organisations to get them in the right place to be making an application. It is what we do every day. At the moment it may be that that application is to ... it might be for venture capital, it might be for a loan from a bank, it could be to private investors. I think we have the resource there, we are - by "we" given most of it is ... at the moment our staff is coming in, it is probably me - we are very honest, probably brutally honest, and we have to be. I can give you a very clear example of that of what I think is a very good business proposal, I have no doubt whatsoever that when the fund is up that it will be heading that way, and

the toughest thing that I had to say to this gentleman was the first thing he needed to do is step down. "Everything is good about the business bar you", because if you are going to invest a lot of money, you are investing in the product, the concept, but the management, you have to believe it can deliver the job in hand. "You need to step aside, take that technology role, bring someone in who can manage it" because it is an international business. But if you are an investor you are looking at those things. You need to believe in the various aspects that this business is going to work. So I think on the way in, I have made the analogy before that we could have the role of being the father of the bride, so we will walk them up the aisle, but we are not actually going to marry them. I see that is where we can do that, we can work with them, so that what we are getting is as good as quality presentation and expression, which may not be the forte of someone who has a very good business idea.

The Deputy of St. Martin:

Would I be right in assuming then, from what you have just said, that you see the number of people coming to you as not necessarily changing very much? Just that in your portfolio of options for them you all of a sudden are going to have another one available inasmuch as the Innovation Fund will be there alongside banks and alongside private funding.

Chief Executive, Jersey Business:

I do not think it will stay still. I think it will go up. The reason is, it is a very basic one, if you put a sign outside your door saying: "Come and get money here" you will tend to have a fairly long queue, even if we are there to help get them. The point perhaps, the way that I would look at it, is: is that a good thing, is it the area that we will earn our keep where we will do better at adding value? Yes.

The Connétable of St. Brelade:

Jersey Business obviously has a set budget of £700,000. If your roles expanded, I mean you mentioned being father of the bride, bringing businesses forward, if you are asked by E.D.D. to provide a monitoring role, could that be done within your existing budget or would you have to ...

Chairman, Jersey Business:

I will speak for the organisation here. Yes, I think it could. Given the staff that we have brought on board, given Andy's background, given our board, given our access to outside mentors and advisers to assist us, I think we could play that role. That is the role we are playing and I think it could be expanded without expense.

The Connétable of St. Brelade:

Do you think that would be very much a role for the expertise you have on the board currently and the connected entrepreneurs and experience and expertise?

Chairman, Jersey Business:

There is not a single person on that board who has not gone through the process of raising capital loans for a new business.

The Connétable of St. Brelade:

And also acts as mentors for some of these companies?

Chief Executive, Jersey Business:

I can add a bit to that. Within our business plan, which is available online should you find the desire to read it, we are already proposing to create a structure to deliver mentoring into the business environment. I am quite careful about how I am trying to say that. There have been several versions of mentoring through the business community. I can absolutely promise you that each business organisation, whether you are talking about Chamber, the Institute of Directors, JADO (Jersey Association of Directors and Officers), ICSA (Institute of Chartered Secretaries and Administrators), et cetera, all are very keen, their members are very keen, to be involved with supporting other businesses and that is a terrific benefit of an Island like Jersey that has that kind of resource in such a small environment. My concern with, and our involvement, will always be that we create a process by which that is managed. That the enthusiasm does not wane at the end of month 2. That you do not have a cross between an organisation over here who he happens just to be a non-exec on some competing organisation you just matched up. It needs to be a fairly sort of robust organisation around that. That is something that we will bring forward as the year goes on. I have no problem at all in seeing how that could work very well with ongoing support in terms of businesses that have received support under the Innovation Fund.

The Connétable of St. Brelade:

In terms of that monitoring or that mentoring, which would be an important part of supporting a business, do you see any role to play for Jersey Business in monitoring the financial success of the company, or do you see that role outside into another?

Chief Executive, Jersey Business:

To be honest with you, you are splitting hairs. There is no such thing as a successful business that does not eventually have ... there is not a line of sight to somewhere where it is making profits.

The Connétable of St. Brelade:

What I am driving at is if there is a problem within a company do you see it your role to highlight that to E.D.D. and say: "This company is not going in the right direction, we need to look at it"?

Chief Executive, Jersey Business:

As it stands now, it is a discussion that has not been had so I think it is fair to say if we were to have that discussion I see no reason why that is a difficulty, primarily because in those particular circumstances E.D.D. would be making a loan in this case based on that condition. In other circumstances ... I am sorry, I am saying it could be built so it is conditional upon X, Y, Z. In other circumstances we would have shared no information about the businesses that we see. I share no information with the board of Jersey Business regarding the businesses we see because there are potential conflicts left, right and centre.

The Connétable of St. Brelade:

But that monitoring is not outside the bounds or remit of ...

Chief Executive, Jersey Business:

No. And the calibre of staff that are coming in is ...

The Connétable of St. Ouen:

Do you gentlemen think that governments should be in the business of loaning money? Do you think we are ... perhaps Andy's experience in this class might be ...

Chairman, Jersey Business:

I think the government should be in the business of funding enterprise. How it funds enterprise, whether it does it through the Innovation Fund as it is proposed, which is part loans and ultimately part equity and some mixture, or whether it does it through investment with other investors, be they private or other public entities, or they do it in conjunction with other funds. In other words, gain leverage, the £5 million becomes £10 million because someone else is also co-investing with you, is the question. Government could initiate it but is it the best executor of investment and investment policy? Traditionally not. Traditionally it is a very poor investor. Can it improve that through the proposed structure in the Innovation Fund proposition? Yes, it can. Can it improve that through drawing on expertise as is anticipated outside of that panel? Yes, it can. Can it do that by co-venturing with other investors? Yes, it can. I mean there is a wide open opportunity here. The first thing is, is the Government prepared to earmark the money and then how is the Government going to control the investment, in terms of how it is made and how it is followed up and how its success or failure is judged.

The Deputy of St. Martin:

Could I just take us back to something you said earlier, which I found very heartening. I have to say I think on this side of the table we were getting a little bit concerned that the fund might be this “fund of last resort”, which I know we are trying to do down a bit. But we felt that by the time you had been through the potential for a bank application and with the amount of money available locally from private or high net-worth individuals who are looking to invest, we were wondering whether this Innovation Fund, because you had to make sure that to fulfil the criteria you had no other options but the fund, we wondered whether the people who would come to us would be such a last resort that the chances of success would be limited. I am encouraged to hear that you said that you see a number of people who do not have the collateral to fit into a bank or to a private loan situation. So my question would be: given that you gentlemen do see some people who will be, you hope, looking to this fund, have you any idea the sort of numbers we could be talking about because we are hearing huge divergence on whether ...

Chairman, Jersey Business:

Divergence in what sense?

The Deputy of St. Martin:

The difference in the numbers that ...

Chief Executive, Jersey Business:

Potential numbers.

The Deputy of St. Martin:

... may be looking or have a chance of success with an application to the fund.

Chairman, Jersey Business:

I could find within a week an allocation of all £5 million.

The Deputy of St. Martin:

Are you in a position to suggest over how many different applications that would be?

Chairman, Jersey Business:

We could go out and find a very good applicant who could make a business case for a £5 million investment. Absolutely. Is that the best way to invest the fund? Undoubtedly not. Would there be 50 people applying for £20,000 or £50,000 or £250,000? You do not know until you open the door

and establish the fact that the funding is there and establish the criteria under which the applications will be assessed and evaluated and the process through which people have to go.

[10:45]

You do not know what is out there. We do know from our direct experience that there are a considerable number of people with good ideas who are having difficulty raising finance. No investor, if they invest in equity, wants to be necessarily the sole investor in an enterprise. You traditionally want to put some money in equity and you want that enterprise to be able to raise a loan or, in other words, to leverage your equity investment. At the moment the banks, in part because of the economy, and in a large part because of the capitalisation requirements that are being imposed on them, are simply withdrawing from the supply of credit. They are not doing that because they are not getting good propositions through the door. They are doing it because they have to reduce their own balance sheets. In that economy or in that economic situation can a fund like this assist? Can it accelerate? Can it meet the objectives that we talked about to begin with and are clearly stated in the fund? Yes, it can. But do not preclude the number of people who might come to the fund or the size of the investments they might seek or the quality of the investment that may or may not be made, it is going to take time.

The Deputy of St. Martin:

Should there be a bottom level and a top level for the amount of money that can be taken out of the fund?

Chairman, Jersey Business:

No, I do not think there should.

Chief Executive, Jersey Business:

Can I come back on a number of points and add some comment? You asked whether the States should be a provider of resource? I think for me, any government role in the States of Jersey, they must be about facilitating and trying ... defining policy and facilitating things that will benefit the Island. There are cases, there are certain times in the economic cycle where just facilitating or removing barriers will do something but sometimes you have to have intervention. This is a mechanics of intervention. Is it the right mechanics? I personally believe this time it is. Do I want to see the States trying to get into the world of global investments? No, quite frankly, but that is how I see it. I see this as required intervention because left to itself the markets will not pick up and will not get to the point of supporting businesses that have not proven themselves yet and that is really what it is all about. It is about that collateral and it is about that ... if you have a long track record and you are heavily capitalised you have a good chance of raising the money, so you should not need the Innovation Fund. It is trying to do that. Does the Island need it from an

economic point of view? Yes, because the world is moving on very fast. Yes, we are in a global recession, but the whole point is that is where everything is moving so fast forward. I believe it is right. I think there are other things that the States should do that do not have a direct financial ... as direct an impact of cash and that is other countries are using certain key areas in terms of their tax system, so whether that is tax breaks on investment or whether that is tax breaks on earnings, whichever way round, and I am not for one second going to suggest what the right models are but I do think, over and above the Innovation Fund, which I support wholeheartedly, there are other things that we can do, and at a micro level that comes right down to having some sort of waiver, a better waiver on everything from social security. So Government have control of things they can do. In terms of last resort, I really do guide you to something that Peter has just said, which is where I think this one ticks such a big box is in the shared investment in an organisation where the Constable is a private investor of an organisation that needs £250,000. Bit rich to take all that on, on your own, but you are prepared to do half of it if another, in this case the Innovation Fund, is. You get leverage out of the fund and in the same way that private investor is not going to put in unless someone else is. I think that is what the shape of the larger applications will look like, and I hope it is.

The Deputy of St. Martin:

Can I just take that one step further? In your wide experience, gentlemen, do you feel that this type of fund is administered best where each application is treated on a case by case basis? Or do you think it is important before we start that we say loans will attract the sort of interest at this type of repayment? Do we need to be rigid or is flexibility the key?

Chairman, Jersey Business:

The fund has to be very flexible at this point and I think it has to look at investment on a case by case basis. That is the best way to go about it. Could it direct the objectives of the investment in the sense of saying one of our criteria is how many jobs there are going to be created, how much potential is there here, is this going to be ... if we invest £100,000 and somebody else invests £100,000 is this going to be a £2 million business in three years or is it going to have a £100,000 a year turnover? It may make its return but it may not grow either. So those are all things that can be evaluated. The question ultimately is how does the fund look at potential investment? In other words, how does it do its evaluation? We are, as mankind, very bad getting eight people around a table looking at one thing and coming to a conclusion. Each of us will have a different view. So somebody and some group with very sound business experience are going to have to do the evaluation and someone is going to have to take the risk. It is jumping off a diving board and not knowing whether there is any water in the pool. You do have to assume that risk, but you assume that risk on the basis of a very hard analysis and a very hard review of where the business may go and who the people are who are running the business and who their partners are and who else is

participating. Andy also mentioned the other possible structures, which are alluded to in the appendices to the proposition. In other words, there are a number of ways governments have invested elsewhere in the world and we would certainly urge the States to look at those and to look particularly at structures such as entrepreneurial trusts and venture capital trusts, which are now raising substantial sums of money on the back of government's participation. They are raising 70, 80 per cent additional funds to invest on commonly agreed criteria with the Government. This fund is going to be invested in companies that are going to have some impact on the environment. This fund is going to invest in companies that are primarily digital related. In other words, there is a strong criteria for that investment but the Government money is there to be leveraged by either private investors or other co-investors, as I said earlier. A lot of that will depend upon tax structure. Why should people not be able in Jersey to do what people in the U.K. (United Kingdom) can do and that is to take a certain percentage of their income and put it into an investment and gain a tax credit for that investment? In other words they have immediately gained an advantage to that investment and have the outcome of that investment be relatively tax free. That is a structure that has been proposed. It is a question of whether or not the States are prepared as a precedent to try to invite capital in by giving tax advantages, and that has been discussed in many areas, but these are certainly things that need to be explored. I think, as Andy has said, and I have said, our position in terms of the fund it is a starting point, it is well thought out, there is a structure there, there are a lot of things that need to be experienced in order to understand how the thing is going to be developed but it is a first step and we would encourage the States to agree that first step.

The Connétable of St. Brelade:

We were talking about government roles about 10 minutes ago and we all know, I think, from experience, governments tend to be risk averse when it comes to borrowing money. Two questions, probably split between who is going to answer it, but you did mention early on, you said you were going to make a comment with regard to due diligence and I ask you to make a comment on that. The other one was: in terms of due diligence, I suppose from a point of view of assessing any potential loan this has been a figure of £100,000, which has been put aside for expertise costs. Do you see a possibility not only of that amount of money but the costs involved with E.D.D. running the fund and also potentially yourselves being involved with it that the potential extra cost could overwhelm the fund in terms of what it will cost to physically run it?

Chief Executive, Jersey Business:

I think I know where you are going. In terms of due diligence per se, I guess where I was going with it was my comments about I personally believe that this fund or any other should look at an application with exactly the same eyes as a bank would or a venture capital would. Those eyes change relative to the amount of risk that you wish to take or that you accept to take. As Peter

rightly said, in this day and age the clearing banks have a constraint on their balance sheet, they are all trying now to keep up with that constraint, which is changing, and for all the right reasons that we know of. But in order to do that, that makes them very risk averse. As I say, 10 years ago it was: "Can your business cover the loan?" or: "Do you have the collateral?" kind of one or the other will do. Today, not a chance. It is both down. You need everything tied up. In terms of the due diligence, you have to believe that this is a business that is likely, that the likelihood of success is there. If it is not nobody should be investing in it. I am sorry, that is quite brutal but that is exactly where it should be because that is where you would get to a 70 per cent plus failure rate. You have to have a belief that there is a good likelihood of success. The other part of the due diligence relates all about risk. I think the fund has to be a risk taker. It is not going to get anywhere if it is not because if it applies the same criteria to the extent that you must have the collateral and by the way we would like to see you can prove that you have done it, then there will not be any.

The Deputy of St. Martin:

The Constable's point is though, it is the cost of running the fund; the invisible and visible costs.

Chairman, Jersey Business:

We are running short of time but due diligence consists of four elements in any investment. One is an investment manager or a group of people evaluating whether it is a good business proposition. The second is outside expertise, which may be required if it, for instance, is a highly scientific project. In other words it looks like a good business but I do not understand what this widget is or this micro business crawling around on the screen. The second element of it is: legal. In other words someone has to structure the loan and the documentation that is involved. The last element is the accountant. Somebody has to go in, if it is an existing business particularly, and say: "Fine, we have been presented with audited accounts but are these audited accounts sound?" In other words, to do checks and balances. The last two are a give-up, in the sense that you are going to run that expense in any investment, whether you make it or not, but you do not make that investment until you get the final stage, having done the first two analyses. The expert you only hire if you think there is a good business case. The good business case should be the judgment that is made by the investment panel or managers who are evaluating a sound business plan.

The Connétable of St. Brelade:

But are the potential invisible costs justified to stream the size of the fund?

Chief Executive, Jersey Business:

I think that is the relative point. If you have an operating cost, which is taken within E.D.D. structure, whatever else, your externals, I mean you are talking about a £5 million pot. You have £100,000 for external advisers. I personally think it is right to put that amount of money.

[11:00]

You have to have a figure, does that feel about right given that nobody knows, probably. I mean in terms of our own costs and in terms of - I cannot really speak for E.D. - but the reality is you will only know exactly what it is the year after, at the end of the year. I am not expecting to see an increase disproportionate to what we are set up to do that should drive costs. If it will we land up in a place, and I no doubt do others, where something has to give. So we either cannot do X, Y or Z and we will come back and say: "Here are the options. We need X pounds to be able to do this or something else has to give."

The Deputy of St. Martin:

We are over time and unfortunately the time has flown past a lot quicker than I think any of us would have liked. If I might, I would just like to finish with one question to both of you, if you would just allow me another couple of minutes, and that is quite a simple and straightforward question. How do you define success in regard to this particular fund? Do you have something which you know in the back of your mind will say to you: "Yeah, that was successful and that is the reason why"? Do you have any preconceived ideas of what success looks like?

Chief Executive, Jersey Business:

I bet they are different.

Chairman, Jersey Business:

I think the Chairman should have the last go at that.

Chief Executive, Jersey Business:

I do not think you should measure success by the financial return on the fund because if that is what you want to do go and be a venture capitalist in the big wide world, in the full market. If that is the purpose of the fund then I do not understand it. I think success should be measured by not just the quantity of businesses that it supports because I think that is ridiculous, 10 businesses that are very small is nothing like 10 businesses that are very large. But I think there should be an evaluation of the economic benefit to the Island. That would come through from directly out of the accounts that says they paid X amount of tax. The amount of payroll that it stimulated. So I would be looking more for those measures. To be honest with you, I think in there you should bring in a

level of probability on future earnings as you would do if you are buying a company. I am looking at what its future earnings are. I am not looking at what it did yesterday. I am looking at what it is going to do in the next three or five years. I believe it should be that kind of economic return which whether the actual fund makes a particular amount this year, there is no relationship to it. So that would be my tuppence ha'penny's worth.

The Deputy of St. Martin:

Peter, do you have a similar outlook?

Chairman, Jersey Business:

The longer the business of business. I define this whole area, including what Jersey Business is doing, as venture capital with a social conscience. A social conscience is what Andy has just outlined. It is the creation of jobs, it is payment of tax, it is the development of enterprise activities that assist the community. The venture capital with a social conscience is however absolutely primary. This fund should have an objective and it should have a return on it. Investment objective, whether that is 20 per cent or 10 per cent or 5 per cent, whether it is a return over 5 years or 10 years, is something to be determined but it must have a return on investment criteria otherwise it will have no money very shortly.

The Deputy of St. Martin:

We could go on.

The Connétable of St. Brelade:

It is a good place to finish.

The Deputy of St. Martin:

It is a good place to finish. Some good conclusions there. We are 5 minutes over so I thank you, gentlemen, for your time this morning.

Chief Executive, Jersey Business:

Thank you for seeing us.

The Deputy of St. Martin:

We look forward to seeing you again soon.

[11:04]