FUTURE OF FINANCE

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FUTURE OF FINANCE

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DEBT FINANCE

How to detect a loyal lender among 'fair-weather friends'

Finding the right lender is hard even when trading conditions are favourable. So what makes a good borrowing relationship? And how might the growing need for net-zero investments change matters?

Ouida Taaffe

In his letter to shareholders in April, Jamie Dimon, CEO of JPMorgan Chase, argued that shadow-bank market-makers – including short-term lenders, hedge funds and private equity firms – were "fair-weather friends" to businesses.

"They do not step in to help clients in tough times," he wrote, whereas banks "flex their capital and provide their clients with a lot of loans and liquidity when they really need it".

Dimon cited the liquidity provided by banks in 2020 when the Covid crisis started as an example of this.

If his claims were accurate, businesses would surely be steering well clear of these "fair-weather friends", but non-bank financial intermediation is already big business, having flourished since the global crash of 2007-08. It accounted for 48.3% of financial assets worldwide in 2020, according to an estimate by the Financial Stability Board.

Moreover, as the global crash and more recent incidents such as the demise of Silicon Valley Bank have shown, banks aren't always copper-bottomed. They can also be tentative when certain borrowers approach them for credit.

A recent report by Standard & Poor's notes that regulatory reforms enacted in light of the 2007-08 crash – increasing the capital charges for lending to higher-risk enterprises – have resulted in less bank lending to small and mid-market businesses. The upshot is that the "markets are entering a moment of fundamental transition… Private markets have moved off the sidelines and into the spotlight for multiple industries and sectors."

The report adds that non-bank lenders tend to operate with "a long-term investment horizon", offering customised funding options that can be particularly useful to fast-growing new businesses.

As non-bank lenders become more important players, they are funding larger deals. In May, for instance, British software firm The Access Group raised an £850m add-on to an acquisition facility that was already the largest private credit deal in Europe last year, at £3.5bn. That was despite a lending climate in which access to liquidity in the conventional banking market was limited.

How, then, should CFOs decide the right funding mix for their businesses? And, as more – and more

JPMorgan Chase's Jamie Dimon has been forthright in his criticism of non-bank lenders

Bloomberg via Getty Images

patient – funders will be required across many industries and the regulatory pressure to move towards net zero increases, what makes for a good long-term borrowing relationship anyway?

Well, it turns out that "funding mix" may not be the right way of thinking about it, at least when it comes to bringing together loans from banks and non-bank lenders. For instance, the market has become more bifurcated than Dimon suggested, featuring less direct competition between the two types of lender.

Victor Basta, CEO of DAI Magister, an investment bank specialising in the climate and fintech sectors, explains that non-bank lenders "take on riskier borrowers and can be more dynamic than banks. But they will charge more and can impose covenants that place certain requirements or restrictions on a business."

Some CEOs and CFOs will find such stipulations too much of a constraint on their decision-making power.

The challenging economic environment is clearly making life harder for companies seeking debt finance. For firms that rely on more costly non-bank loans, this is playing out in how these loans are managed, although that does not necessarily mean that borrowers are being pushed into default.

For example, Standard & Poor's reports a rise in payment-in-kind (PIK) loans, which let borrowers make interest payments with equity or further borrowing, rather than cash. They can be a sign of stress, although deals are usually structured to ensure that a PIK option cannot be used to avoid default in a real liquidity crunch. The aim is to use them to cover growth periods when cash flow is tight.

The prospect of growth is vital, of course, because PIK loans are costly. If a company opts to borrow to cover the interest payment, it effectively ends up paying interest on interest. Nonetheless, Standard & Poor's notes that, for some funds in the US, up to 20% of their investments were making PIK payments in Q3 2022.

But what's best for a company that needs to invest in growth, despite unfavourable trading conditions? If non-bank lenders are willing to take payments in kind to help a firm through a growth phase, does that make them better long-term partners than banks? Not necessarily, especially in cases where there are several creditors.

Basta explains: "If you get into trouble as a company, things are easier to resolve if you have a couple of senior banks that hold all the strings. If you are dealing with numerous non-bank lenders with different views, it can be challenging."

But when it comes to raising debt finance to fund the shift towards net zero, CFOs may soon find themselves getting an easier ride.

"A lot of government money is about to become available worldwide, at very low cost, for firms involved in remediating climate change," Basta says. "Depending on what they want to do, they might not have to borrow from the market at all."

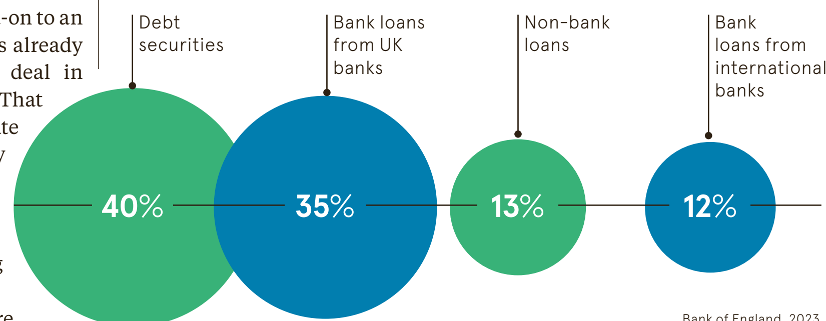
He believes that the blended cost of money to such companies over the next five to 10 years could be more than a third lower overall, predicting that "the cost of debt won't make or break them".

Given that the whole economy has to work towards net zero, the increased availability of cheap public money is likely to shake up funding across the markets. In due course, the closest friends of companies that need loans for essential investment may turn out to be governments, not financial services firms at all. ●

BANKS PROVIDE JUST UNDER HALF OF ALL BUSINESS BORROWING IN THE UK

Composition of the current stock of corporate debt

● Bank lending ● Non-bank lending



Bank of England, 2023

EDITOR'S NOTE

'Don't go chasing fantasy cost-savings by ditching net zero'

UK plc can ill-afford to squander the economic opportunity offered by investing in climate action, but Rishi Sunak evidently doesn't see it that way

When the prime minister announced to the world last month that he wanted the UK to take a "better, more proportionate" approach to reaching its net-zero targets – targets that he then proceeded to push back five years – he ceded ground disastrously in three important areas.

First, Rishi Sunak has just given up the nation's position as a global front-runner in the race to net zero. This aspect of his announcement has attracted the most attention, with independent statutory body the Climate Change Committee stating that the government risks taking the country "further away from being able to meet its legal commitments". Not that such warnings will necessarily faze this administration, of course.

Second, Sunak has also given way to the more rabid among his MPs, including those who've been arguing for some time that the British people are not "cash cows" to be "sacrificed at the altar of a twisted and dogmatic green outlook". Just look at what happened on the previous occasion a prime minister made a similar error of judgement by playing to the backbenches. (If you're not sure precisely which debacle I'm referring to, I'll consider my point made.)

In so doing, Sunak has pawned away something else too. Despite his arguments that pushing back certain net-zero deadlines to 2035 makes good financial sense, saving companies and consumers money, he has further tarnished his party's traditional reputation for being on the side of business and capital.

As Lisa Brankin, chair of Ford UK – which is investing £430m in electric vehicle manufacturing in this country – put it recently: "Our business needs three things from the UK government: ambition, commitment and consistency. A relaxation of 2030 would undermine all three."

This is arguably the most pressing and material aspect of the prime minister's change of policy. Fundamentally, he is sending mixed messages to businesses and investors, potentially restricting the flow of green investment and allowing attention to drift at a time when the economy and the planet can ill-afford this. It is further evidence of an all-too-familiar brand of laissez-faire leadership.

In purely financial terms, too, the move is "baffling", as one leader in the renewable energy sector put it to Raconteur last month. As any salesperson will tell you, urgency is a key motivator and mover of capital, so declaring that your deadlines are a moveable feast is likely to be counterproductive.

And it's not only a question of the investment pipeline. By this time, many companies will either have put their net-zero spending plans in place or started executing them. Examples include investing in more energy-efficient machinery, replacing a petrol-powered fleet with electric vehicles or even retrofitting commercial premises with more effective insulation. Firms that have made such investments will hardly appreciate being told that their efforts sit somewhere on a spectrum ranging from "disproportionate" to "twisted and dogmatic".

So what are these businesses to do? Should they persist with their existing plans or could they potentially scale them back in line with the government's new net-zero timetable to save a bit of cash during these difficult times?

In short, the answer needs to be the former. Funding net zero still matters and ultimately it is still best for CFOs to see achieving this goal as an important investment in their firms' development. There is, after all, a significant competitive advantage in being ahead of the pack when it comes to embracing cleaner technologies and practices. This is a £60bn business opportunity over the next 25 years, according to the Confederation of British Industry. Ignoring that would be myopic in the extreme.

So, no matter what the government says, CFOs mustn't go chasing after fantasy cost savings by ditching or downgrading their net-zero investments. That way madness lies – in the shape of an economic and environmental catastrophe. ●

James Sutton
Deputy reports editor, Raconteur

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PROPERTY ASSETS

Cost in space: the UK's office utilisation conundrum

Many firms that have adopted hybrid working in recent years are facing a tricky efficiency problem: how can they extract maximum value from premises that are seldom fully occupied?

Helen Roxburgh

pidjoe via iStock

The impact of Covid-19 on many British workplaces has been deep and lasting. A Q2 survey of white-collar workers in London by the Centre for Cities revealed that the average respondent was commuting to the office only 2.3 days a week, for instance. The think-tank found that they were spending 41% less time at HQ in total than they had been before the pandemic.

Andrew Farah is CEO of Density, a US software firm specialising in workplace utilisation. He observes that the emergence of hybrid working since the Covid lockdowns were relaxed has been a "seismic shift" that's left much office space underused. His company's research suggests that most premises could accommodate four times more activity than they do.

"We still see big meeting rooms with just one person on a Zoom call and lots of communal spaces that are barely getting used at all," Farah reports.

From a finance chief's point of view, that looks and feels like a serious waste of resources.

Simply moving to smaller premises has been an obvious and popular cost-cutting solution for many firms. One of the most notable companies to have made this choice has been HSBC, which announced plans in June to abandon its skyscraper at London's Canary Wharf for a smaller HQ in the Square Mile.

A flurry of similar moves sparked fears in the real-estate sector about a collapse in the office market, but the reality has been more complex. Seeking a new lease right now, even for smaller premises, may not end up saving CFOs as much money as they might hope.

Richard Proctor, partner and head of London tenant representation at real-estate giant Knight Frank, reports that businesses are "addressing the efficiency of their existing real-estate commitments. We're not seeing a mass release of space, while occupiers assess what space they need and how best it can be used strategically to attract and retain talent."

This efficiency drive has been a long time coming. Research published back in Q4 2018 by workspace consultancy Abintra claimed that firms in England and Wales were collectively wasting £10bn a year by failing to utilise the office space at their disposal. As the cost-of-doing-business crisis wears on, it's no wonder that finance chiefs

> "We still see big meeting rooms with just one person doing a Zoom call and lots of communal spaces that are barely getting used at all

are looking to make their workplaces work harder for them as they exhaust other cost-cutting options.

"We have seen CFOs adjust their focus from reducing costs to optimising every square foot of office space," Farah reports.

In many cases where businesses aren't downsizing or sub-letting, they are thinking more flexibly about their property assets, according to Proctor.

"A trend we're seeing is that some occupiers are renewing leases on shorter terms," he reports. "This enables them to keep their options open as they refine their real-estate strategies for the longer run."

Other companies are considering refurbishments to introduce new amenities and/or more flexible collaborative spaces. That may come at a considerable cost, but the investment could well prove worthwhile if it ensures better utilisation over a longer period.

Standard Chartered, for instance, is revamping its global HQ in London. The banking group's CFO, Andy Halford, predicts that the enhancements will result in a "modern workplace that aligns with our hybrid working model".

Citigroup is also refurbishing its premises in the capital. The US bank believes that this will "maximise collaborative workspaces, supported by technology, to enable us to work flexibly and with maximum agility".

Guy Holden is managing director for European advisory and transaction services at CBRE Group, a US provider of commercial real-estate services. He points out that, while numerous firms "have rethought the use of their offices since the pandemic, driven mostly by their version of hybrid working, it has become clear that "one size does not fit all".

Holden explains: "Everyone is working on their own version of flexibility. Now that employees have a real sense of what that can look like, we see this as a long-term shift in practice. If both employees and employers want something really good, as everyone now does, then real estate has become more important in business decision-making than it ever was."

In July, London-based international law firm HFW relocated to a smaller HQ, which fits well with the working practices it has adopted in recent years, according to managing partner Jeremy Shebson.

"Our new offices are designed to provide greater flexibility and promote formal and informal connections," he says. Although the floor area is 25% smaller than HFW's old base, the new layout is "much more efficient. And, because of our agile working policy in London, which is for people to be here at least three days a week, we actually still have room to continue growing."

Farah says that "the companies we see doing well in the hybrid working world have two things in common: they are adapting constantly to a workforce that's still evolving its preferences and they insist on collecting better data" about the use of commercial space.

Farah's advice to most employers in this respect would be to boost the managerial presence in their offices and create more space for focused work. He reports that one Fortune 500 company recently chose to "hibernate" two underutilised floors at its HQ, cutting occupation costs while "increasing worker engagement" in other parts of the building.

Holden argues that "we must quash this myth that offices are no longer needed – it's quite the opposite. Their ability to increase collaboration, improve productivity and foster company culture should not be underplayed."

Boosting utilisation levels is all about giving people what they want from their workplace, according to Shebson. HFW's management team asked all employees to share their preferences on aspects such as furniture, paint colours and even coffee beans in the new office, as well as consulting them on how they wanted to work.

"For example, rather than having a fixed desk, everyone can choose from a range of settings, including open-plan team spaces and smaller 'focus rooms', based on how they want to work that day," he says. "That's been a big positive change."

And, as finance chiefs reassess all elements of their premises, they'll undoubtedly need to work closely with their C-suite colleagues.

"The ultimate objective for many CFOs", Farah says, "is to transform the office from a financial burden into a strategic asset."

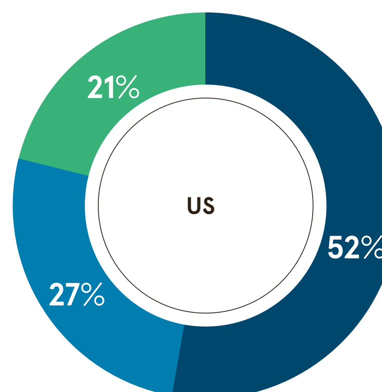
A project with such an ambitious goal should never be attempted by any one function working alone.

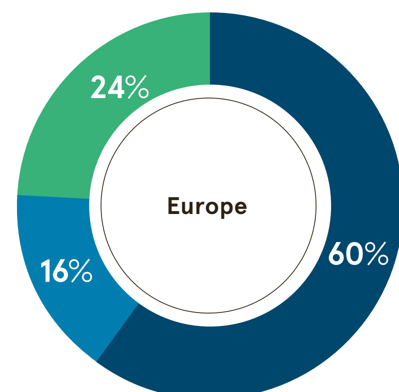
MOST FIRMS IN THE WEST ARE PLANNING TO REDUCE THEIR OFFICE SPACE

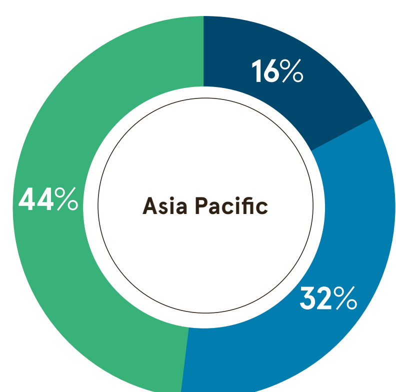
Businesses' expected changes to their real-estate portfolios over the next three years

CBRE Group, 2023

● Contraction ● No change ● Expansion







Commercial feature

Why ESG must be top of CFOs' agendas for 2024

ESG strategy and reporting are set to become priorities for finance teams in 2024. CFOs must take the lead on this journey

CFOs already have enough on their plates, but over the next 12 months they will also take on an increasingly important task: responsibility for ESG strategy and reporting. This will be fairly new territory for many CFOs, and it can be a difficult task to decipher how the alphabet soup of acronyms, mountains of data and a multitude of stakeholders all comes together.

Jamie Benaron, advisory director at VantagePoint, warns that companies must grasp the ESG opportunity in order to get ahead of their competitors, while also understanding that this investment is vital to their top-line growth.

To cope with these added pressures, many finance departments will need to undergo a digital transformation, and CFOs will also need to ensure that the entire business understands the ESG roadmap and the importance of sustainability within their overall operating model.

Benaron explains that preparing now will save time, money and effort and will prevent mistakes later on. "Finance leaders are going to bear the brunt of ESG when it comes to reporting on not just financial data, but also on sustainability," he says.

"If CFOs aren't tactical about how they delegate and manage that workload, it could potentially be too much responsibility on their shoulders to set the agenda."

Benaron suggests that the rising importance of ESG makes it imperative for finance teams to transform in terms of people, processes and systems, even if it is often the last department to do so. He adds that a strong ESG ethos can be built by setting a basic level of understanding, so that everyone knows the implications.

> "If CFOs aren't tactical about how they delegate and manage that workload, it could potentially be too much responsibility on their shoulders to set the agenda

Don't miss the bigger picture

Understanding ESG will not be achieved overnight, Benaron admits. "At VantagePoint, we work with CFOs to demystify the journey to ESG reporting," he says. "This is a daunting task, so it helps to get ahead of the necessary policies, while recognising the benefits that new technology can bring when you're planning a wider strategy.

"Introducing and ratifying policies can be a quick task, but embedding them takes time. It is vital to think at least six to nine months ahead."

The level of investment needed to transform depends on the C-suite's ESG vision and tone, Benaron adds. What technologies need to be implemented will be dictated by whether they see it as a box-ticking exercise, or if it is a full bid to become a B Corp and comply with various regulations.

CFOs must also take enough time to consider all the parties involved, including investors, customers, staff and community stakeholders. ESG materiality assessments offer one way to involve everyone in the planning process, allowing companies to gain valuable insights and feedback and to build trust and transparency. It's also a chance to prioritise the ESG issues that are most critical. For example, wastewater management might be essential for mining, but it would not be relevant for a software firm.

"Without this, you'll be missing the bigger picture," Benaron says. "This could lead to environmental, social or governance goals being missed, or accusations of greenwashing cropping up."

Set and follow your vision

To ensure real-world change, CFOs must avoid many traps, including not spotting bias within the business, spending money twice to arrive at the same outcome, buying the wrong tech or getting left behind in the market.

Overpromising and under-delivering is another trap, says Benaron, who advises the benchmarking of an ESG vision and ambition against an organisation's peers. This does not mean "looking to copy"; instead, these insights will allow CFOs to "take logical measures".

A one-day workshop of the kind VantagePoint offers is one way to navigate this complicated ESG journey, helping firms gain greater understanding of the transformation required and its roadmap.

Benaron says that most people "don't like to change", but he explains that having a "really strong vision" will allow CFOs to guide C-suite decision-making with impartial advice, preventing mistakes down the line.

And while there "isn't necessarily a right or wrong answer" given that every organisation is different, Benaron also warns: "There is a huge cost to getting things wrong."

What else should CFOs be prioritising?

According to VantagePoint's Jamie Benaron, CFOs have a huge opportunity to transform their day-to-day operations. Alongside ESG, here are three things finance leaders should be thinking about in 2024.

1 Make the case for change

While it might be tough for CFOs to argue for funding for the transformation of their own function, as they are usually the ones being approached by other departments wanting to change, it is critical that they make the case for the finance team in a structured way.

Benaron says: "The finance change agenda is actually the part of the business that, if combined with the right relationships between the CFO and other areas of the business, can often lead to the most fruitful insights and strategic direction setting for the entire organisation."

2 Carefully consider which tools are required

The wrong technology purchasing decisions will delay progress and force CFOs to overspend. To counter this, they should avoid hasty tech decisions, lest they fall victim to buyer's remorse.

Benaron explains: "Whatever system or tool you're considering, you must take a measured approach with outside advice to help create your short list of requirements. Then, based on demos and interactions with software vendors and their partners, you can avoid rejection by the existing internal system, because people were brought into the implementation process all along the way."

3 Understand the role of AI in the finance team

Embedding AI into a finance function will allow teams to quickly answer questions such as 'what was the most profitable product last year?' or 'how long will our current inventory last based on current real-time sales?'. No longer will they have to waste time searching through spreadsheets and reports to find this important information.

By maximising AI to handle manual tasks, CFOs can ensure teams have more space to undertake deeper research or have greater levels of human interaction with internal stakeholders.

Speak to VantagePoint about ESG, vantagepoint.consulting/esg

STRATEGY

The great M&A Q&A

Nikolay Pandev via iStock

Persistently high inflation, increasing interest rates and recessionary fears have severely dampened global merger and acquisition activity this year. What are the prospects for deal-seeking companies over the coming months?

Elizabeth Anderson

Most parts of the business world have faced an unwelcome combination of weak growth, high inflation and rising borrowing costs this year. The triple whammy has led to a sharp decline in both the number and average value of mergers and acquisitions.

Global M&A activity in the first half of this year was worth about £1.1tn, according to financial data provider Dealogic – 40% down on the total recorded for H1 2020. And, with the short-term economic outlook still looking uncertain, lenders remain largely cautious about funding new deals.

Few markets have been immune to the slowdown. In the UK, notable transactions among big plcs have been few and far between of late. Alastair Mankin, vice-president at investment bank TD Cowen, reports seeing only three substantial deals in recent months: EQT's takeover of Dechra Pharmaceuticals (£4.5bn); Brookfield's purchase of Network International (£2.2bn); and the UnitedHealth Group's acquisition of EMIS Healthcare (£1.2bn).

It's a far cry from the flurry of acquisitions that happened in 2021, when investors were keen to snap up opportunities created by the Covid crisis. That was a record year for deal-making, with PwC counting more than 62,000 M&As globally – up 24% on the tally for 2020.

Should we expect the lull in activity to continue over the next year or so? For business owners seeking to sell up, might it be better to hold fire on any likely deals, or is now the time to find a buyer?

Despite what has happened – or hasn't happened – so far this year, there are reasonable grounds to expect a recovery in 2024 if inflation eases, interest rates plateau and the global economy stabilises as widely expected. Moreover, the UK and Ireland are expected to enjoy the highest growth in M&A activity next year, according to the *European M&A Outlook 2024* report published by law firm CMS.

"The outlook seems a lot more positive in the UK. Interest rates have reached their peak and will begin to come down over the coming months," says Matthew Wiseman, partner at investment bank Alantra. "As a result, buyers and sellers can more confidently predict market conditions and make more accurate business valuations, leading to an increase in activity."

Deal-makers in the UK are also keen to complete transactions before the next general election, which must be held by January 2025. There are rumours of a potential increase in capital gains tax, which may prompt some business leaders to accelerate their M&A plans to secure the current 20% rate.

Graham Carberry is the managing director of Arrowpoint Advisory, an M&A consultancy that specialises in deals worth between £20m and £200m, including Hyatt's recent purchase of hotel booking platform Mr & Mrs Smith. He reports that the consensus is that 2024 will be a big year for takeovers.

"We have the election coming at the back end of next year, which looks very likely to result in a Labour government," Carberry says. "We don't know exactly how that will change the business tax environment, but those looking to sell assets will be aiming to do so sooner rather than later."

Many deal-makers have complained that the UK's regulatory environment is not conducive to M&As. The Competition and Markets Authority (CMA), for instance, has gained greater powers since Brexit and is scrutinising potential transactions more closely than it once did.

One instance in which the regulator has taken a tougher stance has been Microsoft's planned purchase of Activision Blizzard, originally announced in January 2022. This was initially blocked by both the CMA and the US Federal Trade Commission, only for the latter to withdraw its objection and for the EU to separately clear the takeover.

In August, Microsoft announced that it was restructuring the transaction to address the CMA's concerns and so win the regulator over.

"The CMA's stance on this deal has received widespread attention, given that it goes against the grain of the UK's focus on becoming a tech and innovation hub," notes Harry Coghill, corporate and M&A partner at law firm Macfarlanes.

As this special report goes to press, the latest indications are that the CMA might finally give the revised deal the green light.

Even so, heightened regulatory scrutiny doesn't seem to be deterring buyers and sellers seeking M&As in H1 2024. The technology, media and energy sectors are widely expected to see the most significant surge in deal-making across Europe, according to the CMS report.

> "We have the election coming at the back end of next year... Those looking to sell assets will be aiming to do so sooner rather than later

So, as more businesses gear themselves up to acquire or be acquired over the coming year, it's worth considering what makes a good takeover target and how firms can make themselves more attractive to potential buyers.

Businesses with robust cash flows and strong growth prospects are always obvious targets, as buyers can be confident of long-term value, notes David Newns, co-founder and partner at Contrado Capital, a consultancy that helps entrepreneurs and owner-managers to sell their businesses. He adds that firms that performed well throughout the pandemic will be seen as having proved their resilience. And, given that the cost-of-living crisis is still weighing heavily on consumers, companies with recurring revenues and product portfolios favouring essentials over luxuries are also well placed to secure deals in the short term.

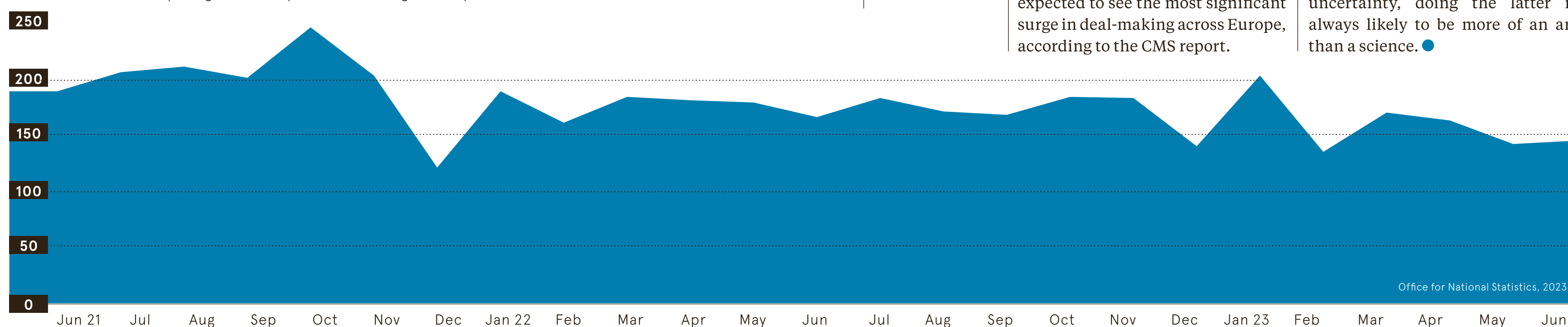
Ryan Brown, deputy group CEO of insurance firm PIB Group, which has acquired 26 businesses so far this year, says that any business with a leader who has entrepreneurial qualities will always be attractive to his company. After it acquires such an enterprise, "its leadership will stay in place", he stresses. "We don't change the formula that has made that business thrive to date."

Companies that operate to a set of clear ethical values will also stand out. Emma Danks, head of the UK corporate/M&A group at law firm Taylor Wessing, observes that environmental, social and corporate governance remains an important consideration. Many companies are looking to acquisitions as a quick way to achieve ESG objectives, so a business that enables buyers to tick such boxes is likely to be well placed in this market.

Broadly speaking, then, for a business to attract potential acquirers, it's a case of getting the fundamentals right and choosing the optimum moment to seek a buyer. In a period of enduring economic and political uncertainty, doing the latter is always likely to be more of an art than a science. ●

M&A ACTIVITY INVOLVING BRITISH FIRMS HAS BEEN ON THE DECLINE SINCE OCTOBER 2021

Total number of monthly mergers and acquistions involving UK companies from June 2021 to June 2023



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INSIGHT

'Fintech is fit and ready for the climate challenge'

The problem-solving spirit of the UK's fintech sector makes it a natural green finance leader, says **Janine Hirt**, CEO of Innovate Finance. But it's vital that the industry and its stakeholders work together effectively

In recent months, disasters caused by extreme weather – from wildfires to flash flooding – have swept across the world, leaving in their wake stark reminders of the existential threat posed by climate change.

Even though the global economy is making headway towards the targets required to reach net zero, as set out in the United Nations' Paris agreement of 2015, these objectives remain alarmingly out of reach, underscoring the urgent need for innovative solutions.

Indeed, £41tn will be needed in incremental investments by 2050 to fund the global economy's progress to net zero and avert a climate catastrophe, according to the World Economic Forum. This cannot be achieved through public financing alone; the private sector clearly has a significant role to play in delivering a successful transition.

It's essential that investment is redirected towards activities aligned with net-zero objectives, supported by a clear long-term strategy and backed by robust data. With this in mind, the fintech sector is emerging as a powerful force in enabling climate solutions that could change our future for the better.

For instance, some UK fintech firms are already using financial data to equip businesses with tech solutions to incorporate climate transition risk into their balance sheets and align their activities with real-world outcomes. This has the potential to go a lot further.

Part of this potential comes from the fact that the fintech sector emerged from the global financial crisis of 2007-08, which imbued it with an innate drive to tackle the world's biggest problems. This became even clearer during the Covid crisis, when the sector provided financial support to 55% of the UK's small and medium-sized enterprises, helping to shore up the nation's economy as the pandemic raged. Armed with its intrinsic capacity for problem-solving, fintech is fit and ready to tackle the climate emergency.

As ever in the fintech world, it is data that reveals the opportunity here. For example, if you analyse personal financial data alongside other types of data – such as that from energy companies or supermarkets – it's possible to establish the carbon footprint of individual items. This approach could theoretically help businesses better understand where to focus their efforts to reduce emissions in their supply chains, or equally facilitate decisions as simple as making sustainable swaps around the office.

For SMEs, industry support and data insights are vital in ensuring that their operations become more sustainable. Since they account for 90% of businesses worldwide, SMEs make a large contribution to greenhouse gas emissions. In the UK they account for a third of the total.

Research conducted by the SME Climate Hub has found that 70% of SMEs surveyed require additional finance to enable them to take action or accelerate progress to reduce their carbon footprints.

This funding gap is another area in which fintech companies can work with other important industry stakeholders, such as banks and global accountancy firms. For example, we at Innovate Finance support Bankers for Net Zero's Project Perseus – a national initiative that brings together a range of stakeholders to develop a data tool and automate greenhouse gas emissions reporting for British SMEs. This could enable lenders to channel extra finance towards 5.5 million SMEs to help them invest in carbon-reduction projects.

It's also worth remembering that the UK is at the forefront of the fintech revolution, making us uniquely positioned to lead the charge in green finance. As we look ahead, it's crucial that innovators, regulators and policy-makers alike work effectively together in aid of fintech's commitment to driving positive environmental change. ●

Janine Hirt
CEO, Innovate Finance

Commercial feature

The future of clean investment is transport

New electric vehicles are still eye-wateringly expensive, which leaves businesses caught between a rock and a hard place when updating their fleets. It's a problem which makes for an attractive investment opportunity

Together, climate, clean and green tech are a booming market. Indeed, more than $495bn was invested in this sector in 2022 – a number which is consistently climbing every year.

That level of investment is partly due to the fact that there's a recognition that green tech is a financial sweet spot. For instance, it provides environmental, social and governance (ESG) benefits, while also signalling to investors and customers alike that your business acknowledges the climate crisis – and, more importantly, is doing something to help. And at this stage, most investors have pursued renewable power projects or green energy investments to fund, often seen as the low-hanging fruit for investors.

"Institutions have invested heavily in renewable energy such as solar and wind," says Dan Saunders, founder and CEO of Zeti, a financial technology company which is revolutionising the way that transport is financed. "A lot of money has gone into those assets, and for good reason. But at some point it creates a concentration of risk in the underlying asset class. There's no diversification."

But there's an emerging, innovative opportunity for those investors who are truly forward-thinking, and it's all around us. Transport is one of the major contributors to the world's carbon emissions, accounting for around a quarter of all emissions worldwide. Greener alternatives are available: electric vehicles (EVs) are becoming increasingly common on the world's roads, and their adoption is being incentivised by governments around the world.

But EVs are also costly – at times, twice the price of their gas-guzzling alternatives – making them beyond the reach of most people. "Barely a day goes by without a news story about the pollution caused by transport. Governments and society want and expect a shift to zero and ultra-low emission vehicles," says Saunders. "At the same time, these vehicles can be very expensive to purchase."

This problem has emerged as part of a wider set of changes. These days, even petrol-powered cars are expensive, and are increasingly bought on finance, with around 90% of new vehicles funded that way in the UK, according to Saunders. At the same time, people are using more on-demand services, whether that's via the likes of Uber or last-mile delivery for their Amazon purchases. As a result, fewer individuals than ever before need to own vehicles. "You've got this view that transport is increasingly becoming a service," says Saunders. "Less and less people own vehicles; it's on-demand, and they're being owned by fleets instead. We'll soon come to view transport as a utility, just like energy."

Those companies providing fleets of on-demand vehicles are themselves tightly run. "They have volatility and seasonality, like any business," says Saunders. "They're always looking to improve cash flow to make sure they're financially secure."

As a result, the demand for creative financing solutions for clean transport is increasing, in turn creating opportunities. "Clean vehicles themselves can be a new, sustainable investment opportunity for these financial institutions, and not just the charging infrastructure to power them," says Saunders. "Rather than invest in an array of solar panels that generate income based on their energy output, you could invest in a fleet of zero-emission vehicles that generate income based on their utilisation."

Saunders argues that by leveraging real-time vehicle data, investment in clean vehicle fleets can now have as big an impact as renewable energy investment. "Unquestionably, renewables investment is good for the planet and will be needed to power clean transport. But transport pollution is immediate, and the localised health risks are obvious. Making capital flow into the adoption of zero-emission vehicles is good for everybody," says Saunders.

Not only does investing in clean vehicles generate good returns – which Saunders says are currently commensurate with the rate of inflation, beating other investment products – it also provides an enduring benefit to society.

Zeti is closing in on 1,000 zero and ultra-low emission vehicles being managed by its digital platform, including a range of London taxis operating on electric power. Further enquiries worth an estimated $500m have also been registered from businesses looking to have their vehicles financed by Zeti's lending partners.

"We easily have demand for another several thousand vehicles that are ready to be financed straight away," says Saunders. "And barely anyone knows about us yet. That's what I'm excited about, to see the positive environmental impact that Zeti can achieve once fleet companies and investment institutions see this new opportunity to generate and share value."

That has interested investors in the business, including early-stage US venture capital investors Powerhouse Ventures and Toyota Ventures, the VC arm of the automotive goliath Toyota.

With obvious parallels to the growth of renewable energy investment, the clean transport investment revolution appears to be upon us. And it looks like it could be big.

"Zeti's aim is to be an enabler, the 'middleware' if you will," says Saunders. "The demand for clean transport finance is clearly there. It's just about whether financial institutions want to be leaders in this field or followers."

Find out more about Zeti at zeti.group/futureoffinance

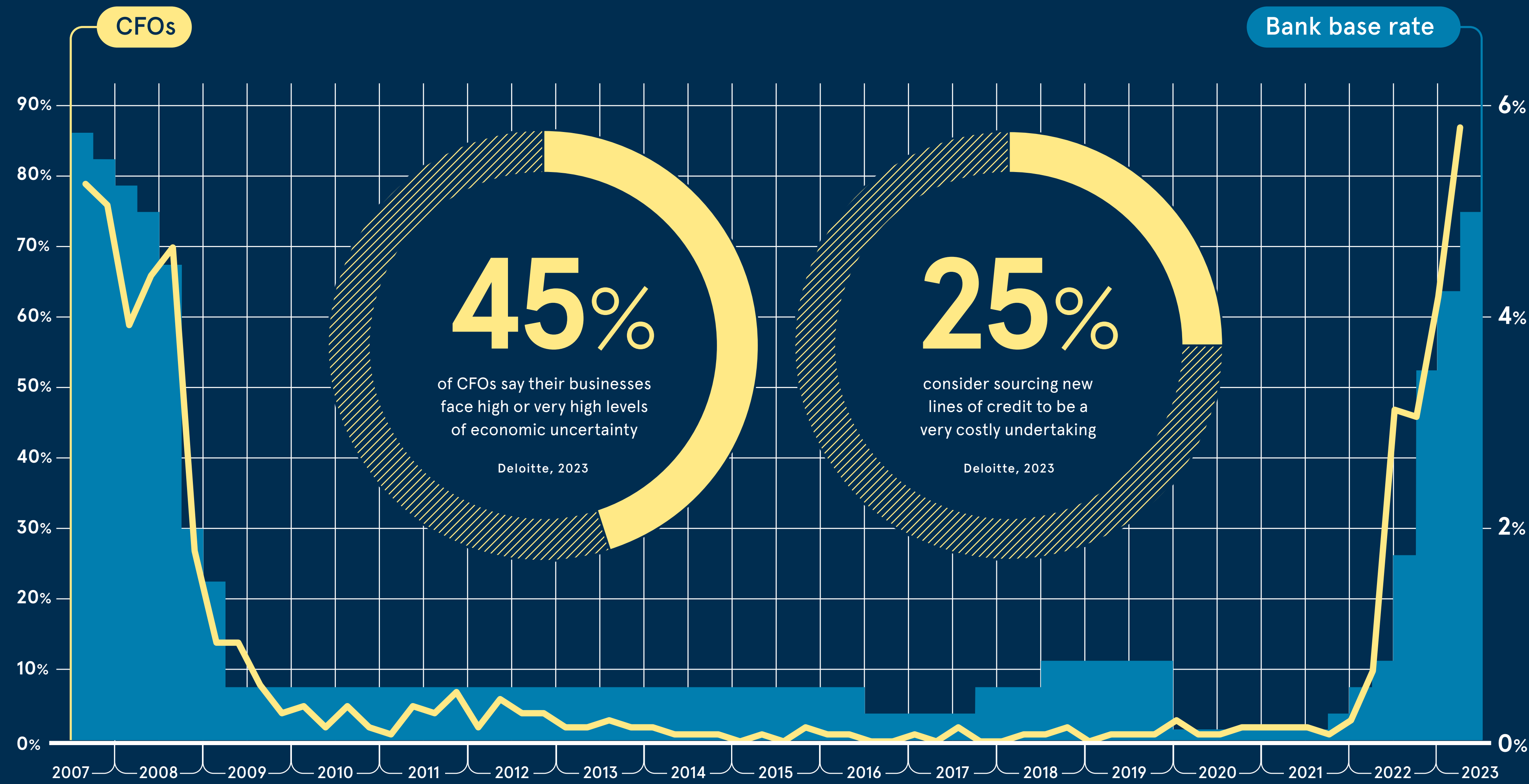
CFOs' INTEREST RATE WORRIES

Base rates have been rising sharply around the world over the past 18 months as central banks struggle to keep inflation under control. With an eye on the cost of credit and the value of their businesses' assets, CFOs are understandably concerned about this, which has reduced their overall confidence in the economic outlook. Are there any bright spots on the horizon?

LIKE INTEREST RATES, CONCERN AMONG FINANCE CHIEFS ABOUT THE COST OF BORROWING HAS RISEN SHARPLY SINCE Q1 2022

Deloitte, 2023

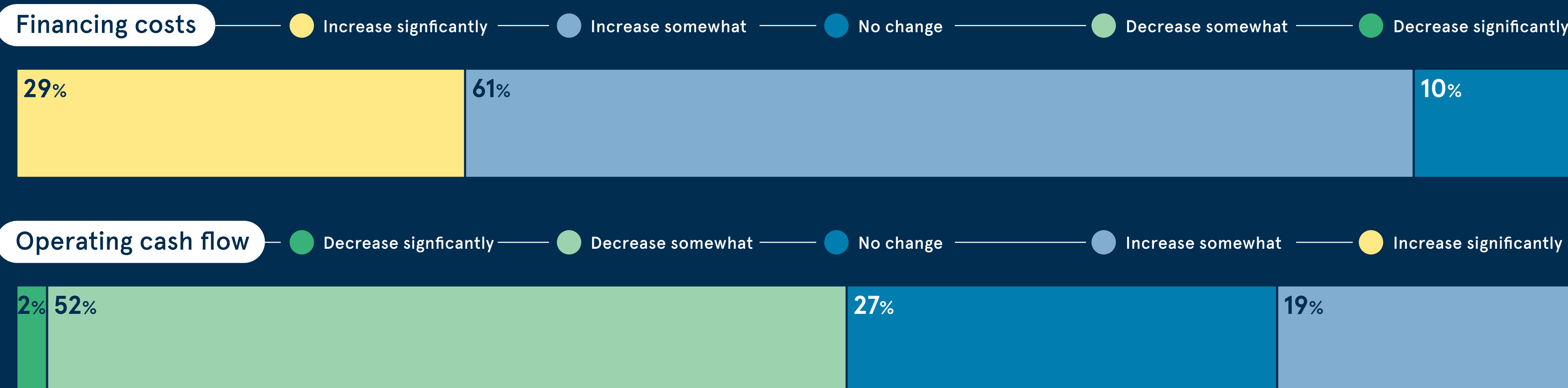
Bank of England base rate and share of CFOs who believe that UK interest rates are "very high" or "quite high" between H2 2007 and H1 2023



CASH FLOW IS LIKELY TO GET SQUEEZED AS A RESULT OF THE INCREASED COST OF BORROWING

Deloitte, 2023

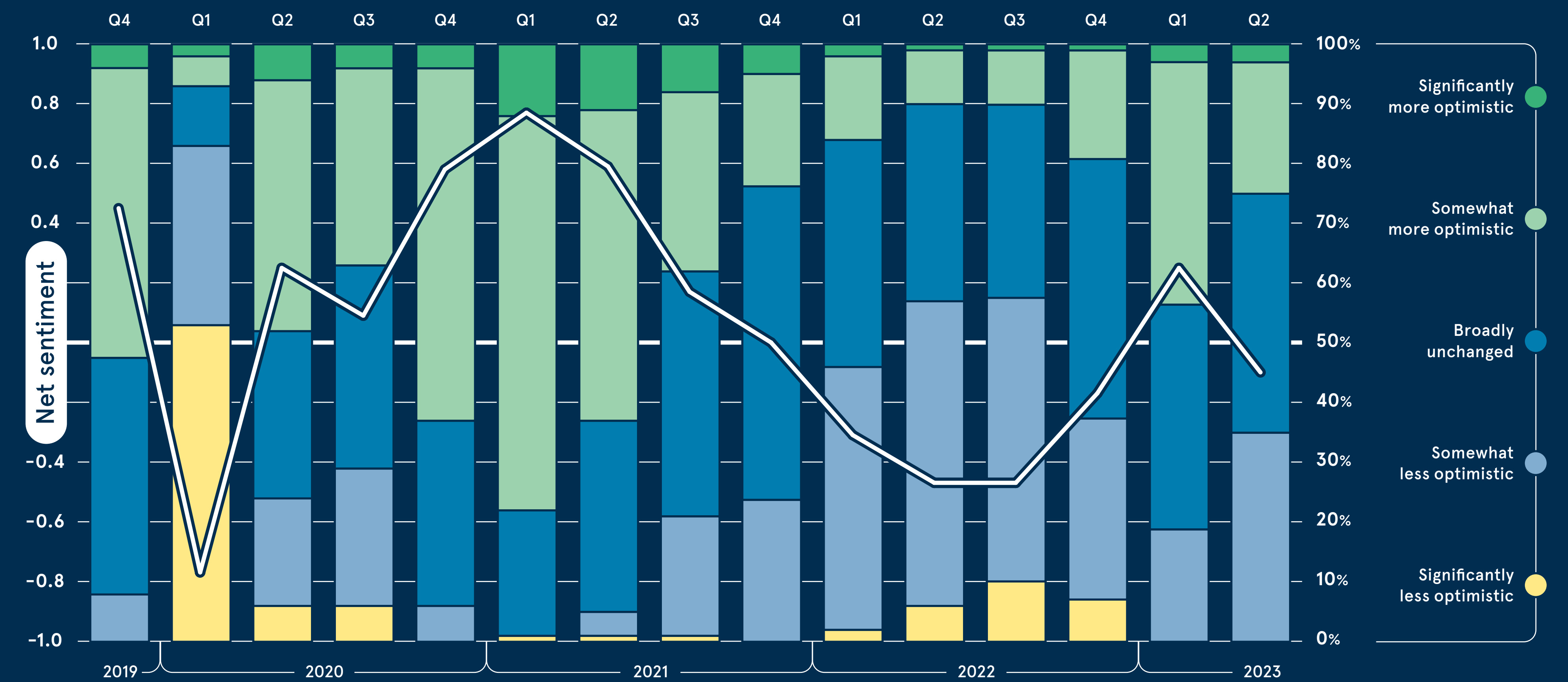
CFOs' expectations over the 12 months starting from Q2 2023



AFTER A RELATIVELY UPBEAT START TO 2023, FINANCE CHIEFS ARE AGAIN LOSING CONFIDENCE

Deloitte, 2023

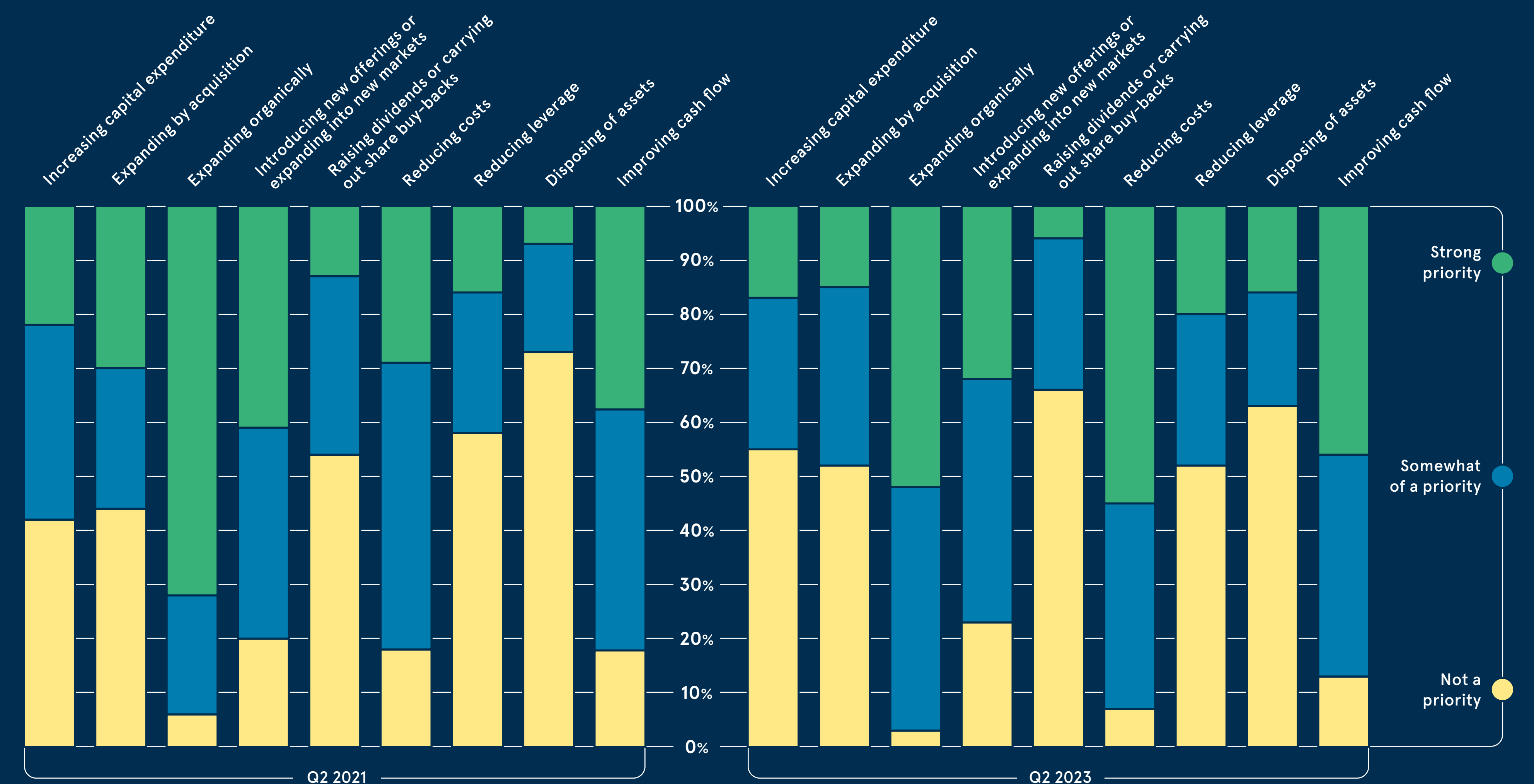
CFOs' views on their businesses' financial prospects compared with the previous quarter



FINANCE CHIEFS ARE INCREASINGLY HUNKERING DOWN AND PRIORITISING THEIR FIRMS' SHORT-TERM SURVIVAL

Deloitte, 2023

Comparison of CFOs' financial priorities for the 12 months starting from Q2 2021 and the 12 months starting from Q2 2023

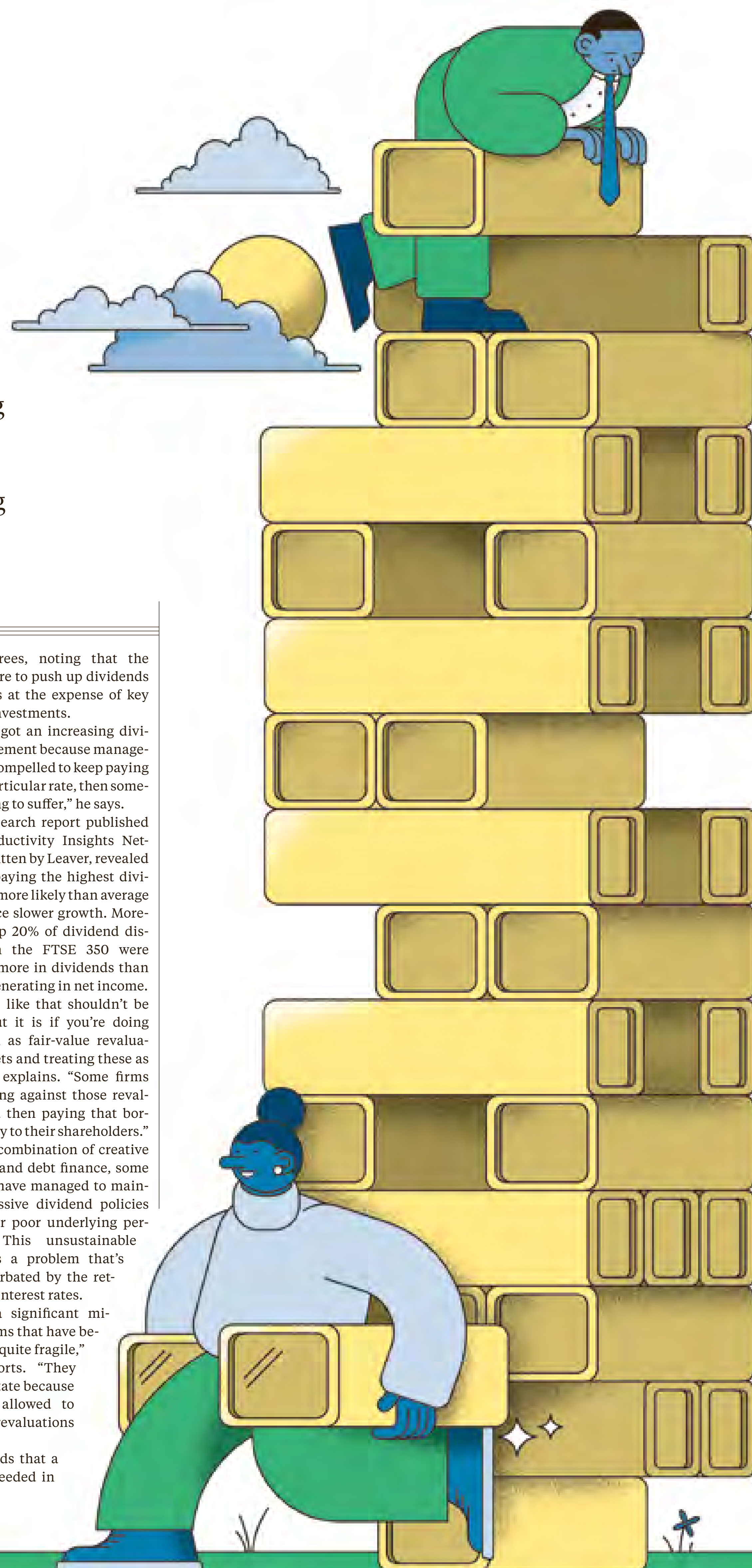


EARNINGS

Largesse oblige – deconstructing Britain's broken dividend culture

Many UK-listed firms are stuck in a rut of rewarding shareholders handsomely while leaving insufficient funds for prudent reinvestment. A backlash against this unhealthy practice has been a long time coming

Ben Edwards



Tough economic conditions have prompted British plcs to slash their costs in several areas, but one thing they haven't been cutting back on is their dividend payments.

UK-listed companies distributed £84.8bn to shareholders last year, representing a 16.5% increase on 2021's total, excluding special one-off payments, according to research published by the Link Group.

That makes the UK an attractive market for investors, but some firms may be taking an unnecessary risk in trying to maintain a progressive, but unsustainable, dividend policy to prop up their share prices.

Hugh Maule is a partner and head of the corporate, finance and tax practice groups at law firm Gowling WLG, where he helps companies seeking to float on the London Stock Exchange. He notes that "there seems to have been an increasing cultural importance over the decades placed upon large listed caps paying income to their shareholders and increasing these payments each year. They definitely don't want to be seen to be reducing dividends."

That is partly because dividends are a way for investors to assess corporate performance. In effect, a company announcing a dividend reduction is telling investors that it's underperforming, which would probably harm its share price.

> Many times I've sat with management teams and told them that they need to reset the dividend because it's too high

"If a management team or board says: 'We can distribute this amount of cash to shareholders next year,' that becomes a yardstick," says Jacob de Tusch-Lec, manager of global income strategies at Artemis Investment Management. "If it the firm then has to cut its dividends, that sends a very negative signal."

Much of the UK's dividend culture is rooted in the fact that the FTSE 100 comprises mature companies that are attractive to income investors who rely on dividends for their revenue streams.

"Income investing is ultimately about targeting companies that have done their innovation and therefore have excess cash that they can return to their shareholders," de Tusch-Lec says.

Also reinforcing the culture is the way that corporate governance and accounting rules operate, according to Adam Leaver, professor in accounting and society at the University of Sheffield.

"The purpose of management is to deliver returns to shareholders," he says. "Management compensation is therefore geared towards delivering shareholder value, which is often measured through things such as dividends and total share return."

This can lead to a situation in which management teams are biased towards maximising immediate returns rather than making choices that, while they may be costly in the short term, generate more lasting benefits for their businesses.

"CEOs in the UK have quite a short lifespan in the job," Leaver says. "So, if you're going to be in post for only four years and much of your bonus is paid in share options or it's triggered by your capacity to increase total shareholder returns or dividends, that encourages short-termism."

Maule agrees, noting that the myopic desire to push up dividends often comes at the expense of key long-term investments.

"If you've got an increasing dividend requirement because management feels compelled to keep paying them at a particular rate, then something is going to suffer," he says.

A 2021 research report published by the Productivity Insights Network, co-written by Leaver, revealed that firms paying the highest dividends were more likely than average to experience slower growth. Moreover, the top 20% of dividend distributors in the FTSE 350 were paying out more in dividends than they were generating in net income.

"It sounds like that shouldn't be possible, but it is if you're doing things such as fair-value revaluations of assets and treating these as profits," he explains. "Some firms are borrowing against those revaluations and then paying that borrowed money to their shareholders."

With this combination of creative accounting and debt finance, some companies have managed to maintain progressive dividend policies despite their poor underlying performance. This unsustainable approach is a problem that's being exacerbated by the return of high interest rates.

"There's a significant minority of firms that have become really quite fragile," Leaver reports. "They are in this state because they were allowed to book asset revaluations as profits."

He contends that a change is needed in the way that businesses are run so that corporate stewardship seeks to maximise benefits for all stakeholders, rather than shareholders alone. This should lead to a more sensible balance between dividend distribution and reinvestment.

> There's a significant minority of firms that have become really quite fragile because they were allowed to book asset revaluations as profits

"That must be backed up with a greater plurality of voices at board level, which might help take the edge off the aggressive distribution culture that British management seems to be following," says Leaver, who adds that accounting regimes may also need to tighten so that there are more limits on what can be included as profit.

"There are two ways in which you can increase a company's market capitalisation," he adds. "One is to inject it with steroids by paying lots of dividends and doing share buybacks. The other is simply to make good management decisions and run the business well. This would be the more sustainable option, but the big problem is that we have made it too easy to book distributable profits through creative accounting."

Maule is one of many market watchers who believe that there should be more dialogue between publicly traded firms and equity investors about the importance of long-term investment.

"Companies are hamstrung by the feeling that they must keep paying more and more dividends to shareholders," he says.

But change may well be afoot – instigated by shareholders rather than the companies they invest in. Indeed, some income investors are pushing back in cases where they consider dividend yields to be too high relative to the underlying performance of the firms concerned.

"Many times I've sat with management teams and told them that they need to reset the dividend because it's too high and they're not investing enough for the future," de Tusch-Lec says. "From our point of view, we want to obtain the maximum benefit from a good, sustainably growing dividend. But we don't want to be dogmatic about this to the point of starving the firm of future growth opportunities."

Reinvesting more profits would not only help to support a company's growth over the longer term; it would also help in the short term by reducing its tax bill through reliefs and allowances.

"In other jurisdictions, it's much more about showing shareholders that you've driven down your tax rate, rather than saying: 'We've met our dividend forecasts,'" observes Charlotte Sallabank, a partner and tax planning specialist at law firm Katten Muchin Rosenman. "US shareholders, for instance, will focus on the effective tax rate that the group as a whole has achieved."

The British preoccupation with dividends is potentially damaging for the London Stock Exchange in the long run. Companies in high-growth industries may shun a listing here because they would rather reinvest profits into R&D and other growth-generating projects than return excess cash to shareholders. British semiconductor manufacturer Arm Holdings, for instance, recently chose to float in New York.

"If the London Stock Exchange is to become a more attractive listing location for such businesses, investors' attitudes towards dividend payments will need to calibrate to take these industry specifics into account," says Rajesh Gupta, CFO at OakNorth Bank.

That would require a wider cultural shift, says Sallabank, who suggests that it's in UK plc's interests to develop an environment in which "a strategy for growth is valued as much as an income return".

For that to happen, companies urgently need to start rethinking their dividend policies and finding more sustainable ways to keep their shareholders happy.

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ANALYSIS

Has the British economy turned a corner at last?

Several of the UK's core economic indicators are improving – albeit slowly. Might it be time to crack open the champagne?

Clara Murray

A dramatic update to the UK's economic figures in September proved that we cannot always trust even the most official of statistics. Revised data from the Office for National Statistics shows that output bounced back from the pandemic faster than first thought. GDP in Q2 2023 is now estimated to be 1.8% above its pre-Covid level. That might not sound much, but it represents £40bn in value and means the UK is no longer trailing all the other G7 members.

It follows a similar reappraisal by the International Monetary Fund, which had forecast in January that the British economy would be the only major one to shrink this year – outperformed even by international pariah Russia. Now it expects the UK to surpass Germany.

The Bank of England's governor, Andrew Bailey, said in July that he considered the British economy to have shown "unexpected resilience" to "substantial – and in some cases unprecedented – external shocks".

Good news all round? Unfortunately, several other key indicators show that the UK still faces a unique combination of problems.

As Bailey's immediate predecessor, Mark Carney, noted earlier this year, the triple pressures of energy price inflation, the pandemic and Brexit have "weighed on the economy", forcing policy-makers to balance controlling inflation with keeping the side effects this causes bearable for ordinary people.

For instance, asset manager Legal & General is still betting on a "significant" downturn in the UK and other major economies as the increased cost of borrowing reduces investment and consumption.

The UK could also be facing a "poisonous cycle" of stagflation, notes Giles Coughlan, chief market analyst at HYCM Capital Markets Group. The economy is "hovering around the break-even point," he adds. "If we win the inflation battle, we'll probably avoid a recession. But I wouldn't be surprised if we gently dipped into one."

Managing inflation, which began rising in late 2021 and was then fuelled by Russia's invasion of Ukraine, is key to solving the UK's economic woes. While the inflation rate, as measured by the consumer price index (CPI), fell last month for the sixth consecutive month, it remains almost five percentage points above the Bank of England's long-held target of 2%.

Economists are worried about inflation becoming "sticky", particularly because core inflation (which excludes food, energy, alcohol and tobacco prices) is not falling as fast as overall CPI. That's despite countries such as France and the US managing to bring their price rises below 5% in recent months.

Increasing the cost of credit is still the main way to control price rises.

> "The UK hasn't exactly worked out a clear post-Brexit direction – and that has started to affect our output

The Bank has been more aggressive than most of its counterparts in this respect, lifting the base rate to 5.25%, its highest level in 15 years.

Another factor that would keep inflation in check would be a significant increase in unemployment. But the labour market is tight, with job vacancies and people in work still at near-record highs.

The Office for Budget Responsibility predicted in November 2022 that unemployment would rise by 50% (equivalent to about 650,000 people) by mid-2024. But in its March 2023 update it revised that down to a 15% increase.

While good news on a human level, that downgrade might not benefit the broader economy. A tighter labour market encourages employers to boost wages, which can prolong inflation because it increases costs for businesses while enabling more people to afford higher prices – an effect known as the wage-price spiral.

Things for ordinary people are bad enough as it is, with consumers still keenly feeling the hit to their disposable incomes. The latest data by market research firm GfK has found that consumer confidence is almost as weak as it was during the depths of the global financial crisis in 2008 and the pandemic in 2020, despite a recent recovery.

GfK's index takes into account people's feelings about their own prospects and those of the wider economy. Joe Staton, its client strategy director, says the results show "the financial mood of the nation is still negative".

Despite such pessimism, many blue-chip companies have been performing strongly. The FTSE 100 index recently neared its all-time peak, falling only slightly since then. But analysts warn this isn't necessarily a sign of a strong economy, because a lot of FTSE 100 earnings come from abroad and do not reflect the domestic economy.

Comparisons with other major stock markets also reveal a more disappointing picture. The FTSE 100 reached its record high back in June 2018 and has only recently neared that mark again. Over the same period, the US's S&P 500 index has nearly doubled in value.

While the markets have all but forgotten last September's disastrous mini-budget from Liz Truss and Kwasi Kwarteng, another political choice continues to reverberate throughout the economy: the UK's departure from the EU in January 2021 amid the pandemic.

Since then, its international trade activity has been slower to recover than that of the other G7 members. British import and export values are still below pre-pandemic levels. By contrast, Italy, Germany and Japan have all increased their commerce with the rest of the world.

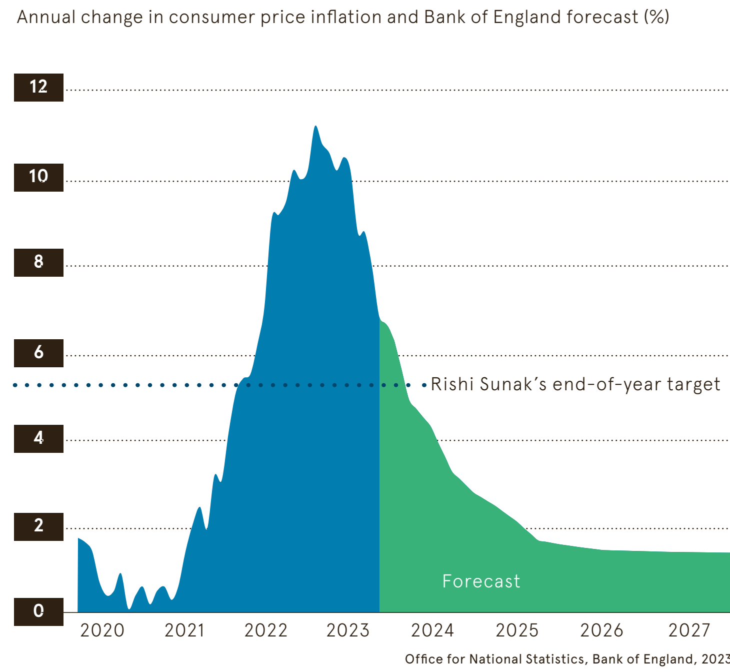
> "If we win the inflation battle, we'll probably avoid a recession. But I wouldn't be surprised if we gently dipped into one

Brexit has cost the UK 4% of its GDP and about £100bn a year in lost output, according to Bloomberg.

"As a nation, we haven't exactly worked out a clear post-Brexit direction – and that's started to affect our output," Coughlan says. "The projections are pretty bleak."

INFLATION IS HEADING BACK DOWN TOWARDS THE LEVEL TARGETED BY THE PRIME MINISTER

Annual change in consumer price inflation and Bank of England forecast (%)

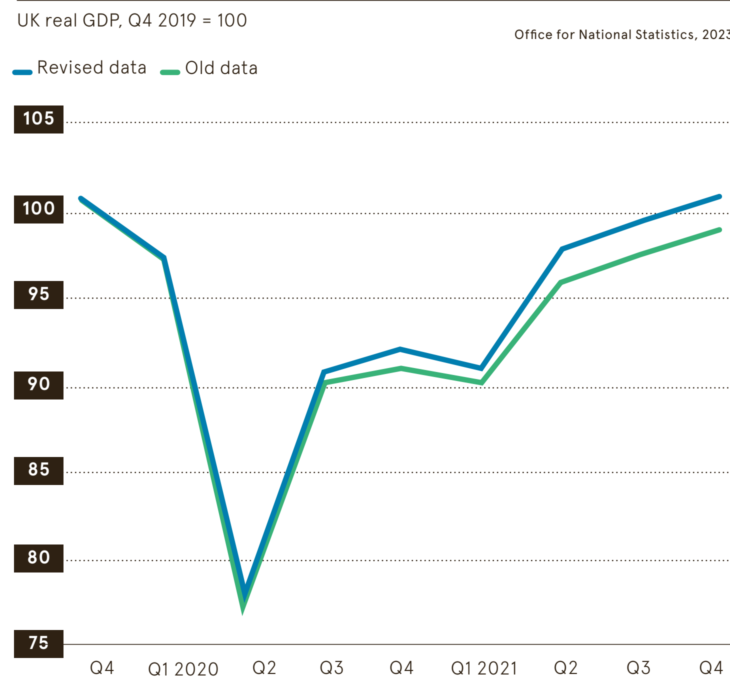


Office for National Statistics, Bank of England, 2023

REVISED DATA SHOWS THAT IT TOOK TWO YEARS FOR UK OUTPUT TO RECOVER TO ITS PRE-COVID LEVEL

UK real GDP, Q4 2019 = 100

Office for National Statistics, 2023



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VANTAGE POINT

Commercial feature

Essential to evolutionary: the phases of banking transformation

Putting essential foundations in place is critical for banks to unlock the fullest potential of digitisation and evolve beyond industry fundamentals

Consumers increasingly expect on-demand services, yet the digital transformation needed to meet this expectation remains a challenge for large financial institutions, particularly if their core banking systems continue to run on legacy technology.

"Large institutions that have been around for years are carrying so much technical debt," says Jeremy Donaldson, managing director of banking and capital markets for EMEA at DXC Technology. "Their challenge is trying to figure out how to digitise in a way that fits within their current technology environment. They might have a strategic direction, but the execution of those strategies can take time because of the environmental complexities in which these transformations need to take place."

For example, most banks are working on giving customers the ability to self-serve and allow transactions to take place across all channels, with digital assets being developed at pace. "These digital assets increasingly trigger digital transactions," says Andy Haigh, head of banking and capital markets for EMEA at DXC Technology. "This requires having the operational agility and capacity to respond quickly to shifts in consumer demand and being able to formulate and launch new products instantly."

These digitisation efforts are increasing both customer data volumes and the number of access points to that data, making banks prime targets for cyberattacks. "The financial risk of losing the data is one thing, but the reputational risk of data compromise is something completely different from a brand value perspective, so a focus on securing the data throughout the digital transformations remains of paramount importance," Donaldson adds.

In a digital ecosystem, banks need to be certain of their customers' identities and that interactions are fully verified and secure across channels. Best-in-class financial institutions will leverage this imperative to build a more holistic view of their customers and understand how they are interacting across all business lines. The upswing for digital leaders is the opportunity to provide more personalised experiences to outcompete the laggards.

"The biggest problem for banks is how to get a centralised view of a customer that is current, doesn't go stale and can drive business decision-making," says Haigh. "Once banks get that right, they can quickly start to put relevant products in front of customers."

As customers become more digitally savvy, banks have a responsibility to ensure their employees speak the same language and possess the skills to meet future banking needs. "These institutions have to change their view of the skills they're looking to recruit and swing the pendulum towards people who are much more analytical and conversant with the use of new technologies," says Donaldson.

To achieve true transformation, the process needs to be broken down into two phases – the 'essential' steps financial institutions need to take and then the 'evolution' stage, where they can start to rethink how their services are delivered, he explains. While some aspects of these two phases can be run in parallel, in many cases the results have been suboptimal because many large banks struggle to implement elements of their evolutionary phase without first having the essential transformation elements in place.

These institutions have to change their view of the skills they're looking to recruit and swing the pendulum towards people who are... conversant with the use of new technologies

The 'essential' phase includes steps like optimising the ability to transact, mitigate risk, manage regulatory change, focus on best practices, and reduce inefficiencies. For example, by modernising core platforms, banks can rationalise, standardise, save costs and be ready to scale transactions to deal with the bigger data footprint that digitisation both creates and demands, Haigh points out. Getting "cloud right" rather than "cloud first" is key to right-sizing and enabling a springboard for new technology toolkits that will later help business thinking.

"Without customer data centralisation, product formation will be limited. Without a modern core platform, the ability to onboard products will be limited. Without real-time risk, the ability to zero-time onboard customers will be impossible," Haigh continues.

"It is an arms race," he says. "It's equally about tightening up operational risk because the more time they spend fighting fires and dealing with compliance issues, the greater the distraction in providing the next level of service their customers expect."

Accommodating the rapid pace of regulatory change creates additional complexities for banks running on a legacy core. Changes to regulatory requirements drive a great deal of development and testing effort across multiple systems to remain compliant. By modernising their fundamental systems, banks can streamline their technology and adapt to regulatory change much faster. In turn, this ensures a higher degree of compliance and pivots focus towards leveraging AI to better understand the potential impact where non-compliant areas are identified.

As customer data centralisation becomes more successful, the overlay of technology will undoubtedly open new areas of analytics and analytical bias, which can challenge banks' moral obligations and force new types of business trade-offs. For example, analytics performed on client behaviours and transactions can easily spot gambling habits; while approaching the customer early to highlight this will be cheaper for the bank to mitigate, it will likely damage customer intimacy.

Haigh argues that getting digital foundations right via essential transformations empowers banks to innovate at speed through evolutionary transformations, rapidly changing product time-to-market and increasing the scope for cross-selling.

"It needs to be executed in very short-step gains that are very tangible and for which the business can see outcomes. This will keep the momentum going on what will be a multi-year journey," Haigh suggests.

The need to advance is pressing. However, a failure to move with the changes can mean customers simply switching to competitors who are digitising faster to meet their rapidly changing needs. Donaldson warns: "The large banks have the competitive advantage regarding long-term customers: they have a wealth of customer data. Those banks must accelerate the execution of essential transformations to leverage that data in order to unlock the benefits of evolutionary transformations. If this is not a priority now, the advantage will be lost."

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INTERVIEW

'We will always be a growth company'

Adam Dodds, the co-founder and CEO of share-trading app Freetrade, explains how a startup mindset influences the way he runs his firm

Rohan Banerjee

Adam Dodds, the CEO of Freetrade, the company he co-founded in 2016 with business partners Davide Fioranell and Viktor Nebehaj, is wearing a hoodie, jeans and a baseball cap. The ensemble matches the casual feel of his firm's working environment.

Is that deliberate? Dodds says that Freetrade aims to foster a culture that lets people "unwind in the office and feel more comfortable". Having spent six years as a KPMG auditor, he is all too aware that many firms in the finance world still insist on smarter office wear. While he's not against that, he believes a firm's dress code is far less important than its output. If people feel relaxed, they're more likely to do good work, he suggests.

While Freetrade's culture might be casual, the business is not. The company aims to "democratise" the trading of shares, Dodds says, opening up the stock market and making it accessible to anyone interested, not just professionals. It has an Android and iOS app where it operates a freemium model, with the paid-for tiers adding more functionality. As of 2022, the firm had more than 1.4 million registered users and held more than £1.5bn in assets.

Dodds says he was motivated to start Freetrade because he wanted to demystify the stock market. He is proud of its progress to date. Against the backdrop of the cost-of-living crisis, Dodds thinks that investing in the stock market has the potential to help hard-pressed consumers make their money work harder. He doesn't dispute there's a significant element of risk attached to this type of investment. But he believes that, if people do their research, it can be more rewarding than simply letting money sit in a typical savings account.

Dodds says that his biggest challenge has been to raise the company's profile and reach a market of consumers who feel alienated from the trading market. There are, he estimates, millions of people who have never bought a stock or even realised that they could.

"Our target audience is people who want to invest but don't know how," he says.

And Dodds has big plans for growth. He is not content with making a "dent" in the market; he wants to transform it. User numbers, while in the millions, are only "scratching the surface. Less than 2% of the UK population has signed up for Freetrade. The incumbents still dominate, so we've got a lot of work to do to progress our mission," he says.

Key to that growth is hiring the right people. Early teething problems at Freetrade, Dodds reflects, were all too often down to recruiting the wrong people. This wasn't because they were ill-qualified or even bad at their roles, but because "the kind of person who thrives in a 10-person team is not necessarily the kind of person who thrives in a 100-person team and vice versa."

Some financial professionals want the ready-made security and routine of a legacy brand, he says, "and that's OK", but Freetrade was, and still is, a work in progress. That means the firm is focused on hiring people who are aligned with its mission and are willing to work hard, says Dodds, adding: "We want people who want to be here and who get what we are about."

That's also important because, as with most startups, Freetrade cannot necessarily compete on pay. In the early days, Dodds admits with a chuckle, Freetrade was "pretty stingy, because we had to be." Nebehaj, who now serves as COO, was initially paid the London living wage, albeit topped up with considerable equity.

When hiring, you've got to balance your economics with your vision

That equity option is one Dodds thinks more firms should consider. "It's not for everyone, for sure. But, if someone buys into the project and has shares in the company, that will probably motivate them more to make sure it succeeds."

Freetrade can now afford to pay more, with Dodds highlighting that it also offers a range of benefits, including stock options, private health cover, an enhanced pension scheme and a "generous" annual leave allowance of 35 days.

But he hopes that the "frills" are very much a secondary consideration for any prospective Freetrade employee, behind a genuine interest in, and passion for, its business.

"There's an old Silicon Valley trope: missionaries and mercenaries," he reflects. "You've got your missionaries, who believe in the mission. And you've got your mercenaries who are there for the cash. Someone who's willing to jump ship for £20,000 more is not necessarily the profile we're looking for. I'm not saying that there isn't a little room for manoeuvre [when it comes to hiring someone from a rival firm] for a bit of an incentive. But you've got to balance your economics with your vision."

For Dodds himself, the vision seven years in remains the same as when he started. This means that, while his firm might technically be too old and too big to still be considered a startup, he believes it is.

"Being a startup is a state of mind. It's more to do with the culture and vibe of a company than with its age or size. You could call [Elon Musk's space exploration and research company] SpaceX a startup if you wanted, even just because it's founder-led."

As long as Dodds is in charge at Freetrade, he says, it will always be a "growth company, with a growth mindset. We'll never stop looking for ways to improve the company, introduce new products or build on existing ones."

And, as a founder-CEO himself, Dodds is not seeking an exit strategy. "The best founders stay at their company and grow with it," he says, adjusting his cap. "I've no plans to tap out or retire."

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