

Why 'corporate easing' should be welcome news for business

Credit (pardon the pun) where credit is due: "corporate easing" is likely to be a step right direction, albeit we do not yet know the details.

Although the announcement about just how corporate easing (also known as credit easing) will work will not be made until the end of next month, the Treasury, it seems, has a range of ideas including; buying smaller company corporate bonds directly; purchasing pools of SME loans from banks; and subsidising others to buy these loans.

But how does this help SMEs specifically, very few of which actually issue corporate bonds in the way large corporations do? The theory is that since it provides the banks, who are currently holding SME debt (which is inherently more risky than large company debt), with an opportunity to package up and/or sell those loans to the government – who, in turn, may sell them on to private investors – the banks will be more willing to make fresh loans to SMEs, who would otherwise be unable to access the debt funding they need to grow.

In fact, longer term some believe this government funding will help to create a permanent, more formal bond market for SMEs who are, after all, the real drivers of growth in the UK economy. If this was achieved, even to a fairly minor extent, it would still be a significant and very welcome addition to the sources of funding available to SMEs.

That there is a real and present need among SMEs for sensibly priced short, medium and long term debt finance is not in question. If credit easing goes, at the very least, some way towards improving credit conditions for SMEs it is to be welcomed. Far more so, one could argue, than the Business Growth Fund, recently launched by a consortium of large banks which, some say, was designed to divert attention away from their lack of enthusiasm for conventional lending to SMEs.

Arguments against corporate easing

There are, of course, arguments against credit easing – most notably the one of moral hazard i.e. if banks believe they can pass on the risk of providing credit, will they make an appropriate effort to assess it properly? Will it precipitate a repeat of the sub-prime mortgage CDO (collateralised debt obligations) debacle?

This is fair comment to some extent although I believe there is a very real difference between what banks, particularly investment banks, were trying to achieve for themselves and their shareholders in the run up to the crash of 2008 and what the UK government is trying to achieve now. Is it not unreasonable or irresponsible for a government to do what it can to help SMEs in the present economic climate, particularly when the likely sums involved are tiny in comparison to what has been made available to banks.

Credit easing must, however, be part of a bigger, more innovative plan to encourage and / or compel banking institutions to lend more freely. No serious person would expect banks to make bad loans to poor quality businesses without appropriate security. The difficulty is, sadly, that many SMEs with strong balance sheets and solid cashflows are unable to secure even modest debt funding in the present climate. Some are reluctantly seeking equity funding instead; others are simply putting off growth plans and investment decisions which is bad for them, their shareholders, their employees and, most importantly, the UK economy.

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Story from Growing Business:

<http://www.growingbusiness.co.uk/why-corporate-easing-should-be-welcome-news-for-business.html>

Published: 18/10/2011 10:56:00 GMT

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