Why it makes sense to invest in the creative industries and support them

While many fast-growth companies in the creative industries are currently the target of heavy private equity investments and a flurry of mergers and acquisitions, it makes sense, from a tax and financial standpoint, for individuals and corporate investors to go "long" on creative startups and SMEs.

1. "Good times" are coming back: it's time to invest in the creative industries

With the global economy recovering from the 2007-2012 recession and a tangible boost of confidence, financial investors and corporates alike are becoming more bullish and enterprising, especially in relation to the creative industries. It is time to invest in the creative industries.

In the luxury goods sector, the historical data is very promising, with 2012 being the third year in a row of double-digit growth for personal luxury goods, at 10 percent annual growth rate, now over the Euro200 billion ceiling (1). There was no recession at all, in the luxury goods sector.

As a reflection of the outperformance of this creative sector, many luxury stalwarts have been either acquired (such as Loro Piana and Bulgari sold to LVMH as well as Christopher Kane and Pomellato sold to Kering), invested into (such as the investment of equity investment funds Ardian and Blackstone into a minority participation stake in Versace (2) and the negotiations for an investment made by buyout firm Permira into a Euro450 million majority stake in Roberto Cavalli (3)) or introduced on the stock market at sky-rocketing valuations, which are ever increasing (Prada, Salvatore Ferragamo, Michael Kors, Brunello Cucinelli).

The technology sector is also back to acquisitive mode in full swing, with Facebook spending USD19 billion (!) to purchase WhatsApp, a cross-platform mobile messaging app for iPhone, BlackBerry, Android, Windows Phone and Nokia, which allows to send text, video, images, audio messages free of charge.

The USD19 billion figure is split between USD4 billion in cash, USD12 billion in shares and USD3 billion in Facebook shares, which will be distributed to the founders and employees of WhatsApp, spread over four years after the closing of the deal. Sequoia, the investment fund which invested USD8 million for 15% of WhatsApp’s capital in 2011, is about to make USD3.5 billion out of this transaction.

Juicy business.

With many sectoral experts saying, and proving, that the creative and cultural industries are the booster to global and, in particular, European, growth and recovery (4), the future looks very bright indeed for all those companies which main assets are their intangibles (knowhow, intellectual property, brand value, reputation, etc).

2. How to benefit from the bullish market in a tax efficient way

If you have some back pocket money (5), i.e. some money sitting around idly in a savings bank account remunerated between 0.5 percent and 1.00 percent, which you absolutely do not need in the short and medium term and which you would not feel badly hurt if you were losing, now is the time to take advantage of the situation.

The taxman is generous to individuals ready to part with their cash to invest in the creative industries, on both sides of the Channel.

In Great Britain, HMRC is only inclined to give tax credits to individuals, the so-called “business angels” who are UK tax residents with an entrepreneurial mind. Enterprise Investment Schemes (“**EIS**”), Venture Capital Trust (“**VCT**”) and Seed Enterprise Investment Scheme (“**SEIS**”) are the three tax tools through which individuals can invest in eligible companies (i.e. companies with no more than 250 employees or gross assets lower than GBP15 million, or GBP200,000 for a SEIS) in a tax efficient way.

Tax breaks are summarised below:

<u>SEIS:</u>

Maximum investment: GBP100,000

Inc tax relief/investment: 50 percent

Holding period: 3 years

Capital gain tax: exemption

EIS:

Maximum investment: GBP1 million

Inc tax relief/investment: 30 percent

Holding period: 3 years

Capital gain tax: exemption

VCT:

Maximum investment: GBP200,000

Inc tax relief/investment: 30 percent

Holding period: 3 years

Capital gain tax: exemption

In France, individuals who have to pay the French wealth tax (wittily called "*impôt de solidarité sur la fortune*" ("**ISF**"), and invest in SMEs, are also rewarded by the French state.

Through the "*ISF PME*" tax breaks, individuals subjected to the ISF can deduct up to 50 percent of the sums invested in French SMEs, up to Euro45,000 per year (6).

For everybody else who pays income tax in France, a new tax break of 18 percent of the cash invested in a French SME, capped at Euro50,000 per taxpayer per year, has been set up (7).

If the SME you have invested in goes bust, you will still have been able to take advantage of the tax breaks. If the SME produces many sparks and is being acquired, at a later stage, by a private equity investment fund, a competitor or any other third party, the early-stage investor individual will be able to cash in and realise a substantial capital gain on its early investment.

In the UK, such capital gain is exempted from taxation, unlike in France. That may explain why there are more than 50,000 business angels in the United Kingdom and around 5,000 (!) in France.

Sadly, corporate venture is not currently actively encouraged by either the French or British governments, which results in Euro230 billion sleeping idly in the coffers of all the companies listed on the French CAC40 index, for example.

More lobbying should be done, by institutions representing the creative industries such as Comité Colbert, Fondazione Altagamma, Walpole and the European Cultural and Creative Industries Alliance, to influence governments to provide tax incentives to companies wishing to invest in SMEs in a tax efficient way.

Positive changes are looming though, since corporate venture should kick off on 1 July 2014 in France, with companies paying taxes in France being able to amortise their corporate venture investments in innovating SMEs over a period of five years (8).

Let’s watch the space and hope that Cameron and Osborne are going to take stock and act accordingly, in the UK soon.

It is time to think carefully how to invest any spare cash that you may have and, with the bright economic outlook and new tax schemes pushed by governments to accelerate growth and recovery, both individuals and corporates have more and more investment options at their disposal, to encourage innovative and creative industries.

(1) Luxury goods worldwide Market Study Spring 2013 Update, Bain & Company

(2) M&A in 2014? Luxury brands on sale or seeking for financial partners, Portolano Cavallo Studio Legale

(3) Sources Say Roberto Cavalli Nearing €450 Million Sale to Permira, Business of Fashion

(4) 1er panorama des industries culturelles et créatives, EY, November 2013

(5) Back pocket money, Jimmy C. Newman

(6) "*Réductions, impôt de solidarité sur la fortune*"

(7) "*Réduction d'impôt pour souscription au capital de sociétés non cotées*"

(8) Corporate venture: "*pour financer l'innovation*"

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