PRAETURA EIS 2020 FUND

Praetura Ventures Limited

	Positives	Issues
Why Invest	▶ **Strategy:** Exposure to a portfolio of companies across a range of sectors, the majority likely to be based in the north of England.	▶ **Track record:** Although the track record to date looks very promising, it still lacks depth.
The Investment Manager	▶ **Team:** Diverse range of experience in team, with clear strategy and well-structured approach for post-investment support.	▶ **Rate of growth:** Praetura has grown the team quickly in recent years.

Nuts & Bolts

- **Duration:** The Fund is limited lifespan, with a closing on 19 December 2019, or when the target is reached, if earlier.
- **Diversification:** The manager expects to provide between six and eight investments.
- **Valuation:** There will be no formal valuation, but information on the latest transaction prices will be supplied to investors.

Specific Fees

- **Fees:** Combination of direct fees and company charges. Annual management fee mostly accrued and recovered from exits.
- **Performance fee:** Charged at 20% on aggregate returns over 120% of gross subscription on a portfolio basis.

Risks

- **Target returns:** The target return of 2x capital suggests a high-risk investment strategy.
- **Companies:** Supplying risk capital to early-stage companies, most of which will rely on technology. There will be a spread of company returns as the successful ones will do very well, but those which fail may do so completely.

	Manager information	Contact details
Analyst *Brian Moretta* 020 7194 7622 bm@hardmanandco.com	▶ ***Scheme assets:*** *£nil* ▶ ***Scheme target:*** *£10m* ▶ ***EIS assets:*** *£14.5m* ▶ ***Total FUM:*** *£247m* ▶ ***Scheme launch date:*** *2019*	***Contact:*** *Jonathan Prescott, Business Development Director* *+44 (0)7710 087 636* *+44 (0)161 641 9475* jon.prescott@praetura.co.uk

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Factsheet

Praetura EIS 2020 Fund	
Product name	Praetura EIS 2020 Fund
Product manager	Praetura Ventures Limited
Tax eligibility	EIS
Target return	2x capital
Target income	None
Type of product	Discretionary portfolio service
Term	Open in 2019 only
Sectors	Generalist with technology bias
Diversification:	
Number of companies	6-8
(Expected) Gini coefficient	0.13-0.17

Fees	Amount	Paid by
Initial fees:		
Application fee	2.5% (1.0% advised) (excl. VAT)	Investor
Deal fee	Up to 4.0%	Investee company
Annual fees:		
Management fee	2.0% (1.5% advised) (excl. VAT)	Investor- accrued
Annual admin charge	£75 (excl. VAT)	
Monitoring fee	£36,000	Investee company
Exit fees:		
Performance fee	20%	Investor – aggregate proceeds over 120% of gross subscription
Exit deal fee	0.35%	Investor

Advisor fee facilitation	Yes
Advisor fee amounts	As agreed with investor
HMRC Approved?	No
Advance Assurance	Yes, for each investment
Reporting	Six-monthly
Minimum investment	£25,000
Current funds raised	£nil
Fundraising target	£10m
Closing date(s)	19 December 2019, or when fundraising target reached if sooner
Expected exit method	Mostly trade sale

Source: Praetura, Hardman & Co Research

Fund aims

The Praetura EIS 2020 Fund is a discretionary portfolio service, which will provide a portfolio of investments in unquoted companies. The target return is an aggregate of 2x capital. Returns will be focused on capital gains, and investors are unlikely to receive any dividends. The Fund has a limited lifespan.

Summary of risk areas

Note: *There are generic risks associated with investing in EIS or unquoted companies, in addition to the specific risks commented on below. Comments on relative risk refer to other EIS investments and not to wider investments.*

Investments

Portfolio risk

Each investment will be providing risk capital to an unquoted early-stage company. Praetura aims to provide between six and eight companies in the portfolio, with position sizes between 5% and 20%. There will be some sector diversification, but stock-specific risk should dominate market risk.

The benchmark return of 2x capital suggests a high risk and seems appropriate for the strategy.

Sourcing and external oversight

Founded in 2011, Praetura appears to have established a solid network for sourcing new investments. The new EIS funds require a faster rate of investment than previously, but that seems manageable within current sourcing arrangements.

The Investment Committee consists of senior executives of Praetura. With little involvement in deals at an earlier stage, they provide a more neutral oversight of the investment decisions.

Ongoing support and monitoring

Praetura's emphasis on support after investment is very strong; the support team is almost as big as the one that is doing deals. Praetura takes both a board seat and an observer role: the latter to allow specialist expertise to be brought in. A well-structured monitoring process is in place, including a direct IT link into investee company accounting systems and a focus on monitoring key metrics in a systematic way.

Exits

While the primary focus is expected to be trade sales, so far, Praetura has also seen a flotation and PE buyout in its exits.

Manager

Team

The Praetura team has a broad range of experiences. Having expanded over the past couple of years, it seems to have adequate capacity for the enlarged deal flow that the EIS Funds will bring. The team is complemented by a group of Venture Partners. Although this is a relatively new addition, it should bring useful supplementary specialist knowledge, whether for diligence or support.

Track record

Since 2011, Praetura has deployed £42.0m into 25 companies. There have been eight full exits and one partial exit, with four of these being successful exits. Including the partial exit, the gross return on invested capital is a highly credible 3.7x. The pace of exits is good given the relatively short time that Praetura has been investing. Nevertheless, the track record still lacks some depth, though shows good signs of promise for the future.

Regulation

Product

Advance Assurance is sought for each investment.

Manager

The manager of the Fund is Praetura Ventures Limited. It is FCA-registered (number 817345). Submissions to Companies House appear to be up to date.

Risk analysis/commentary

Praetura appears to be a very well set-up company with a credible investment process. The team brings a range of entrepreneurial and finance experiences. The bias towards northern companies reflects the strength of its network, and the lower valuation of companies based there should contribute positively to returns. Although the track record lacks depth, the good pace of exits is almost as promising as the returns achieved.

Investors do need to be aware that they will be investing risk capital into early-stage companies. Praetura's emphasis on post-investment is as strong, or stronger, as anyone in the sector. It is also better structured than many. It remains to be seen what difference the Venture Partners will make.

Diversification is an important consideration for any investor – while the companies that succeed are likely to produce exceedingly good returns, those who do not may return little. Diversification within the Fund is limited, although typical for products in this area. This EIS fund should be considered in the context of an investor's entire portfolio.

Investment process

Deeper dig into process

Praetura is a generalist investor looking at innovative growth companies, with most investments being technology or technology related. Based in Manchester, it has a strong network in the north of England.

This geographical bias affects the sector focus, too. Praetura lists the following sectors as its focus:

- Creative, Digital & Tech;
- Financial Professional & Business Services;
- Energy & Environment;
- Advanced Manufacturing; and
- Health & Life Sciences.

Praetura believes these are areas that the north of England is particularly strong in, and so are likely to provide the best opportunities. We note that some of these titles are somewhat general and may encompass a wide range of businesses.

There is a strong emphasis on what happens after investment, with Praetura employing the 'more than money' tagline being used in its marketing. Praetura looks for businesses that it can add value to through its support. Unusually for EIS managers, it has a separate team dedicated to supporting investments that is almost as big as that making the investments.

The Praetura framework uses 5Ms: management, market, model, momentum and money. While this is not innovative in itself, it does help bring structure to the Praetura investment process and should help to ensure more consistent decision-making.

Praetura is flexible about the stage of development at which it funds companies, although the expected investment sizes for this fund suggest that few will be seed or pre-revenue. This is corroborated by the requirement for investee companies to have a CFO or equivalent – a role that is usually filled only once a company has started to make good progress.

Overall, the targeted areas are not unusual among EIS funds, although the implicit emphasis on the north is less common. While most managers talk about their post-investment activities, Praetura does this in a more structured way than many. As usual, the key is the quality of execution.

Sourcing deals

Praetura's range of sources is fairly normal for the EIS sector and includes its professional adviser network, accelerator programmes, entrepreneurs it has worked with and its wider network.

The latter includes its Venture Partners. These are HNW individuals who have made significant investments into Praetura's funds, have relevant business experience and are willing to take an active role in Praetura's investments. They have much in common with angels for some other companies. This is a relatively new arrangement and currently there are just over 35. Opportunities for the Venture Partners to be active have been limited to date, but they should be a useful additional to Praetura's resources.

Recently, Praetura has been averaging approximately 60 enquiries for funding a month. There is the intention to grow this.

Although Praetura is agnostic about the location of investee companies, in practice, there is likely to be greater exposure to companies from the north. This reflects deeper connections and better referrals from this region, although the team also notes that valuations outside the south tend to be more attractive, too.

The run-rate of ca.60 enquiries a month is less than some other managers, but the overall quality does seem to be better than average. Since it launched its first EIS fund, the pace of investments has stepped up from previous years, but it looks like sourcing is adequate to satisfy this demand.

Decision-making

The decision-making process for Praetura has much in common with other managers, reflecting good practice in the industry.

Potential new investments are considered at a weekly meeting. Of these, roughly 15%-20% will secure an initial meeting and 5%-10% will get serious consideration. After the initial meeting, Praetura will have a preliminary idea of what the valuation will be.

Critical in this initial assessment is how well the team gets on with company management. The more in-depth assessment will include digging deeper into the company's pitch, looking to understand the key metrics of the business. Praetura also looks for momentum in the business, assesses the skills and experiences of the management team, the depth of that team and the financial model.

It is at this stage that the 5Ms will be assessed and scored. As would be expected from start-up companies, the aim is not to produce perfect scores but more to give a structured thought process. This will also guide the team on areas where it can support the investee company. The team will also request information from the Venture Partners who have relevant knowledge.

Once through this process, a paper is written for the Investment Committee. The latter meets when required rather than on a regular schedule. The terms for investing are only put to the investee company once the IC has given approval.

The IC also sanctions further diligence, which may include using external advisors. The emphasis in the commercial diligence is on validating the customer base and pipeline, although there may be a market assessment as well. Venture Partners may contribute to or lead this. Technology diligence is another area where a specialist provider may be used. In each case, the third-party will work alongside the team rather than separate from it.

The commercial and technology diligence will take place concurrently with the legal diligence. This includes Advance Assurance submission, with the investee company expected to get external support in its application.

If the diligence is satisfactory, the IC gives final approval for the transaction. Fund investors will receive a document on each investment, which summarises the information supplied to IC (typically ca.20 pages while the IC is about four times that length). Venture Partners receive more detailed information.

Companies in the fund will receive investments of between £0.5m and £2m, with investors normally receiving 10%-30% of the investee company's equity.

Investors will receive a minimum of six investments, but Praetura is aiming for eight companies. The pace of investment is a little faster than previously, but sourcing appears adequate and the team size has also increased. Some investments may be follow-ons from existing investments.

It is worth noting that the founders of Praetura have invested alongside external investors to date and almost all of the staff were investors in the first EIS fund.

Exits

Exits are expected to be via the usual routes, with trade sales dominating. Praetura guides investors to expect five to seven years for realisations.

Governance and monitoring

Advance Assurance is sought from HMRC on all investments prior to completion.

All client assets, including shares and cash, are held by The Share Centre, under instruction from the fund manager.

A report will be issued to investors twice a year, including performance update on each investee company. Praetura will not formally value the investments, but will include a valuation on a latest price basis. The reporting will also include a meaningful update on each investee company, including how it is performing relative to the targets and future plans for progress.

After investment, contact with the investee companies is handled by a dedicated team. Unusually, Praetura looks to take both a board seat and an observer position at board meetings. The former role is filled by the team member that is deemed to be the best fit, whether for sector knowledge or specific expertise. In the future a Venture Partner may also be considered. The observer position allows additional flexibility, as the attendee can be the most appropriate person for the current circumstances.

Praetura also aims to establish technology integration with the investee company's accounting systems. This allows the former to upload balances and accounts directly, as well as KPI information. Apart from corroborating management accounts, it helps to remove reporting elements from board meetings, allowing them to focus on strategic issues.

A clear framework for financial monitoring is in place. This has two elements – cash runway and a target KPI. The former is a focus of most start-ups, as running out can be fatal. Praetura brings a graded approach, with investee companies that have less than six months of runway expected to take action.

The KPI is a single metric that is most appropriate for the stage of the investee company's development. At the early stage of development, revenue growth is the most common. Progress on this metric is compared with an agreed budget. If a company is falling short, then extra support may be provided through the board observer position. Sensibly, Praetura's categorisation for 'High Performance' allows the company to fall short of the target, as most start-up management teams tend to err on the optimistic side when budget setting.

A standard term sheet is used, with most of the conditions such as drag-along and tag-along being common in the sector. Two less common elements include a priority return on a successful exit and the re-vesting of founder shares (usually over a five-year period). There is also a provision that, if the company has less than three months cash runway, Praetura can appoint additional board members.

Given the areas in which Praetura is investing, it seems likely that many investments will require follow-on funding. Some of this may come through later Praetura funds, and a conflicts committee looks at all transactions to make sure clients are treated fairly.

Track record

Between Praetura's inception in 2011 and the end of 2018, it has invested £42.0m into 25 companies over 46 transactions. This includes four investments in Praetura Asset Finance, which is a connected business.

The investments are a mixture of EIS and non-EIS eligible investments, with 10 of the companies receiving no EIS eligible money. We understand that several of the non-EIS eligible investments could have qualified, but the investors had no available relief so a different structure was used. Others were in ineligible sectors.

Of these companies, there have been eight full and one partial exit. For the full exits, £10.2m of investment produced a total exit value of £48.1m, for a credible 4.7x average multiple. If the partial exit is included this reduces to 3.7x, which is still very good. Of the full exits, half (four) were liquidations, which led to some small recoveries. The successful exit multiples ranged from 2.7x to 19.6x.

The ongoing investments have an ongoing valuation of £77.9m, a 2.4x multiple over book cost. These gains are spread across several investments, with 12 companies showing uplifts, including Praetura Asset Finance. If the latter is excluded the multiple is still 1.9x.

For a company that has not been investing for a long time, Praetura has produced a reasonable number of exits. On average, these have produced good returns, although the absolute number is not large. The success/failure ratio is typical for managers in this area. Although the track record lacks depth, the exits and unrealised values both indicate strong signs of promise.

Fees

The fees for the Fund are set out in the table on page 3. Most of the fees are straightforward, other than as noted below.

Annual fees

The annual management charge is charged annually in advance. The first year's fee will be deducted at the outset, with the balance accrued and recovered from exits.

Exit fees

The performance fee has a threshold of 120% of the gross subscription. The performance fee is based on the aggregate capital return over the investor subscription, and is charged after the other fees.

Investors who become Venture Partners will pay reduced fees.

Fundraising targets

Praetura aims to raise £10m. The Fund will have a single close on 19 December 2019, or earlier if the fundraising target is reached.

The minimum subscription is £25,000.

Investment manager

Praetura started raising money for unquoted investments in 2011, with a mixture of companies that were eligible and non-eligible for EIS investment. It launched its first EIS fund in early 2019, raising almost £15m. It has raised both equity and debt funding for companies.

People

David Foreman – Managing Director
Qualified as an accountant with KPMG. He has spent 12 years working in corporate finance and venture capital and is the co-founder of Praetura.

Peadar O'Reilly – Managing Director, Praetura Debt
Started his career at Bank of Ireland, focusing since 2002 on asset-based lending in the UK. In 2009, he moved to ABN Amro in a similar role, before co-founding Praetura Capital in 2011.

Michael Fletcher – CEO
Qualified as a Chartered Accountant with PwC before moving to Altium Capital in 2000. He spent 10 years in a corporate advisory role before co-founding Praetura. He also has various non-executive roles.

Rob Memmott – CFO
Another accountant who qualified with KPMG. He has had CFO or Finance Director roles at Servisair, Alfred McAlpine, Leeds Bradford Airport and Arrow Global Group. He joined Praetura in 2019.

Darren Carter – Non-executive Director
Worked in sales and trading at Cresvale Ltd, before taking a senior role at D.E Shaw Securities International. When the latter was bought by KBC, he took on CIO and CEO roles within investment divisions. He has been Chairman of Peel Hunt since 2010.

Jonathan Brown – Chairman
Has more than 25 years' experience as a lawyer handling commercial and corporate transactions. He is non-executive Chairman of Hill Dickinson LLP.

David Moore – Non-executive Director
Also an accountant, in 2001 he co-founded Axon Moore, a recruitment agency specialising in senior executives, especially finance professionals.

The Investment Committee consists of the members listed above, with the four executives being permanent members and the three non-executives being invitee members. The latter are invited if executive members are unable to attend or if their skill set is applicable to the decision being considered.

Praetura has a seven-strong investment team and a six-person portfolio team that provides the post-investment support and monitoring. Both teams have members with strong experience, although we note that Praetura has grown the team quickly over the past couple of years. While this means the team has the resources to handle the increased pace of investment that the EIS funds are bringing, there is the usual small risk for teams that have grown quickly.

Appendix 1 – due diligence summary

Summary of core due diligence questions		
Manager	**Praetura Ventures Limited**	**Validated by**
Founded	2018	Hardman & Co
Type	Private limited company	Hardman & Co
Ownership	Praetura Group Limited (see below)	Hardman & Co
FCA Registration	Yes – 817345	Hardman & Co
Solvency	Confirmed	Praetura
EISA member	Yes	Hardman & Co
Administrator and Custodian		
Company	Reyker Securities plc	Information Memorandum
FCA Registration	Yes – 115308	Hardman & Co

Source: Hardman & Co Research

The manager of the Fund is Praetura Ventures Limited. It is authorised by the FCA to manage an unauthorised AIF. Founded only in 2018, it has not yet produced annual accounts. Praetura states that it ensures that it will keep a balance of at least £50,000, which is multiple of its requirement.

The parent of Praetura Ventures Limited is Praetura Group Limited, ownership of which is spread over eight directors and staff members and one third party. The directors in aggregate have a controlling stake.

Appendix 2 – example fee calculations

This calculates the estimated total amount payable to the manager under certain assumptions.

Basic assumptions	
Term	5 years
Investor amount	£100,000
Company investment	£500,000
VAT on company fees is offset against revenue	

Source: Hardman & Co Research

Calculations

		Hardman & Co standard			Target
Gross return		**-50%**	**0%**	**50%**	**200%**
Amount (pre-tax relief)		**£100,000**	**£100,000**	**£100,000**	**£100,000**
Initial fees	**Rate**				
Initial charge	1.0% + VAT	£1,000	£1,000	£1,000	£1,000
Initial deal fee (company)	4.0%	£3,900	£3,900	£3,900	£3,900
Total		**£5,076**	**£5,076**	**£5,076**	**£5,076**
Annual fees – first year					
Manager (deducted upfront)	1.5% + VAT	£1,800	£1,800	£1,800	£1,800
Annual admin fee	£75 + VAT	£90	£90	£90	£90
Net investment		**£96,910**	**£96,910**	**£96,910**	**£96,910**
Annual fees – from company					
Monitoring fee	£36,000 p.a.	£13,955	£13,955	£13,955	£13,955
Gross fund after investment return		**£48,455**	**£96,910**	**£145,365**	**£193,820**
Exit fees					
Annual fee (accrued balance, 4 years)	1.5% + VAT	£7,200	£7,200	£7,200	£7,200
Dealing	0.35%	£170	£339	£509	£678
Performance	20% over 120%	£0	£0	£3,531	£13,188
Net amount to investor		£48,285	£96,571	£141,325	£179,953
Gain (pre-tax relief)		-£51,715	-£3,429	£41,325	£79,953
Gain (post-tax relief)		-£22,642	£25,644	£70,398	£109,026
Total fees to manager		£28,291	£28,461	£32,161	£41,988

Source: Hardman & Co Research

Notes: post-tax relief figures assume initial income tax relief only; other reliefs may be available to investors

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