

Smith & Williamson

Foresight 3 & 4 Linked Top Up

Venture Capital Trust Review

2 December 2009

Introduction

Rating: n n n n

- | A combined £20m generalist offering split equally between Foresight's existing 3 and 4 Venture Capital Trusts comprising of over 70 distinct companies.
- | This will add to their portfolio of VCT funds in the generalist technology sector. The focus of this fund will be a mixture of mature technology companies and 'cleantech' investments into companies operating in the sustainable and renewable energies sector.
- | The VCT will invest predominantly in unquoted companies which are substantially based in the UK.
- | Pending investment cash will primarily be held in triple A rated money market funds.
- | Of the 44 VCTs that fund raised in the 05/06 tax year, Foresight 3 and 4 are ranked 1st and 4th respectively for performance.
- | It is intended to maximise distributions to shareholders via a steady stream of dividends from income (a minimum target of 5p per share per annum) and realised capital gains to pay larger dividends as and when appropriate.

Track Record

Rating: n n n n

- | Foresight manage 4 VCTs, although funds 3 and 4 were taken over from Advent in July 2004 (the performance under Advent had been appalling).
- | The track record of Foresight VCT comprises two parts as both the O and C shares merged in 2007 and have provided a combined total return of 92.2p as at 6 November 2009.
- | Pre merger the return of the 'O' Shares (1997) was outstanding, providing a total return to shareholders of 221p, 165p of which as dividends, which is still the best performing VCT ever launched.
- | Foresight 2 "C" shares were the first VCT to target a diversified spread of environmental and cleantech investment opportunities. The O shares have a total return, incorporating Net Asset Value (NAV) and dividend distributions, of 86.8p, while the C share have provided a total return of 106.8p.
- | Foresight 3 and 4 were launched in 2004 and have total returns of 122.2p and 129.8p respectively.
- | Foresight intends to operate share-buy backs at a target discount of 10% of NAV.
- | Foresight Group recently won the 2009 Venture Capital House of the Year Award at the Unquoted British Private Equity Awards.

Management Group

Rating: n n n n

- | Foresight manages approximately £200m in their VCTs and this will be further bolstered this year. VCTs represent the major focus of the firm and as a result they are totally committed to the market and very reliant upon preserving their performance reputation.
- | Co-investment is likely to take place between VCTs 3 & 4. Other funds managed or advised by the Foresight Group are also likely to participate in co-investment.
- | Foresight have completed 26 deals since January 2006 and given their status in their chosen markets it seems reasonable to believe that they will be able to maintain this and fully invest this VCT within 3 years.

People

Rating: n n n n

- | The investment team is 17 strong and very experienced in the private equity, environmental and technology sector.
- | Bernard Fairman co-founded Foresight Group in 1984. Prior to this Bernard trained as an economist, before gaining experience at various small oil and electronics companies and then subsequently joining 3i.
- | The board and partners of Foresight are anticipating investing a further £100,000 in the offer. This is in addition to the £500,000 they have already invested.

Costs

Rating: n n n n

- | The AMC is 2.5%.
- | The TER is capped at 3.5% per annum, excluding irrecoverable VAT.
- | Foresight Fund Managers has been appointed as company secretary and accountant to both VCTs. It will receive 0.3% of net funds raised from Foresight 3 (subject to an annual cap of £100,000 which currently applies) and £60,000 plus VAT from Foresight 4 – both of these are increased each year by RPI.
- | There are separate performance fees for each VCT. For Foresight 3 the manager is entitled to a performance fee of 15% of dividends paid to shareholders provided the total return (comprising NAV plus dividends) exceeds 100p. The fee may be settled by either a cash payment or the issue of Foresight 3 Ordinary shares, or a combination of both at the board's discretion.
- | The absence of any hurdle rates before this incentive fee takes effect makes it easier to achieve than most on the market. You could argue that this aligns the interests of manager and shareholder well and will ensure that the manager is well motivated.
- | Funds raised prior to the offer for subscription launched in 2005 by Foresight 4 are subject to the right given to Foresight Group to subscribe at par for 2,109,574 Foresight 4 Ordinary Shares if the return per Foresight 4 Ordinary Share then in issue is not less than 270p prior to 1 August 2011 or 360p thereafter. Return for these purposes is the aggregate amount of all distributions (whether in cash or otherwise) paid or declared by Foresight 4 pro rata to all holders of Foresight 4 Ordinary Shares from time to time since incorporation plus the NAV per Foresight 4 Ordinary Share.

Exit Strategy

Rating: n n n n

- | There is no specific exit strategy for this VCT. It should be seen as a long-term private equity fund, with shareholder return likely to come mainly through the payment of tax-free dividends as the portfolio matures and individual investments can be realised.

Disclaimer

This note does not constitute a personal recommendation to invest and may not be suitable for everyone. Reasonable care has been taken in the compilation of this review but its accuracy is not guaranteed and all facts stated should be independently checked. No investment decision should be based on this note. Investors should review the prospectus for a VCT carefully and take appropriate financial advice from a person authorized and regulated by the Financial Services Authority to give such advice before investing. Bases and rates of tax relief are subject to future change. As such, their value depends on individual circumstances. VCT shares must be held for a minimum of 5 years to attract tax reliefs. VCTs should be seen as high risk and only suitable for individuals who can endure losses and take a long term perspective, as their value can fall as well as rise and an investor may lose all of his investment. The market in VCT shares is illiquid and it may be difficult or impossible to sell shares. Past performance should not be seen as an indication of future performance.

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