The Association of Investment Companies

Going for growth

A guide to Venture Capital Trusts

www.theaic.co.uk

Venture Capital Trusts provide finance to some of the most dynamic small businesses in the UK to help them grow.

This guide explains the benefits and risks of investing in VCTs, and takes a closer look at some of the exciting businesses that VCTs have helped to flourish.

New to investment companies?
Read 'A guide to getting started' to learn the basics


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A guide to getting started

Find out what makes an investment company tick

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Introduction

Young, innovative businesses often struggle to raise finance to help them expand. They may still be developing their products or services, so haven't been able to generate any profits from sales yet. They may be pioneers in new technologies or services which are untested. They may not have been around long enough to generate a strong financial track record, which lenders often look for when deciding which businesses to support.

These businesses can therefore find it hard to raise finance from traditional sources such as banks, something that has been made worse by the banking crisis. However, they often need a lot of capital in these early stages, well beyond the means of most individual investors. VCTs help to bridge this 'finance gap' by allowing smaller investors to pool their resources and invest in a diversified portfolio of investments to spread risk.

Though the companies VCTs invest in start small, and are high risk, they can become household names in the future, helping to create jobs and economic growth. So the government offers generous tax benefits to compensate you for the risks involved. But you should not invest in a VCT just for these tax benefits and should make sure you fully understand all the risks. If you are in any doubt, you should take independent financial advice.

This guide is aimed at retail investors aged 18 or over who are UK income tax payers.

Seeds of potential
Although the companies VCTs invest in start small, they can become household names

Parsley Box

Adrienne and Gordon Macaulay, Founders, Parsley Box

The business

Adrienne and Gordon Macaulay founded meal delivery service Parsley Box in 2017 out of frustration when they found it hard to find simple and healthy meals for Gordon's mother. Parsley Box offers more than 80 different meals delivered straight to customers via next day delivery, allowing for independent and healthy meals particularly for the elderly or those who live alone. Customers benefit from choice, easier storage, long shelf lives and on-demand service.

The opportunity

Estimates suggest that the online food delivery market will be worth around £175bn by 2025. At the time of investment, Parsley Box was projecting an annualised revenue of over £5m and had completed 130,000 orders for over 75,000 customers.

How VCTs helped

Mobeus VCTs invested £3m in 2019. The investment is being used to accelerate product development, customer acquisition and recruitment.

The results

Parsley Box is on course to hit revenues of £7m for 2019 and is targeting a long-term goal of serving 5% of the UK's 12.3m senior citizens.

www.parsleybox.com

"The traditional meal delivery services we saw were both very expensive and suffered from slow delivery. Parsley Box has reinvented the service by offering next day delivery and a wide range of meals for customers just like my mother."

Gordon Macaulay

The risks

As with all stock market investments, when you invest in VCTs your income and capital is at risk and may fall as well as rise. You should not invest in VCTs if you need a guaranteed income or if you cannot afford to lose any of your money. There are some other specific reasons why VCTs are considered to be higher risk.

- **VCTs invest mostly in small, younger companies**
  These tend to be much more risky than well-established public companies, which may have large cash resources to fall back on in tougher times.
- **The value of the underlying investments can be uncertain**
  Unlike companies that are traded on public markets, shares in private companies do not have an exact market value. A VCT will use well-established valuation methods to estimate the value of any investments they have in private companies, but they can only be estimates. Given the work involved in performing these valuations, VCTs will often only value the portfolio every three or six months and so any valuation may have been calculated some weeks, or even months, earlier.
- **Compliance with tax rules**
  VCTs have to meet strict tax rules in order to obtain their preferential tax status. If the VCT does not meet these conditions, you could lose your income and capital gains tax benefits.
- **Selling your shares**
  VCTs are generally smaller than other investment companies and so the amount of shares you can buy and sell at any one time on the stock market will tend to be lower. If you want to sell a large amount of VCT shares, you may have to plan to do this over a longer period of time. Some VCTs also offer to buy back shares to provide you with another way to sell your shares.

The tax benefits

To compensate you for the extra risks of investing in small, growing businesses, there are a number of tax benefits available when you invest in a VCT.

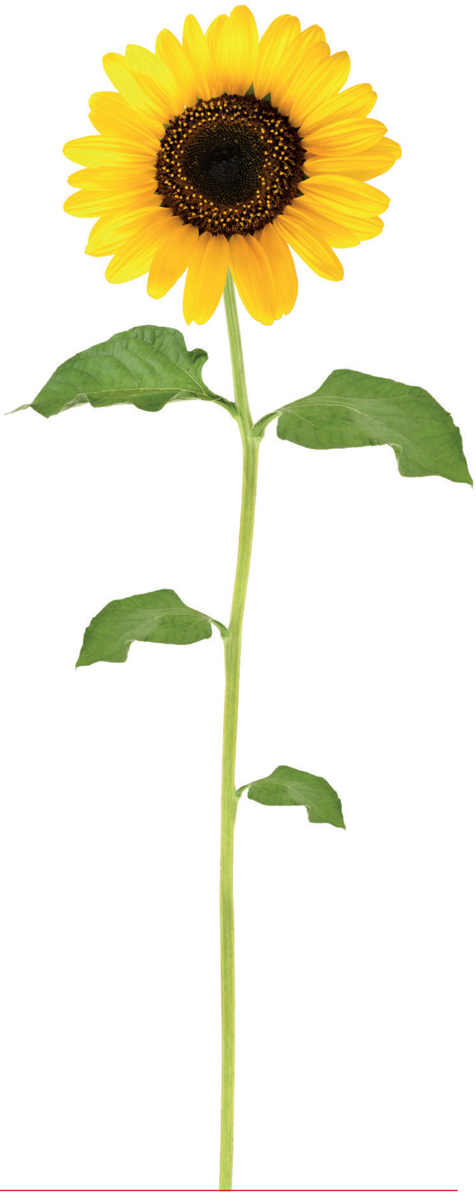
For example, you will pay no income tax on any dividends you receive, and no capital gains tax on any profits you make when you sell your shares. These two reliefs are available at all times, irrespective of how much you invest, how you buy the shares or how long you hold them.

However, if you buy shares issued on the launch of a VCT or when it raises new money, then further tax relief is available to reduce your income tax bill, providing you hold the shares for a minimum period of time and subject to certain limits and conditions. This is known as 'initial' (or 'upfront') income tax relief.

Although the tax benefits are generous, you should not invest in VCTs just for tax reasons

Current 'initial' income tax reliefs, limits and conditions

Rate of income tax relief	**30%**
Maximum investment eligible for income tax relief	**£200,000**
Minimum time investor must hold VCT shares to qualify for income tax relief	**5 years**



How you buy VCT shares

As with all investment companies, you can buy existing VCT shares through the stock market. You will still benefit from tax-free income and capital gains, but you won't get any further income tax relief. If you want to benefit from initial income tax relief, you will have to invest in new shares either on the launch of a VCT, or when it raises new money.

The VCT will issue a prospectus, which is a document that provides a lot of information about the VCT and the risks involved. You can apply for VCT shares directly via the prospectus, or you can use an independent financial adviser to help you decide which VCT would be best for you and help you make an application. There are also other financial firms that can help you to apply for VCT shares, though they do not provide advice as part of this service.

Whichever route you choose, you should read the information provided carefully and make sure you understand the risks involved. You should also consider the costs and make sure you are happy with them.

The economic benefits of VCTs

VCTs are a boost to the UK economy providing vital finance and expertise to smaller British companies and stimulating high levels of job creation. VCT-backed businesses have high levels of exports, indicative of their potential value to the UK economy.

BioAscent

The business

BioAscent is a leading provider of integrated drug discovery services.
The company was founded by former pharmaceutical executives responsible for delivering numerous clinical drug candidates over the past 30 years. It is located in state-of-the-art biology and chemistry laboratories in Scotland.

The opportunity and how VCTs have helped

Funding of £1.6m from Maven VCTs has enabled BioAscent to significantly expand its services, adding complementary chemistry and biology services to its existing compound management offering. BioAscent operates from a secure, state-of-the-art facility, currently housing over 1 million compounds on behalf of clients.

The provision of integrated drug discovery services allows it to take advantage of the growing trend towards the outsourcing of drug discovery activities.

Paul Smith,
CEO, BioAscent

"Investment from Maven has helped accelerate our growth."

Paul Smith

The results

Since Maven's investment in 2018, BioAscent has developed an enviable customer base and earlier this year the company was recognised in the Alantra Pharma Fast 50 as the top-performing outsourcer, having recorded a two-year compound annual growth rate of 67%. BioAscent was ranked third in the overall listing recognising the quality of its research and development.

Paul Smith, CEO of BioAscent commented: "We are delighted to have been recognised in the Alantra Pharma Fast 50 as the UK's fastest-growing drug discovery CRO (contract research organisation). This is a market that's now growing very rapidly and investment from Maven has helped accelerate our growth by expanding our offering and the business is now targeting international expansion."

In 2020, BioAscent was heavily involved in the UK's response to the coronavirus pandemic, helping to set up and run in conjunction with the Scottish government, a new Glasgow COVID-19 testing facility.

www.bioascent.com

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The basics of VCTs

In many ways, VCTs are like other investment companies. They give you access to a diversified portfolio of investments managed by a professional manager.

However, they differ in a number of ways:

- they invest most of their money in small, up-and-coming businesses
- in return for the higher risks, they offer additional tax benefits
- the way you normally invest in them is different

The businesses VCTs invest in

VCTs are required to invest in small, private businesses. They can also invest in similar investments traded on the Alternative Investment Market (AIM), which is the London Stock Exchange's market for smaller growing companies.

There are limits on the size of companies VCTs can invest in. Most VCT investments must be in small companies (up to £15m in size). These businesses are much more risky than the large, established companies other funds tend to invest in. Some of these companies will struggle even with the support of VCT investment, and may fail altogether. However, those that succeed can develop into some of the most exciting businesses in the UK.

Rich variety
A VCT can give you exposure to a range of up-and-coming companies

Things to consider

Are VCTs suitable for you?

VCTs are generally for more experienced investors who have already built up a solid 'core' of other investments and who fully understand the risks. If you are not sure whether, or which, VCTs might be suitable for you, you should take independent financial advice.

What type of VCT?

There are three main types of VCT. Generalist VCTs invest in a wide range of companies in different sectors. AIM VCTs invest mainly in companies quoted on AIM or other similar markets. Specialist VCTs invest in particular sectors, such as the environment, infrastructure, media, leisure or technology.

Need advice?
You should speak to an independent financial adviser

How long can you invest for?

VCTs, like all investment companies, are intended as long-term investments. If you are likely to need the money in the near future, you should not invest in VCTs. Remember that to qualify for the initial income tax relief, you have to hold on to your VCT shares for at least five years.

The costs

Managing a VCT takes specialist expertise. For example, the VCT manager has to undertake more due diligence when making an investment. They may even appoint someone to the board of the investee company. When they sell an investment, they need to find willing buyers and negotiate with them to get the best price. This additional work means that VCTs often have higher running costs than other investment companies.

Elvie

The business

Elvie is a femtech business that creates female-focused products and solutions. Their mission is to improve women's lives through smarter technology. Elvie's first major success was a pelvic floor exercise trainer and other products include a silent, wearable and wireless breast pump.

The opportunity

Femtech is one of the fastest-growing tech sectors, attracting considerable interest from investors. Over £800m has been invested in the sector since 2014 and around £600m in 2019 alone. Estimates suggest the industry could be worth £40bn by 2025.

Tania Boler,
Founder and CEO, Elvie

How VCTs helped

Octopus Titan VCT first invested in 2016, when Elvie had 17 employees. In April 2019, Octopus Titan helped support £32m of new funding, the largest femtech fundraise in history. The investment goal was to accelerate Elvie's development and expand distribution across America, Europe and Asia.

The results

By December 2019, Elvie had expanded to employ 87 people and grown revenues by more than 400%. The company also agreed a strategic partnership with the NHS that will make its pelvic floor training device available nationwide.

www.elvie.com

elvie

octopus ventures
A brighter way

Support where it's needed
VCTs help young businesses in the UK that might otherwise struggle to obtain finance

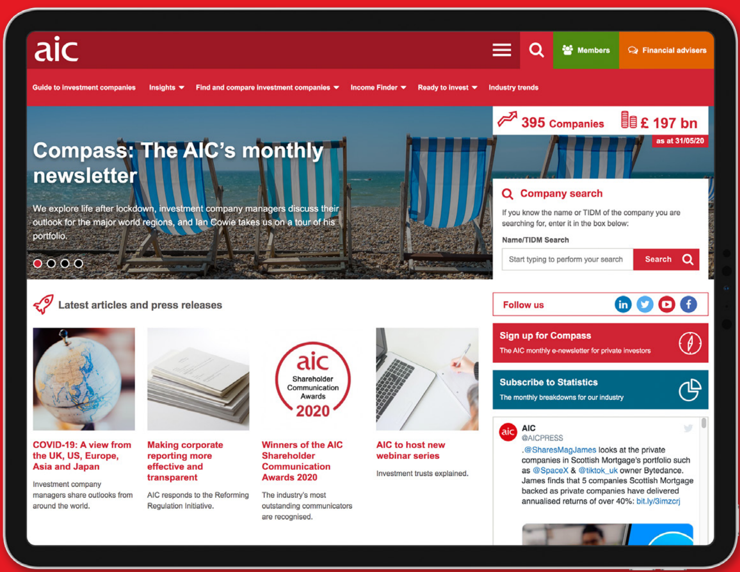
Key things to remember

- VCTs help to support some of the most dynamic young businesses in the UK, which might otherwise struggle to obtain finance. These businesses can grow to become household names, helping to create jobs and economic growth.
- In return for the higher risks, VCTs offer generous tax benefits, but you should not invest in them just for these.
- VCTs are intended as long-term investments. You will have to hold on to the shares for at least five years to benefit from the full range of tax reliefs available.
- Your income and capital are at risk, and you should not invest in VCTs if you need a guaranteed income or if you cannot afford to lose your capital.
- If you are not sure whether, or which, VCTs are suitable for you, you should take independent financial advice.

Don't forget
If you are uncertain about whether, or which, VCTs might be suitable for you, you should take financial advice

Visit the AIC website for news, statistics and comment on investment companies

www.theaic.co.uk



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