

VCT RESEARCH REPORT

PEMBROKE VCT 'B' SHARE OFFER

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Limited Life
Limited Life VCTs often invest in one sector and are normally designed to be lower risk and lower return than other VCTs.

This report is not a substitute for reading the prospectus, and any decision to invest must be made purely on the basis of the prospectus.

Risk factors

VCTs are substantially higher risk than mainstream equities. They invest in smaller companies, which can be prone to failure. VCT shares are difficult to buy and sell – the market price may not reflect the value of the underlying investments.

The value of the shares will fluctuate, income is not guaranteed and investors could lose money. Tax and VCT rules can change and tax benefits depend on individual circumstances. If a VCT loses its qualifying status investors may have to repay any tax rebate. The prospectus will give fuller details of the risks.

Their place in a portfolio

VCTs must be held for five years in order to retain the tax relief, but a ten-year view would be better as dividends are the primary source of returns as the VCT portfolio matures.

VCTs are sophisticated, long-term investments only suitable for inclusion in significant portfolios. The general view is that they should account for no more than 10% of an equity portfolio. It is difficult to access the capital invested in the short term, and anyone considering an investment should ensure they are comfortable with this, and all other risks. We assume investors will make their own assessment of their expertise and the suitability of a VCT for their circumstances. Those with any doubts should seek expert advice.

OFFER SUMMARY

Fund(s)	Pembroke VCT 'B' Share Offer
Amount seeking	£25 million
Minimum investment	£3,000



OUR VIEW

Pembroke VCT was launched by Oakley Capital in 2013 and has a bias to consumer-facing businesses, primarily those in the leisure and luxury brands sectors. While we are broadly positive on the Oakley Capital team and their investment approach, we are less keen on the structure of this VCT offer.

We like the approach of supporting promising entrepreneurs in a traditionally competitive area, where it could be difficult for businesses to obtain funding and investment from elsewhere. The Oakley Capital team is experienced in identifying unquoted investments and we believe they have the potential to deliver good returns. Their track record managing VCTs is short though and we would like to see more evidence of returns delivered to shareholders before becoming more positive.

Previous investments in Pembroke VCT have been concentrated in the health & fitness; hospitality; apparel & accessories; and media & technology sectors.

However, this 'B' share offer will raise a separate pool of money. It will be invested using the same approach and some follow-on investments will be made in existing companies (albeit at a higher price than the original investment), but new investments will also be made and the 'B' portfolio will be different overall to the ordinary share portfolio. We tend to prefer top-up offers into existing portfolios, where investors gain exposure to more mature investments that could be close to sale, as well as exciting new investments. We believe top-ups into mature and established portfolios tend to result in earlier dividends.

The VCT also has a limited life of 10 years (from the closing date of the original launch on 31 January 2014), which could be extended by up to 3 more years. At this point the VCT will wind up, aiming to sell its investments and distribute the proceeds to shareholders. As nurturing and developing smaller businesses can take time we prefer 'evergreen' VCTs, which have no fixed life.

WHAT ARE LIMITED LIFE VCTS?

Limited life VCTs, as the name suggests, have a fixed life. After a set period the manager will start selling the investments and distributing the proceeds to shareholders as tax-free dividends. Many limited life VCT managers aim to shelter capital and pay modest dividends through the life of the investment, but this VCT is managed using a higher risk approach that places more emphasis on generating attractive returns than preserving capital. While a lot of limited life VCTs are designed to be lower risk and lower return, we consider this offer to have a similar risk profile to an 'evergreen' VCT. Investors should note neither dividends nor the value of capital is guaranteed. Often, the bulk of any return from this type of investment comes from the tax relief.

PHILOSOPHY

The team aims to back some of the UK's most talented entrepreneurs, running businesses with significant growth potential. They will target those with an established brand or those with the potential to develop their brand into a well-known name.

PORTFOLIO CONSTRUCTION

Previous investments in Pembroke VCT have been concentrated in the health & fitness; hospitality; apparel & accessories; and media & technology sectors. It is likely the 'B' share capital will be invested in similar types of company. The team will consider companies at all stages of their development, from start-ups, which

are higher risk, to more mature businesses already achieving a degree of success.

Consumer-facing companies tend to be reliant on discretionary spending and can therefore struggle during a recession or tougher times when people cut back their spending. This is arguably less true for luxury brands as wealthy consumers tend to maintain their spending power through a recession. Nevertheless, we consider the focus on more economically-sensitive companies in a limited number of sectors to be higher risk.

A substantial proportion of investments are expected to be in ordinary shares, meaning gains are likely to come from any increase in value of these shares when the company is eventually sold. Part of the proceeds will then be distributed to VCT shareholders as tax-free dividends. The VCT might also provide some investments in the form of loans, the interest from which can be used to pay dividends to VCT investors, while loans also rank ahead of equity for repayment in the event the business fails, meaning the VCT could recover some of its investment to limit losses.

As the 'B' shares represent a brand new pool of assets the offer will not proceed unless gross proceeds of £5 million have been accepted by 2 April 2015. If this threshold is not reached subscription monies will be returned to investors.

COMPANY CASE STUDY

Kat Maconie, founded in 2008, designs and manufactures ladies shoes. They are sold online, in boutiques and department stores globally. Pembroke VCT invested £320,000 in June 2013, citing the following reasons for their positive view:-

- A differentiated and high-quality product at an attractive price point
- A celebrity following, including Jessie J, Ellie Goulding, Pixie Lott and the Saturdays
- Strong brand awareness, with approximately 10 pieces per month appearing in leading publications
- An international wholesale presence with shoes stocked in 20 countries
- Experienced and talented management team with design skill and commercial acumen

Please note, Kat Maconie is an investment held in the Pembroke VCT and while the team will target similar types of business for the 'B' share pool, investors in this offer will not be gaining exposure to all the existing investments.

Hargreaves Lansdown is offering a discount of 3% off the initial charge which will be paid in the form of additional 'B' shares

PERFORMANCE & DIVIDENDS

The team will aim to achieve significant capital gains from the sale of successful investments and pass part of these gains on to VCT investors as attractive tax-free dividends. There is no specific dividend target.

Having only launched in 2013 the VCT has yet to build a track record of successfully selling businesses and distributing the proceeds to investors, though the Oakley Capital team does have previous experience investing in and selling unquoted companies.

ABOUT THE MANAGER

Oakley Capital was established in 2000 by Peter Dubens. Prior to the launch of the VCT the team focused more on investing in medium-sized unquoted companies, but the VCT was launched in 2013 to take advantage of the opportunities they are seeing among smaller companies.

Most investments are sourced through an extensive network of contacts the team has built throughout their careers. They seek companies with significant growth potential and aim to take a meaningful stake in order to have influence over the company's strategy and operations, in order to help them develop successfully. They will aim to sell the business three to seven years after investing.

So far the team has made 19 investments in Pembroke VCT and the aim will be to build a similar portfolio of companies with the proceeds from this offer.

CHARGES & FEES

The initial charge is 5%. Hargreaves Lansdown is offering a discount of 3% off the initial charge which will be paid in the form of additional 'B' shares. This means investor's effective net initial charge is 2%.



The annual management fee is 2% and there are other charges and expenses. The VCT also has a performance fee. Full details can be found in the prospectus which must be read in full. Investors should ensure they are comfortable with the charging structure and risks before investing.

SHARE BUY BACK POLICY

The VCT will endeavour to buy back shares which shareholders wish to sell, but there is no specific target discount to NAV at which buybacks will take place. Investors should remember VCT shares must be held for a minimum of 5 years to retain the tax relief. Please refer to the prospectus for further details.

HOW TO APPLY

To apply please read the prospectus for the offer and fill out the application form at the back. The prospectus is available to download from the Hargreaves Lansdown website or by calling **0117 900 9000**.

The signed application and a cheque for the amount you wish to subscribe should be returned to Hargreaves Lansdown. The cheque should be made payable to the VCT, as indicated in the prospectus, but the application

and cheque must be returned to Hargreaves Lansdown in order for you to benefit from our discount. We will acknowledge your application and your share certificate and tax certificate will be sent once the shares have been allotted.

You can elect for dividends to be paid into your bank account. Please see the relevant section of the prospectus and application form for further details.