VCT RESEARCH REPORT

ELDERSTREET VCT

www.hl.co.uk
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HEAD OF INVESTMENT ANALYSIS

Generalist

Generalist VCTs primarily invest in unquoted companies in a wide variety of sectors and stages of development.

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 you could get back less than you invest. Tax and VCT rules can change and tax benefits depend on your 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
We feel VCTs should account for no more than 10% of an equity portfolio. They 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 only suitable for sophisticated long-term investors with significant portfolios. They are unlikely to be suitable for investors who may need access to their money in the short term, or for whom loss of the investment will cause hardship. We assume you will make your own assessment of your expertise and the suitability of a VCT for your circumstances. If you have any doubts you should seek expert advice.

OFFER SUMMARY

Fund	Elderstreet VCT
Amount seeking	£2.9 million
Minimum investment	£6,000

OUR VIEW

This VCT is managed by a small, but experienced team. We like their hands-on, high conviction approach which often involves taking significant stakes in companies and a seat on the board. They invest in smaller companies with already established products and services, as well as exciting businesses at an early stage of their development.

We believe this approach could result in steady annual dividends with the potential for income to be boosted from time to time if special dividends are paid following the sale of particularly successful investments. The higher conviction approach along with some earlier stage companies means we view this as a slightly higher risk VCT which could complement other generalists as part of a diversified portfolio.

WHO SHOULD CONSIDER GENERALIST VCTs

Generalist VCTs are relatively broad-based, usually investing in a range of unquoted companies across a wide variety of sectors. Some target companies which are already established and profitable, while others have a bias towards very small businesses at an early

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stage of their development. Most aim to provide steady dividends to investors with the potential for higher payments if and when they sell successful investments. They also aim to maintain or steadily grow capital over the long term.

Investors should ensure they are comfortable with an individual VCT's approach before investing. We believe building a portfolio of different VCTs is sensible as the diversification reduces risk. Starting by selecting those focusing on more mature, established companies; and then adding higher risk VCTs targeting early-stage companies to an already diverse portfolio could be wise. While you must hold the VCT for five years to benefit from the tax relief, we believe 10 years plus is a more realistic time horizon.

PHILOSOPHY

To blend established and profitable businesses with a smaller number of higher-risk, earlier stage businesses which the team believe have strong growth potential. The main focus is on identifying established companies, with strong, well-motivated management teams not overly reliant on one individual.

COMPANY CASE STUDY

Fords Packaging is a good example of a niche company in which the team has taken a significant stake and adopted a hands-on approach. It is a leading supplier of presses and sealers for closing and sealing food and drink packages. Elderstreet first invested in February 2009. They have changed the management team and are impressed with how the business is progressing, highlighting the following developments:-

- A global market for the company's products, including untapped opportunities in the US
- Its technology is being designed directly into products from big food groups such as Nestle
- There is no bank debt and £1.2 million cash on the balance sheet
- Turnover and earnings are expected to increase for the year ending December 2014

In addition, the VCT recently sold one of its investments – Wessex Advance Switching Products (WASP), a manufacturer of military and aerospace switches and lighting products. The investment was made in 1999 and highlights the long-term view needed when investing in VCTs. The successful sale has so far resulted in a 15p special dividend which was paid to shareholders in September.

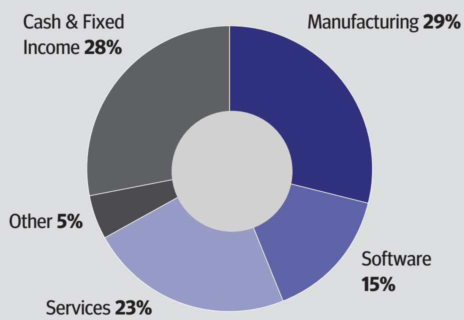
PORTFOLIO CONSTRUCTION

Investments are made across a range of industry sectors and in companies supplying products and services to a range of markets. The team has extensive experience in the software sector, and many of their higher growth businesses will come from this area. They believe they have the knowledge and experience to identify promising companies at an earlier stage of their development.

There are currently 24 smaller company investments, but there is a bias towards the top 10 which account for over 60% of the portfolio. Rather than aggressively seeking new investments the team is currently happy nurturing the current portfolio and helping existing companies become more successful.

The team also invests in some AIM-listed businesses and part of the portfolio will be invested in cash and fixed-interest investments. The chart below shows the portfolio breakdown by sector:-

Sector Breakdown



Source: Elderstreet

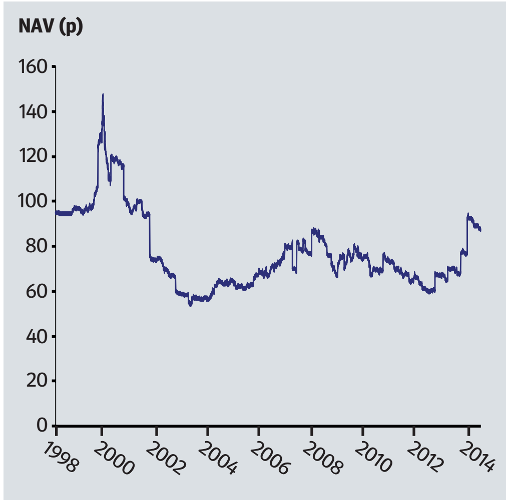
PERFORMANCE & DIVIDENDS

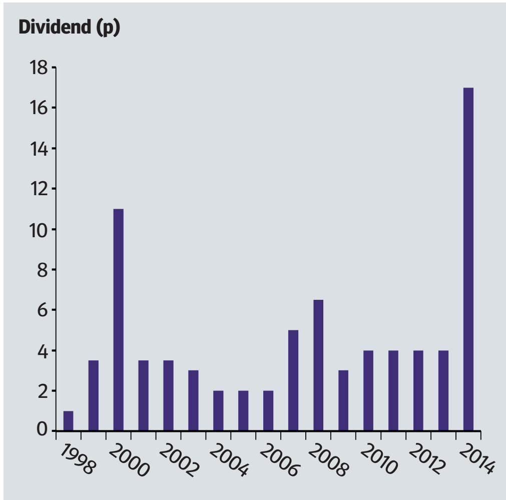
Stanislaw Tokarski / Shutterstock.com

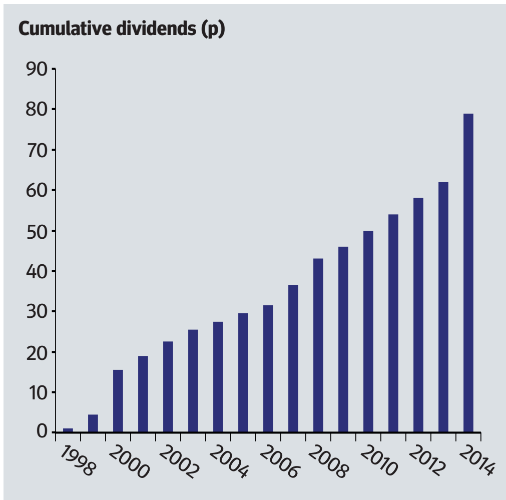
Annual dividend target:	4p to 5p per share
Payment frequency:	Semi-annually
Current yield:	5.52%

Recent performance has been good and a steady annual dividend of 4p to 5p a share should be achievable going forward, although this is not guaranteed. Over the long term the manager also aims to achieve some capital and dividend growth, including special dividends after the sale of successful investments.

In terms of long-term performance the VCT's asset value was hit following the tech crash in the early 2000s. Performance subsequently recovered, before another difficult period during the credit crunch. Performance since has been good and the VCT has paid a dividend every year since launch. Please remember past performance is not a guide to the future.







Hargreaves Lansdown is offering a discount of 5% off the initial charge for applications accepted before 14 December 2014.

ABOUT THE MANAGER

Founded in 1990 by Michael Jackson, former Chairman of FTSE 100-listed Sage Group, Elderstreet manages over £30 million on behalf of retail and institutional investors.

The team is small but experienced, comprising six individuals from a variety of backgrounds. As well as having previously worked in venture capital and private equity some of the team have direct industry experience, in the software sector for example, and some have run their own businesses. This breadth of experience has enabled them to build a wide range of contacts which helps with the sourcing of new investments.

In addition to robust management, the team seeks companies with a sustainable competitive advantage and clear opportunities for growth. Earlier stage, less mature companies are considered where there are substantial and verifiable first year sales prospects.

CHARGES & FEES

The initial charge is 5.5%. Hargreaves Lansdown is offering a discount of 5% off the initial charge for applications accepted before 14 December 2014, and 4% thereafter. The following net initial charges therefore apply (please note discounts are applied in the form of additional shares):-

Before 14 December 2014	0.5%
After 14 December 2014	1.5%

The annual management charge is 2% and there are other expenses. There are also performance fees, full details of which can be found in the prospectus. Investors should ensure they are comfortable with the charging structure before investing.

SHARE BUY BACK POLICY

The aim is to buy back shares at a discount to NAV of 7.5%, but this is not guaranteed. Buybacks will occur up to four times a year, shortly after the publication of the annual report, half-yearly report and interim management statements. 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. Shares are allotted periodically and allotment could take up to two months following the acceptance of your application. Shares will be issued according to the most recently announced NAV per share of the VCTs, adjusted for the costs of the offer.

Dividends are usually paid by cheque, but you can elect for them to be paid into your bank account.