

Full SEIS Report

The Third Seed Advantage SEIS Fund

Amersham Investment Management

The Third Seed Advantage SEIS Fund is a discretionary portfolio service that will invest in start-up or early stage companies. The process is sector agnostic and is distinguished by a very structured mentoring process.

Positives

Issues

Why Invest?

Strategy: Exposure to portfolio of start-up or early stage investments across a range of sectors.

Portfolio Risk: Early stage companies carry significant risk, though Seed Mentors have had no failures to date.

The Investment Advisor

Team: Seed Mentors have built an interesting process with the most structured mentoring scheme in the market.

Depth of staff: Although the mentors give some implicit scale and there is a lot of experience on the Seed Mentors team, it is very small.

Nuts & Bolts

- ▶ **Investing:** Future closings depend on fund raisings and tax dates. Likely dates are around end of July 2016 and March 2017.
- ▶ **Diversification:** Minimum of three companies and up to ten.
- ▶ **Valuation:** Initially companies will be unquoted. Validation prior to exit mainly through follow on investments.

Specific Issues

- ▶ **Fees:** All charged via the investee companies. Notably there is no performance fee, though the other fees may be higher than average.
- ▶ **Investment Process:** Selection is focussing on a pitching and interview process. Seed Mentors feel they have a bias towards traditional businesses, though they do some limited tech too.

Seed Mentors Information

Scheme assets	£0.8m
Scheme target	£1.5m
(S)EIS assets	£3.1m
Total FUM	£7m
Launch date	2016

Analyst

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Risks

- ▶ **Target return:** The target return is £1.20 for each £1 invested, which is appropriate for a low to medium risk product. However, the stage of the investee companies suggests medium to high risk.
- ▶ **Risk mitigation:** The Seed Mentors process is very focussed on finding good management and giving them lots of appropriate support.

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Investment Process

Fund Aims

The Third Seed Advantage SEIS is a discretionary service that will invest into a portfolio of early stage or start-up companies. The target return is £1.20 for each £1 invested. There is no income target. The Fund has no set exit target, but Seed Mentors believe the investments should be viewed with a horizon of at least five years and a variety of potential routes are outlined.

There are two parties involved in managing the Fund:

- ▶ **Amersham Investment Management:** Are the managers of the Fund.
- ▶ **Seed Mentors:** Perform a role similar to an investment advisor for the Fund, sourcing the investment opportunities.

Seed Mentors are not FCA authorised, though they are intending to obtain authorised representative status. Amersham provide the appropriate FCA permissions.

Deeper dig into the process

Seed Mentors, in conjunction with Amersham, have sourced capital and investments for six SEIS funds over the last three years. It also has a relatively new EIS product to supply follow-on funding - most SEIS companies will require this if they are to be successful.

The core of the Seed Mentors approach is a pitching / interview session which has some similarities to the *Dragons Den* TV programme. To get to the pitching stage the company must satisfy some basic criteria. These include making sure they satisfy the criteria to be SEIS eligible: size, age and lack of previous funding. The companies need to present a business plan and proper financial projections. Seed Mentors inspect the latter before admitting a company to pitch.

For each pitch, a panel with a minimum of three people is convened. Currently this is done twice a month. The panel usually consists of an accountant, an experienced entrepreneur/business person from the Seed Mentors network and a Seed Mentors representative. Occasionally this is supplemented by another appropriate person.

The panel has a chance to see the business plan in advance. Each pitch lasts 45 minutes, of which about 5 minutes is an overview of the business plan and the rest is effectively a management interview. It is clear that Seed Mentors see the quality of management as the most important factor in choosing potential investments. They feel they have a finely honed questioning process and can assess management with a few key questions. Interestingly, they have had some very positive feedback on the panel sessions even from those who have been rejected, some of whom have returned at a later date and been successful.

There are a couple of key issues that Seed Mentors is looking to get clarity on. They are looking for management who have at least five years of experience in a relevant area. They are also assessing whether they have the knowledge and experience to run a company.

Sourcing Deals

Seed Mentors has a very open approach to sourcing deals. Their reputation means that they get a lot of direct approaches. They do get referrals from their network, which includes business angels, professional introducers such as accountants, existing investee companies and business coaches.

This openness does mean that often they are in a competitive position with other funders. Seed Mentors believe their mentoring process (see below) is a significant part of the reason why they are successful. We cannot determine if valuation is playing any part in this.

There are no geographical restrictions on where investments are based, though the bulk of the companies are based in the south and midlands. They do get quite a few from Wales and some from Northern Ireland, but few from the north and almost none from Scotland. We would suggest this most likely reflects their network rather than any bias.

Seed Mentors profess to be sector agnostic, but they are a little wary of tech and have a preference for more conventional businesses. They see the former as often having higher ongoing cash needs. This is not ban though and they do sometimes get peer reviews on technology, but still do not invest if it is beyond their comprehension. Looking at their existing portfolio, we can see some technology companies, notably software with specific applications.

We understand that investors in the Third Seed Advantage SEIS Fund will receive a minimum of three investments. Previous fund closings have seen between six-eight investee companies, though it could range between three and ten depending on the size of the closing and available opportunities. Seed Mentors believe that their real constraint is the amount of funds available rather than the opportunities.

In the SEIS Fund, they are looking to supply up to £150,000 per company. In most cases, this will be released in stages as a company achieves appropriate benchmarks.

It should be noted that Seed Mentors do look to complement the SEIS money invested with some from other sources. Grants are one particular source, particularly match funding, about which Seed Mentors believe they are well-informed. They also have several overseas offices which provide funds from international investors. That people are willing to make the same investments without the support of tax benefits does provide some independent validation of Seed Mentor's process.

Decision Making

Once a company passes the pitching process, it progresses to Seed Mentor's due diligence. This is a legal check on the company and the relevant individuals and an independent report on the financial projections from an accountant. It also includes a further management interview. Seed Mentors estimate that about eight out of ten who pass the initial panel also get through their due diligence.

Seed Mentors will present each investment proposal to Amersham, who will have to approve the latter. This is more than a rubber-stamping process. Amersham have a similar process in place for other EIS funds that they manage, but with investment opportunities supplied by an investment advisor. Amersham have their own due diligence, which overlaps with, but is distinct from, Seed Mentor's.

The Directors of Amersham bring significant experience themselves. Across the full range of funds that they manage, they reject around one in ten to one in twelve of proposed investments.

Governance and Monitoring

The intention is for investee companies to receive Advance Assurance from HMRC wherever possible and either to have this in place or to be in the process of obtaining it; this is a pre-requisite to start the pitching process.

Investors will receive reports from Seed Mentors every six months. Where there has been a subsequent share transaction then the valuation will be based on that. Otherwise, they will be based on Seed Mentors internal assessment in conjunction with the company's management. We note that this will bring some subjectivity to the valuations.

A key differentiator of the Seed Mentors approach is their inclusion of a structured mentoring scheme. For investee companies, a condition of agreeing to be funded is to take at least 20 hours a year of mentoring support. In practice, the support is greater and around 40 hours will be delivered this year and included in the mentoring fee. The normal agreement is for a five-year period of mentoring.

There are over 70 mentors who are drawn from the Seed Mentors network. These include several former Business Link coaches and there are specialists in various areas. There is a stated minimum of 12 hours related to finance and accounting, a typical area of weakness for new companies. Other topics may include marketing, social media, CRM or HR issues.

Delivery is normally by webinar. Topics are made known to the companies in advance so they can supply questions or raise issues beforehand. There is some pre-recorded content, though delivery is live with a Q&A facility so the mentor is able to respond to any issues that are raised. All sessions are recorded so participants can review if necessary. After each session feedback is solicited with the aim of helping the mentor and making sure the sessions are relevant.

Although several other managers are involved in supporting their investee companies, there are very few that have such a well-structured scheme for doing so. We understand that the company feedback is generally positive.

Seed Mentors also takes a Director position on investee companies. We understand that this position is usually taken by Harvey Shulman, the Seed Mentors CEO. Communication with each company usually takes place at least once a fortnight. With 25 current investments, he needs to manage his schedule effectively, though he reckons he has capacity for another 10-15. Having said that, he appears to be clear about the stage in a company's development where his input is most valuable and seems willing to be replaced when a company matures beyond that. Despite that, we do note that this does place significant reliance on a single individual.

Many of the companies are expected to require follow-on funding. A standard clause is that the Nominee (who represents the SEIS Fund shareholders) is required to consent to any future equity issue. This means that existing investors will be able to participate in follow-ons, and should be aware that failure to do so could lead to dilution. Seed Mentors are very clear about where they sit in the size chain and are comfortable supplying funding up to around £500,000-£600,000. Beyond that, they

see companies moving on to larger providers. Investors need to be aware that successful investments may bring in other managers who deal with things differently.

As noted below, due to its short history Seed Mentors have not had any exits yet from their funds. The information memorandum cites a list of possible methods, including further fund-raising, use of internally generated cash, company sale / merger or third party sale. Although the Information Memorandum makes reference to the three year minimum holding to get SEIS tax relief, Seed Mentors believe that the investments should be viewed with a horizon of 5 years or more.

Track Record

Seed Mentors was one of the earliest SEIS investors, but, like the scheme, is a relatively young company, having first raised funds in 2012. It has raised money for six SEIS funds to date and has now invested in almost 40 companies. Performance data is consequently very limited. Here we summarise the information available to date.

The latest data that we have is from August 2015 and relates to the first 17 investments made from September 2013 to April 2014. Of the seventeen companies, five (29% of the total) have had valuations validated by subsequent share transactions, mostly by other parties. These are showing an average gain of 77%. Across the whole portfolio Seed Mentors is showing a valuation uplift of 60%, with the caveat that the 12 other companies are based on internal assessments. Even ignoring the internal valuations, the average gain would be 23%, in line with the target return.

None of the investments is showing a loss, and Seed Mentors are (rightly) proud that they have had no failures in their portfolios yet. This does mean we have no insight into how Seed Mentors deals with difficult situations, both practically and for valuation purposes.

Overall it is still early days with no exits having been achieved as yet, though we understand a couple of investee companies have received bid offers. Despite that, the track record so far does look promising

Fees

All fees are charged via the investee companies. This is tax efficient and may have dilution benefits as well. VAT will be charged on all fees as applicable.

Initial Fees

Seed Mentors will charge the companies 7.5% of the amount invested into them. In addition, there is a Manager's launch fee of 2% of the funds raised.

Ongoing Fees

The Information Memorandum outlines an unusual fee structure, though it has the caveat that an alternative may be arranged and in practice almost all the investee companies have chosen this. Some of the ongoing fees are structured in a different way from normal in the area and are linked to the investee company turnover. In particular, the Annual Mentoring Fee is 5% of turnover. The Directors Fee is 2% per director of turnover.

Almost all the investee companies have preferred to go for a more certain structure and pay a total of £7,000 per annum - £5,000 for mentoring and £2,000 for the director. On a £150,000 investment this is 4.7% of the capital.

For the Manager's Fee, each company will pay £2,750 per annum on an ongoing basis.

The Custodian Fee is aggregated and split between the investee companies. This is estimated at an initial fee of £3,500 with an aggregate annual fee of £8,500.

There are also some other fees. Investee companies can pay for additional mentoring if they wish at a rate of £75 per hour plus VAT. This would only be applied to one-on-one sessions and, although some of these have taken place, in practice there have been no charges for this service. The Manager or Seed Mentors have the right to charge "reasonable arms' length expenses". Seed Mentors tell us that this covers requests from companies outside their normal involvement, and again is rare. There is also provision for an Introducers Fee for services, but we understand this is not charged in practice.

Exit Fees

There is a fee when the manager's services are terminated of £1,500.

There are no other exit fees. In particular, there is no performance fee.

The absence of a performance fee is positive in terms of creating value for shareholders. However, the other fees may be higher than average, particularly for smaller investments.

Fund-raising targets

The aim is to raise a total £1.5m for the fund over the next two years. Closings may take place in tranches of £250,000 in order to allow funds to start to be invested. The minimum amount raised will be £250,000 (subject to manager discretion) and the manager currently anticipates that this figure will be exceeded. The fund has a target life of between three and six years.

The minimum investment is £5,000.

Risk Analysis/ Commentary

Note that there are generic risks from investing in SEIS or unquoted companies in addition to the specific ones commented on below. Comments on relative risk refer to other (S)EIS investments and not to wider investments.

For direct clients, shares and client money are held by the custodian, Woodside Corporate Services Limited (FCA registered – number 467652). Cash is held in a separate client account. No interest is payable on funds held.

The target return of £1.20 for each £1 invested suggests a medium to low risk product, though most investee companies will be at an early stage suggesting a more medium to high risk product. Seed Mentors do emphasise that the target is set as a realistically achievable one rather than as an aspirational one.

With a minimum of three investee companies, there is some benefit from diversification. With a target fund size of £1.5m and investments of up to £150,000 the ultimate diversification may be dependent on the actual assets raised.

Investments will all be unquoted. The approach is sector agnostic and has no geographical limitations, though in practice most investments have been made in the south and midlands.

The structured mentoring scheme is very positive and should be helpful in mitigating risk.

The track record is limited, but it is promising. In aggregate, valuations to date are ahead of the target return, even if only subsequent transactions are considered (29% of companies). Seed Mentors are rightly proud that they have had no company failures to date, but investors should be aware that given the profile of the investee companies there will be some eventually.

As yet Amersham's track record is not sufficient to provide significant support in itself. The Directors do bring appropriate experience and the extra scrutiny of investments may provide retail investors with additional comfort.

Overall the Seed Mentors approach is an interesting and distinctive one with a track record that suggests it may be a successful one.

Investment Manager

Regulation

Amersham Investment Management

Amersham Investment Management Limited is a limited company incorporated in 2009 as Beach Street Financial Solutions, changing its name in 2012. It is FCA Registered (number 507460) with appropriate permissions for a fund manager. The latest accounts are as of 31 October 2015 and are abbreviated under the small company provisions. Shareholders' funds at that date were £136,000. The company is a "BiPru 50" firm and exceeds its capital requirement comfortably.

Paul Barnes owns 81% of the ordinary shares of Amersham, with the balance owned by Michael Waller-Bridge.

Seed Mentors

Seed Mentors Limited is a limited company incorporated in 2012. It is not FCA Registered. The latest accounts are as of 31 May 2015 and, as it is a small company, they are abbreviated. Shareholders' funds at that date were a negative amount of £188,806. There has been a small share issue since.

Harvey Shulman is the majority owner of Seed Mentors, with other members of staff owning small stakes.

People

Paul Barnes – Director, Amersham

Has a broad background, having been involved in Tradepoint Stock Exchange, and was Executive Financial Director of Tristel and Oxford Catalysts during their AIM admission. Established Beach Street as a corporate advisory firm.

Michael Waller-Bridge – Director, Amersham

Worked at the London Stock Exchange before co-founding Tradepoint where he served as CEO from 1994 to 1997. Until 2008, he worked as an advisor to various ventures including online stockbroking, fund management and a business incubator.

Harvey Shulman – CEO, Seed Mentors

Qualified and worked as a solicitor from the early 1970s. Created several innovative property-based BES products and continued with pub and film companies for EIS. Built up Solitaire, a residential property company which was sold in 2006 for £40m. Has acquired some solicitors' practices and still consults for law firms.

Shani Randall – Operations, Events and Sales Manager, Seed Mentors

Has an extensive background in sales and marketing in the software, call centre and business centre markets. Is responsible for the mentor programme as well as sales at Seed Mentors.

Edward Mackewn – GH Canfields LLP

A corporate solicitor at GH Canfields, he is very involved in the documentation and the due diligence process: Seed Mentors regard him as a key member of their team. Has experience in advising start-up companies and specialises in SEIS.

In summary, the Seed Mentors team, especially Harvey Shulman, brings a lot of relevant experience. The mentors add some implicit scale, though the core team is very small. The Amersham Directors also have widespread experience in many technological areas, and possess a broad range of contacts who they will use in their validation of suggested investments.

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