Seneca EIS Portfolio Service

Tax-Advantaged Investments

EIS Review

APRIL 2018

Contents

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Overview

Seneca Partners Limited ("Seneca" or the "Manager") is raising funds for the Seneca EIS Portfolio Service (the "Service") for the tax year 2017/18.

As an evergreen product, it has been open to new and existing shareholders since December 2012 and has raised over £50 million to date.

Investment Details:

Score:	**85**
Offer Type	Discretionary Non-Approved
EIS Strategy	Generalist
Share class AUM (Pre-Offer)	£50 million
Manager* AUM	£104 million
EIS Risk Level	Medium

Investment:

Minimum subscription	£ 25,000
Maximum qualifying subscription per tax year	No maximum subscription
Early bird discount	None

Closing Dates:

N/A

*AUM of Seneca Partners Group

This document verifies that *Seneca EIS Portfolio Service* has successfully completed our independent due diligence process, having passed through all stages of the governance process in the run-up to the report's publication on the date listed below. It has therefore been awarded the MJ Hudson Cornerstone Trustmark.

Risk Warning for EIS Schemes

Individuals should always read and bear in mind the risk warning notices that are included within providers' investment offer literature/documentation, including prospectuses, information memorandums, securities notes, brochures and other related marketing literature. Whilst the following list is not exhaustive, some of the main risks to be aware of include:

- Investments are in small, unquoted companies and should be considered as high risk;
- Investments are illiquid and need to be held for at least three years in order to retain the initial income tax relief;
- An EIS/Seed EIS investment should be viewed as a long-term investment;
- Legislation, along with the nature and level of tax reliefs is subject to change. There can be no certainty that investments will be eligible or remain eligible for EIS/Seed EIS Relief;
- Historic investment performance cannot be used as a guide to future performance, and the value of any given investment may rise or fall;
- Many EIS/Seed EIS Schemes involve investment in a single company or sector and therefore should only be considered as a small part of an overall portfolio;
- Investors may not have independent representation on the Boards of investee companies which can mean their interests are not adequately considered relative to the executive team;
- EIS/Seed EIS investments should only be considered by sophisticated investors who understand, and have given careful consideration to, the underlying investment strategy and associated risks. For help in determining potential investment suitability, professional advice should be sought;
- Often there will be no regulatory oversight and investors will usually not be eligible for compensation if things go wrong.

Executive Summary

Offer: *Seneca Partners Limited ("Seneca" or the "Manager") is looking to raise funds for the Seneca EIS Portfolio Service (the "Service") for the tax years 2017/18 and 2018/19. The Service seeks to provide investors with a portfolio of between four to six EIS-qualifying investments in UK small companies situated mainly in the Midlands, the North West, Yorkshire and the North East. The Manager aims to achieve an exit in less than five years.*

MANAGER:

Founded in 2010, Seneca Partners Limited ("Seneca" or the "Manager") is a specialist corporate financier providing equity/debt funding and advisory services to small and medium sized enterprises ("SMEs"), which Seneca defines as businesses with an annual turnover of up to £100 million. It operates mostly in the Midlands, the North West, Yorkshire and the North East, where it has established a strong presence across its group of Seneca branded companies. In order to help SMEs to raise capital tax-efficiently, Seneca entered the tax-advantaged sector in 2012, raising funds for the Enterprise Investment Scheme ("EIS") qualifying companies and an inheritance tax service using business relief ("BR"). It also provides corporate finance and debt advisory services to SMEs. The Seneca family of companies have an aggregate staff count of 70 and assets under management ("AUM") of circa £730 million. These associated companies provide a range of financial services including equity investments, debt funding and corporate advisory services to SMEs. This review concentrates on the Seneca entity that manages the EIS Portfolio Service, Seneca Partners Limited.

PRODUCT:

Launched in December 2012, the Service has invested £49.7 million in 66 investment rounds across 36 companies in a wide number of sectors, in companies where Seneca believes it has the expertise and connections to enhance the operational and trading efficiency of the business, thereby raising its valuation in order to facilitate an exit strategy, such as attracting a third party buyer or via an AIM flotation. Seneca's network of long standing relationships with intermediaries, accountants and business advisers suggests that adequate suitable opportunities can be sourced in its preferred regions outside London and the Home Counties. The Manager believes valuations can be more attractive outside the South East since there is a lower supply of venture capital ("VC") funding. The Service is generalist and sector agnostic, although the portfolio historically has been biased towards biotech/pharmaceutical companies. Seneca has stated that it has up to £16 million of potential new opportunities which could receive immediate funding from new subscription. This pipeline is shared with the Seneca Evolution EIS product, which in the case of a shortage of pipeline opportunities would be likely to take priority given its need to invest within 12 months to retain its EIS 5 certificate, although Seneca maintain this is very unlikely. Seneca remain committed to having subscriptions fully invested within the period indicated in the Information Memorandum.

SUMMARY OPINION:

Seneca's regional presence may help EIS investors with existing EIS portfolios to gain a degree of geographical diversification. Seneca has been very active in acquiring, establishing and affiliating companies to trade under the Seneca name. We acknowledge that this should boost economies of scale and rise the firm's market presence, helping it to attract good deals and raise funds. Whilst the investments in the Service are still at an early stage (most of its portfolio companies are still within the three year obligatory EIS holding period), half of the portfolio comprises of AIM listings which, if repeated for new investors, will potentially provide some liquidity for investors who like to exit promptly after the minimum holding period.

Although a smaller investment manager than the biggest players in the market, we found its governance and due diligence to be thorough and robust, and its investment team well resourced, with expertise in identifying VC opportunities. In summary, investors seeking to widen the geographical diversification to an existing portfolio of venture capital EIS companies may be attracted to the Service. Whilst the limited track record and evidence of ability to achieve exits is a concern this is in part alleviated by the group's links to the AIM market which may help successful investments to obtain a listing. It is worth pointing out that the majority of the investments were made between 2015 and 2017, and therefore a large of portion of the companies in the portfolio are still within the three-year obligatory EIS-holding period.

Positives

AT THE MANAGER LEVEL:

- Seneca has demonstrated very strong growth in assets under management ("AUM") year on year since entering the tax-advantaged sector in 2012, with particularly strong fundraising in the last year;
- The product range has grown from the provision of equity, debt and corporate advisory services to include an EIS portfolio service and an inheritance tax service as part of their tax-advantaged product range, and is expected to expand to include a VCT in the near future;
- Seneca has a wide group of affiliated companies, through which it can exploit economies of scale through the pooling of central resources for many back office and middle office functions, such as Human Resources and payroll;
- The Advisory Partners Network, which is made up of successful business owners and senior executives with whom Seneca has longstanding relationships, has helped to further boost their profile amongst potential target investments;
- Seneca is a financially stable, profitable company with adequate cash reserves, and with clearly identified future revenue streams;
- Seneca's regional presence may allow it to employ stronger investment professionals since the locations should prove attractive to those not wishing to work in London or the Home Counties, where VC firms historically tend to prefer to be located;
- All the senior management are shareholders in the business; and the shareholding is diverse, which reduces key-man risk;
- The Manager has consistently met its fundraising targets over the past four years, which has allowed it to expand its product offering;
- Governance is controlled and overseen by four committees, each linked to the Board of Directors, which is a reassuring feature;
- The Investment team of eight is, in our opinion, of ample size to fulfil the Service's mandate; it has evidenced itself as being as skilled in the construction and management of EIS investment in early stage companies.

AT THE PRODUCT LEVEL:

- The investment selection, screening and process is robust, clearly defined, and established;
- The Manager has previously made investments that subsequently listed on AIM which may increase the likelihood of being able to achieve an exit through an AIM listing for successful investments;
- Seneca's regional presence should ensure that the Service receives good deal flow from its network of professional advisers and intermediaries situated outside the South of England, where valuations, the Manager believes, are lower, thanks to the shortage of readily available capital in the regions;
- The annual management charge is deferred and until it can be paid from the proceeds of a third party sale and is only taken once investors have received back their original net subscription. This aligns the interests of the Manager with those of investors somewhat in that it strongly incentivises the Manager to achieve exits, although it should be noted that Seneca may also charge investee companies up to 4% in arrangement fees, which is implemented on a deal by deal basis;
- The pipeline appears strong, with £16 million in identified opportunities;

- The focus on businesses in the Midlands and North may provide an element of geographical diversification to investors with existing EIS portfolios;
- The Service's investment strategy is consistent with the approach encouraged in the Patient Capital Review.

Issues to consider

AT THE MANAGER LEVEL:

- The Manager has only made a small number of successful exits from any of its EIS funds and only five companies, all in the technology sector, have proved successful enough to merit a valuation uplift. However, if an investor had subscribed £100,000 to the Service and it had been invested in the five exits detailed later in this report, they would have received back £164,536.51 after all costs and charges had been paid, excluding any tax reliefs;
- The corporate structure, while creating economies of scale, is also complicated, and may lead to a lack of clarity over the different Seneca companies' functions and the conflicts of interest between them;
- The Manager is somewhat dependent on the income generated from its tax-advantaged products, and thus vulnerable to potential future commercial and legislative changes. However, relative to the wider Seneca group of companies, the revenue from the tax-advantaged business is small, and as such the impact of these risks could potentially be absorbed by other parts of the group;
- Seneca's corporate finance involvement with investee companies could potentially create a conflict of interest, however, Seneca has put in place compliance procedures to address such matters and we found the conflicts of interest policy comprehensive and detailed.

AT THE PRODUCT LEVEL:

- While Seneca regards itself as a generalist investor, the current portfolio is heavily weighted towards bio-technology due to some of the earlier investments made. Investors who have subscribed in in recent years have typically seen a lower exposure to that sector. Seneca has expressed a desire to continue lowering this exposure, which should lower the concentration risk;

- At the time of writing (February 2018), a majority of the AIM-quoted investments were trading below their cost even though the overall portfolio has risen in value, although this must be seen in the context of an overall lower market value for AIM;

- Unlike unquoted investments, Seneca has less influence over board decisions made by the AIM-listed companies;

- Given the small sample size of exits, it is difficult arrive at a meaningful conclusion about the performance of the Service. Nonetheless, it is worth pointing out that the majority of the investments were made between 2015 and 2017, and therefore a large of portion of the companies in the portfolio are still within the three-year obligatory EIS-holding period;

- The arrangement fees and monitoring fees that the Manager charges to investee companies create a conflict of interest in that the interests of those investee companies are not necessarily aligned with those of investors and they will also reduce both the cashflows and the profitability of investee companies.
- The new 7 year rule may make it more difficult for the Manager to find opportunities amongst AIM listed companies, hitherto one of its most successful areas of investment;
- Investing part of the portfolio in AIM listed stocks means performance will be vulnerable to the volatility of the AIM market as a whole;
- In exceptional circumstances, the Manager has historically shown a willingness to sell investments ahead of the minimum holding period which means investors would lose out on part of their EIS reliefs, albeit this risk is partly mitigated by the fact that each holding should represent less than 15% of the overall investment;
- The Service will be investing in similar opportunities to the Seneca Evolution EIS Service. Given that the latter service has an EIS 5 certificate that is dependent on investments being made within twelve months there is a theoretical possibility that the Service will be at the back of the queue when it comes to investment opportunities resulting in delays in putting capital to work. However, Seneca state that they have access to sufficient opportunities so that this is highly unlikely to be the case and they remain committed to having subscriptions fully invested within the period indicated in the Information Memorandum.

Manager Quality

Manager Profile

Seneca Partners Limited ("Seneca" or the "Manager") was formed in 2010 by private individuals with the aim to provide small and medium sized companies ("SMEs") with equity/debt funding and corporate advisory services, particularly in the Midlands and North of England. It entered the EIS sector in 2012, with the launch of an approved EIS fund. Subsequently, three more EIS products were launched: the EIS Portfolio Service in December 2012, under review here, the Managed Storage EIS Fund in 2016, and most recently, the Evolution EIS Approved Fund in 2018.

Since the firm's founding in 2010, the Directors have been very active in assembling an affiliation of companies to trade under the Seneca name ("the Companies"), in order to provide a range of complementary services. Thus far, it has created one subsidiary and acquired another, as well as four stand-alone entities. Although the Companies cannot be viewed as a corporate group through interconnecting holdings, they share central systems conducted from the Haydock central office, including human resources and payroll. Seneca believes this brings advantages in the form of economies of scale and increased commercial opportunities. We note these benefits, but remain mindful that the overall corporate structure is somewhat informal.

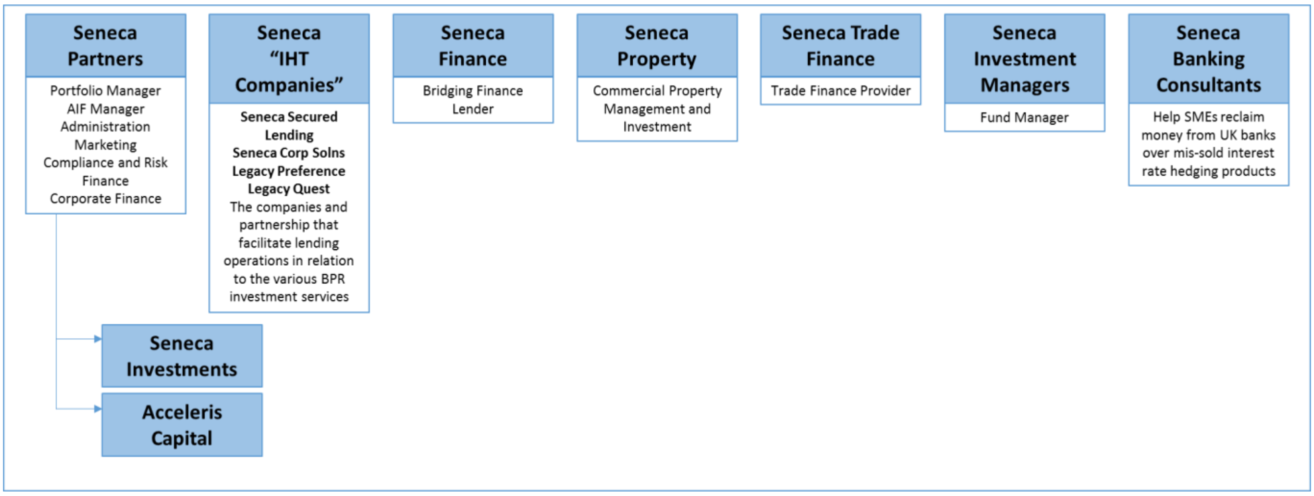
The table and chart below summarise the current seven related entities trading under the Seneca name:

TABLE 1: SENECA COMPANIES

ENTITY	ACTIVITY	LOCATION	AUM (£M)
Seneca Partners Limited	Corporate Finance/Investment Management	Haydock/ Birmingham	105
Seneca Investments Ltd	Management Consultants Turn around special situations	Leeds	Included under Seneca Partners (as AIF Manager)
Acceleris Capital Ltd	Venture Capital Investment EIS and non-EIS	Haydock	32
Seneca Investment Managers Ltd	Fund Management	Liverpool	561
Seneca Secured Lending Ltd	Asset Based Lending & Bridge Finance	Haydock	Included under Seneca Partners (as Manager)
Seneca Finance	Bridge Finance	Haydock	29
Seneca Property	Property Investment	Haydock	10

Source: Seneca; AdvantageIQ

CHART 1: SENECA COMPANIES CORPORATE STRUCTURE

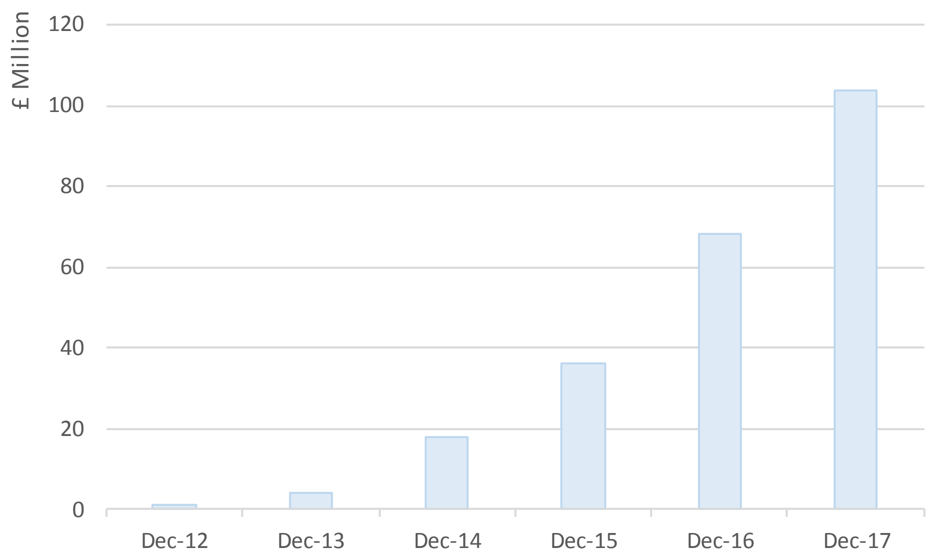


Source: Seneca; AdvantageIQ

The Seneca companies have a total staff of almost 70; Seneca Partners Limited, under review here, employs 21, and manages assets of £105 million: £73.3 million of EIS funds, and £23.5 million of BR inheritance tax products. In total, the Companies manage around £730 million. Having started as a corporate financer of SMEs in 2012, Seneca has steadily expanded its product range, and has launched products in the EIS and BR spaces, and there are plans to launch a VCT in April.

There has been considerable AUM growth, to over £100 million, with an increase of £35 million in the last year alone.

CHART 2: SENECA AUM GROWTH AS AT 31 DECEMBER 2017

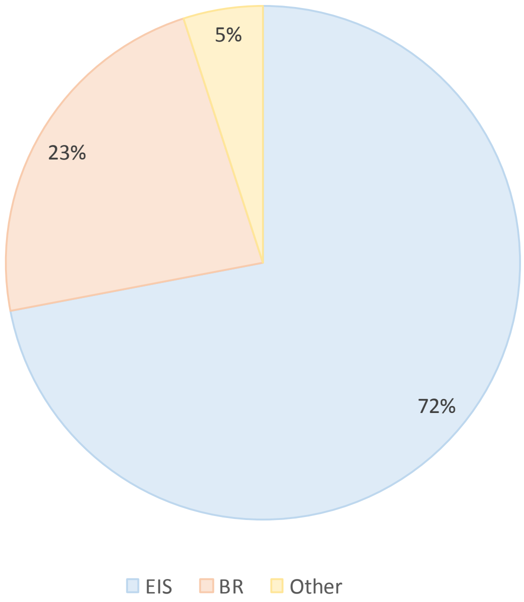


Source: Seneca; AdvantageIQ

As Seneca continues to expand its product range, it seems likely that AUM will also continue to grow. It has also benefited from Seneca's strengthening market profile; the firm has successfully established itself, through its sales campaigns, as a regional alternative corporate financier and EIS funding provider.

The chart below illustrates the breakdown by AUM of Seneca's retail product range ("Others" refers to non-tax-advantaged, bespoke investments such as loan stock on a large property assets):

CHART 3: PRODUCT BREAKDOWN OF AUM AS OF 1 FEBRUARY 2018



Source: Seneca; AdvantageIQ

We would expect Seneca's AUM to continue rising in the foreseeable future, thanks to the lack of strong competition from regional managers in EIS, and the commitment of Seneca's board to its ambitions to grow, as evidenced by the resource it allocates to the growth in tax-advantaged investments. To help maintain its AUM growth, Seneca has engaged additional salespeople to help the sales director cover a widening audience of wealth managers. In addition, Seneca has engaged the specialist marketer, LightBridge Partners[1] , since January 2015 to help raise assets. The launch of the Evolution EIS Fund, as well as plans to launch a VCT in April, both with target fundraises of £10 million, should further boost AUM.

Seneca has a dedicated client relationship team at its Haydock office, which handles incoming queries from advisers and clients. Seneca has two field-based staff to visit advisers and high net worth investors at their offices and three dedicated customer service managers. IFAs can access valuation statements online for their clients, although clients currently cannot do so themselves. However, Seneca are in the process of implementing a new CRM system which will give investors and advisers access to an enhanced online portal. Valuations of the portfolio companies are updated every month. With the changes introduced under MiFID II, investors will now receive a quarterly valuation statement on their investments, showing performance and corporate activity. For each deal, investors will receive a business summary of the rationale for investment on a six monthly basis. The Seneca website provides details of each portfolio investee company, with updated news flow on and pricing for the AIM-listed companies.

We reviewed the Manager's complaint procedure and found it robust and detailed. The Manager received one complaint in the last year which was not upheld, and stated that to date it has not received a complaint that required escalation.

In the last five years, Seneca's fund raising has steadily increased. Initial fundraising was modest, as might be expected, but fund raising has grown substantially, as the firm established its regional presence and widened its product range.
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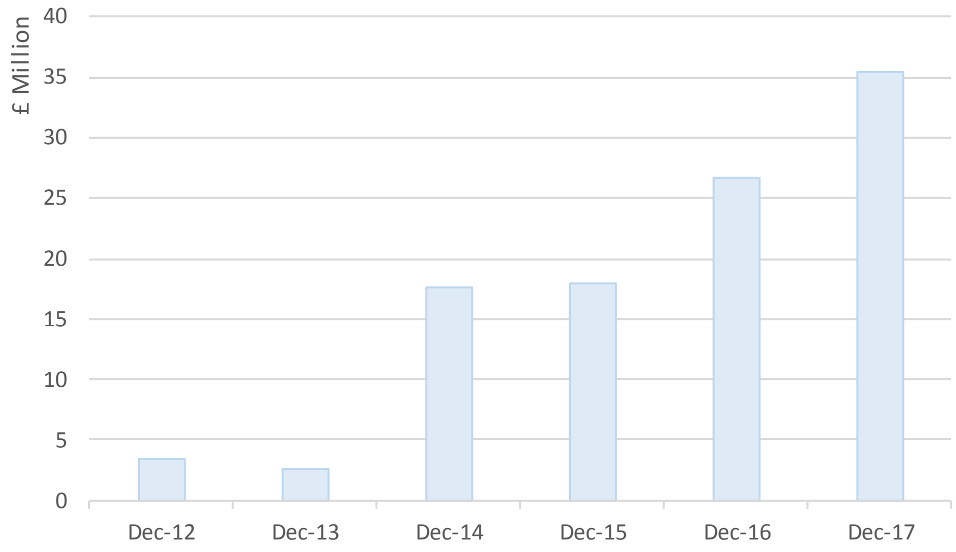
[1] Formerly LGBR Capital

CHART 4: FUNDRAISING TRACK RECORD



Source: Seneca; AdvantageIQ

Financial & Business Stability

Seneca Partners is a profitable and a growing business which is mainly dependent on tax-efficient products. Total revenue rose significantly (at a CAGR of over 50% during the past three years) throughout the 3-year period thanks to strong fundraising. Additionally, net assets rose significantly, indicating that the Manager has established a solid financial position over the past three years. Seneca Partners had a healthy cash balance as at the end of the financial year, 31 March 2017. At the time of review, the Manager had no borrowings.

The table below summarises the key financials of the Manager from 2014-2017.

TABLE 2: KEY FINANCIAL METRICS SUMMARY

	2014	2015	2016	2017	3 YR. CAGR
Revenues	1,234	3,148	3,427	4,327	52%
Revenue growth (%)	*0.00*	*155.11*	*8.86*	*26.26*	
Administrative Expenses	1,328	2,464	2,859	4,166	46%
Cost to Income ratio	*1.08*	*0.78*	*0.83*	*0.96*	
Operating Profit	-94	684	568	161	
Net Profit	-94	622	457	116	48%
Net Profit Margin (%)	*-7.64*	*19.76*	*13.34*	*2.69*	
Net Assets	511	1,133	1,591	1,708	50%
Current Ratio	*3.02*	*2.16*	*2.71*	*3.30*	
Total Debt/Equity	*0*	*0*	*0*	*0*	
Total Assets/Liabilities	*3.26*	*2.58*	*3.00*	*3.60*	

Source: Seneca; AdvantageIQ

Note: Financial statement of Seneca Partners Limited for the years ended 31 March 2015, 31 March 2016 and 31 March 2017

As described to Allenbridge, a significant portion of Seneca's revenue has to date been derived from fundraising, that is the initial fees levied on the tax-advantaged products and the arrangement fees earned from investee companies. Both these fees depend strongly on Seneca's ability to fundraise but, given its fundraising performance (as noted above), it is reasonable to expect that this is likely to be a relatively reliable source of income for the foreseeable future. However, it is worth noting that a significant drop in fund inflows may add pressure on Seneca's profit margins. The Manager, depending on the success of the EIS Portfolio Service, will be due to collect annual management fees and also performance fees once hurdle rates have been met. However, as the majority of the holdings within the Service are within their 3-year minimum holding period, the aforementioned revenues may take some time to crystallise, hence, Seneca has to depend heavily on initial fees, arrangement fees and monitoring fees. The remaining turnover is generated from activities relating to Seneca's corporate finance business and administration for other parts of the wider Seneca 'group', which adds some diversity Seneca's revenue streams. Overall costs rose by a CAGR of circa 46% over the past three years. Given the nature of Seneca's business, staff salaries and related compensation took up bulk of the total costs.

The Manager (as distinct from the wider 'group') could be vulnerable to legislation changes, since it relies to a significant extent on the revenues generated from tax-advantaged products. However, as mentioned above, the revenues generated from Seneca are relatively small in comparison to the income generated by the wider group of Seneca branded companies, hence, the impact of changes in legislation could potentially be absorbed by the wider group whilst any necessary adjustments are made to the product offerings. In this context, the Manager accounts for approximately 20% of group turnover. It should also be noted that the group is likely to provide the Manager with support in terms of staff and working capital if called upon. We note however, since three of the six affiliated companies are not controlled by Seneca but by common shareholders, it may not be enforceable and could also prove unpredictable.

Seneca informed us that it does not expect any key personnel changes, nor foresees any major corporate restructuring, in the near future. The Manager operates from an office in Haydock, and employs 21 members of staff.

Quality of Governance and Management Team

As mentioned above, Seneca was founded in 2010 by five professionals, raising additional funds from personal contacts who became passive investors. Three of the five professionals formed the board: Ian Currie, Richard Manley, and Steve Charnock. No individual shareholder owns more than 12.5%, resulting in a shareholder base that is unlikely in the near future to be influenced by one or more shareholders and can operate relatively democratically. The directors also benefit from diversified revenue from other Seneca companies.

Seneca has put in place governance structures which are robust and defensible, especially so when considering is size. There are four committees which detail processes and allocate responsibility to individual directors: the Executive Committee, the Management Committee, the Investment Committee and the Compliance Committee. Minutes are taken for the meetings of all the committees except the Management Committee.

Details of the committees are found in Table 3 below:

TABLE 3: OVERSIGHT COMMITTEES

NAME	DETAILS
Executive Committee	**Mandate:** Manage, oversee and implement the daily strategic and operational activities of the firm **Members:** All executive board members **Frequency:** Quarterly
Management Committee	**Mandate:** Project management of all products **Members:** Main directors plus heads of department **Frequency:** Weekly
Investment Committee	**Mandate:** Oversee and ratify daily and ongoing investment/portfolio activities **Members:** All executive board members plus senior investment personnel **Frequency:** Monthly, or as required
Compliance Committee	**Mandate:** To review daily activities in relation to risk and compliance **Members:** Compliance Director, Compliance Officer, CEO **Frequency:** Daily

Source: Seneca; AdvantageIQ

The ultimate decision-making body is the Executive Committee, which sets strategy, allocates resources and rules on compliance or risk issues escalated by the Compliance Committee. There has recently been an addition to the Committee in the form of Tim Murphy, a co-founder of Seneca, who is now a director.

The Management Committee sits weekly to deal with activity issues within project management, including the allocation of resources available within the firm, dealing with staff issues, project analysis, and pipeline development. Decisions are arrived at democratically, through compromise and agreement between the different divisions. If ratification at the executive level is required, issues will be escalated to the Investment Committee, but normally points are resolved.

The Investment Committee is specifically comprised of individuals with expertise in EIS and early stage company investment (it is constructed differently from those which monitor the inheritance tax service). It considers issues relating to the review and management of the Seneca EIS Portfolio Service's investment policies, strategies, transactions and direction. It sets all aspects of the investment process, reviews existing investments and ratifies proposals of new ones. It reviews client portfolios, agrees valuations, and considers offers to exit proposed by its portfolio companies. There have been two changes in the past twelve months: John Davies replaced Norman Molyneux and Gordon Lane replaced Steve Charnock.

The Compliance Committee deliberates on ongoing risk mitigation issues, the firm's compliance monitoring programme, client issues including money laundering checks, and suitability and appropriateness checks. The firm's CEO, compliance officer, and compliance manager meet daily to discuss regulatory and compliance issues, generally with regard to individual client checks and the information that clients are receiving. If any issue is outside their knowledge base, they will seek third party specialist advice.

Seneca provides corporate finance and advisory services to some of the investee companies which may create a conflict of interest with investors. However, Seneca operates under a stringent compliance procedures to address such matters and the conflicts of interest policy adhered is detailed and comprehensive.

Product Quality Assessment

Investment Team

Seneca has eight investment professionals actively running the Service, of which four have worked together or known each other for over five years as the directors and founders of the firm, with Tim Murphy most recently taking on the role of director in this part of the business. They are supported by the Portfolio Management team, which is comprised of three additional investment managers hired in 2014 and 2015, and a member of Acceleris Capital, the Manchester-based subsidiary and VC specialist acquired in 2014. All members of the team have knowledge and expertise of investing in SMEs and EIS. Acceleris advises and raises funds for early and development stage businesses, many of which are EIS qualifying.

Seneca also has access to its Advisory Partners Network (the "Network"), comprised of successful entrepreneurs and business owners, as well as senior executives. The Network allows Seneca, with its generalist approach, to access sector-specific expertise; if Seneca is unable to bring in the right level of knowledge, they will not make an investment.

With Acceleris available to cover any need for additional personnel, the Network providing specialist knowledge, and the committee approach mitigating Key Man risk, we conclude that the team is appropriately qualified and has (or has access to) the relevant expertise to run the Service's mandate.

In terms of compensation, staff are salaried with discretionary bonuses available, dependent on performance. In addition, some members of the investment team invest into companies alongside the Portfolio Service. Members of the Network who have advised on an investment also co-invest in around 60% of cases.

The biographies of the key personnel can be found in Appendix 1.

Investment Strategy & Philosophy

The Service is an evergreen product that aims to allocate investors' funds across four to six EIS qualifying investments in UK SMEs, located mainly in the Midlands, the North West, Yorkshire and the North East on a generalist basis. The current rate of deployment of investors' funds is six to eight months, well within the stated upper limit of 12 months.

The primary objective of the Service is capital growth, with the investments into later-stage, established, well-managed businesses to promote growth projects. The companies will need to have strong management above all, sound financial metrics, established market share, and a product or service that can be quickly scalable. Both the EIS Portfolio Service and Evolution EIS Fund target a return of 1.6 to 1.8x, equating to a net IRR of c. 11% and c. 13% respectively.

The Service's strategy comprises three main buckets:

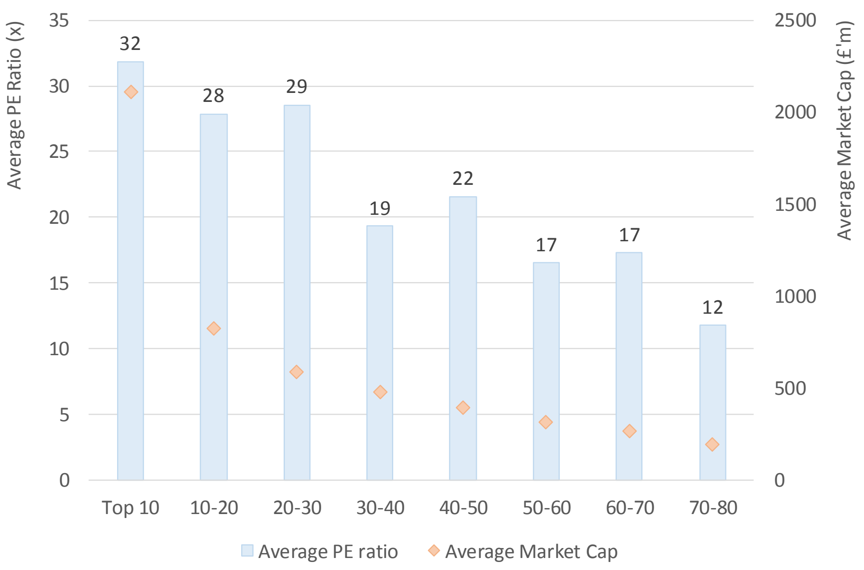
- Investing in private companies which will exit via a trade sale, to private equity or in a management buyout (MBO);
- Taking stakes in private companies with the idea of floating them on AIM and selling down their position at a price which Seneca considers represents value; and
- Tracking a company for a long time and then buying a position in that company once it has already floated on AIM.

The benefits of a blended strategy is that it allows investors to access liquidity on an ad hoc basis by instructing Seneca to sell down their AIM-listed holdings, while also diversifying away from AIM with some private holdings too. It remains to be seen if the new 7 year rule has an impact on the number of potential AIM investments that will fall into the third area above. There is a risk that investors may lose the opportunity to sell AIM holdings if they reach a good price before the end of the minimum holding period for EIS. However, the Manager has shown willingness to exit early in exceptional circumstances- for example, following a tenfold uplift within 18 months in the value of Optibiotix, 80% of each client's holding was sold gradually over a two year period to de-risk the portfolio as well as to benefit from the high valuation. In general, the Manager does not plan to exit within the minimum holding period, and Seneca would like investors to hold their investments ideally well past the minimum EIS-qualifying holding period, as many tech or biotech investments (to give a most likely example) tend to take more time than this to fully mature and realise maximum profits for investors.

There are three common objections to including AIM in an EIS strategy of this kind. The first is that valuations are already very high, and so further large uplifts are unlikely. Seneca counter this with the answer that the largest companies on AIM skew the headline statistics, and that valuations at the level Seneca looks to invest in are less frothy. For example, price-earnings multiples at the top end of the market can often be around 30x, whereas those further down the market are at more realistic levels (see Chart 5 below).

Seneca counters the first objection with the answer that it depends on which part of the AIM market one is referring to. The largest companies on AIM tend to dominate discourse around it as well as the headlines statistics; while price-earnings multiples at the top end of the market can seem pretty frothy (often around 30x), those farther down the market are at much more realistic levels (see Chart 5 below).

CHART 5: AVERAGE PRICE/EARNING OF AIM 100



Source: AdvantageIQ

The upshot that the third arm of the investment strategy, tracking a company then buying a position after it has floated on AIM, does not mean buying into companies with sky-high valuations or prohibitively expensive multiples. This chart does show that companies which float at the lower reaches of the market can see impressive PE multiple jumps as VCT money and, most clearly, Business Property Relief money comes in at higher levels of market cap. Once a company gains momentum, earlier investors can see large profits as these bigger scale investors come in at later stages of the company's development.

The second objection raised is that AIM can be very illiquid and volatile in times of market distress. This was seen clearly during the 2007/8 financial crisis, when the AIM suffered a huge collapse. While the market is now a lot more mature, deeper and more liquid than it was at that time, it is clear that AIM is more volatile and illiquid than many other markets. However, the share price of a company listed on AIM does not always reflect its value, and Seneca might well advise investors to hold on for a market rebound. Equally, it is worth noting that in the event of an AIM crash, it is likely that the entire economy, would also be under pressure, including private companies, which have an even greater lack of liquidity. A risk of the strategy, therefore, is that its advantage in providing investors with additional liquidity will not always hold.

Finally, there is the question of whether AIM companies at an EIS level could ever really deliver the returns targeted. More detail on the performance of the Service can be found in the that section, but it has already had a couple of good exits which show that such uplifts are possible, even if the number of exits is too few to be representative of exactly what sort of distribution of returns an investor might expect.

In terms of private trade sales or other exit routes, Seneca's network does lend credibility to its knowing private equity firms or trade buyers who might offer investors a good price for their investments in a private company, although the Service itself does not have enough exits here to underline this point (albeit valuation uplifts have been largely positive when franked by an arms-length third-party investment).

The Service tends to avoid technologies that require high levels of capital to develop, or firms that are in heavily regulated environments. The Service will provide small businesses with growth and development capital and advisory support, where the fundamentals appear to offer good growth prospects within five years of investing. The Manager will expect to invest between £500,000 and £2 million in each portfolio company, making four to six diverse holdings within each investor's individual portfolio (as a portfolio service, each investor gets their own individualised portfolio).

Seneca is a generalist Service, although there is currently a strong bias towards healthcare, which makes up 45% of the composite portfolio. Each investor's portfolio should have a degree of sector, industry and investment-stage diversification. However, the Manager prefers to select investments on their commercial merit rather than as part of an overall investment strategy.

The Service will seek to exit between six to seven years after the initial investment, although they emphasise that investors should expect to be invested in the long-run with exits based more on value than simply exiting quickly post-EIS qualifying holding period.

The Service is likely to make follow-on capital available to its portfolio companies before flotation. Generally, it will pay a price at par with the original investment valuation, or potentially at a premium. In the case of a potential premium, the uplift in valuation must be fully evidenced by Seneca, through the demonstration of clear growth and key milestones achieved in accordance with the original plan.

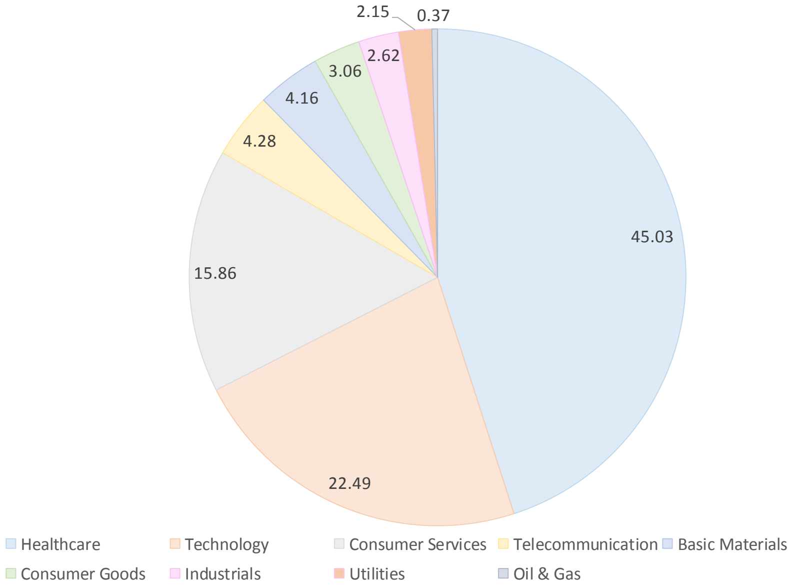
Overall, we find the strategy credible: we like the flexibility that the strategy allows, but to benefit from this flexibility the investor may have to track their investment more than a more straightforward product; the first few results show that the strategy has potential to deliver; and the ability for investors to access liquidity during benign market conditions is a plus. We look forward to seeing how the strategy fares over time: how Seneca might exit smaller companies which have been floated and which they own a large percentage of without spooking the market (otherwise selling a large chunk of the company to a single buyer makes it much like a private sale anyway), and how further exits confirm Seneca's aim to have a few great successes that more than make up for the inevitable investments that do not make out at this very early and high-risk stage of development for young companies.

Pipeline/Prospects and Current Portfolio

This is an evergreen service and its existing portfolio of investments has evolved over time to adjust for the market opportunity. The current portfolio is comprised of 66 investments into 36 companies, of which 18 are AIM listed.

As stated, the Service is sector agnostic, however, healthcare, and specifically biotech and pharmaceuticals, is a significant component of the aggregate portfolio, which Seneca attributes to the chance success of the companies in this sector (four of the nine in this sector have progressed to AIM), which both grew and received further financing rounds. Seneca expects the bio-technology/pharmaceutical sector to reduce significantly as the relevant portfolio companies become a smaller component of the overall portfolio, although over the past year biotech/pharmaceuticals has only declined from 32.8% of the portfolio to 30.7%.

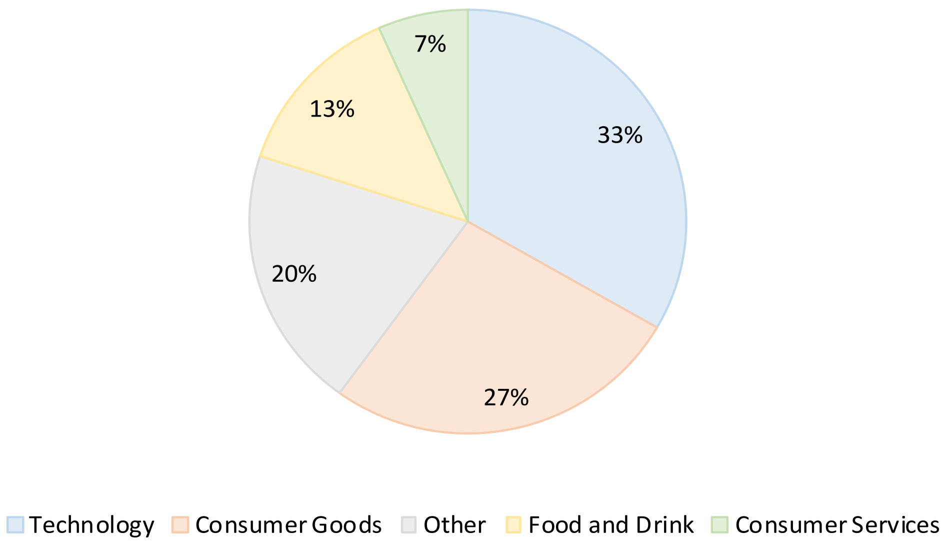
CHART 6: PORTFOLIO SECTOR BREAKDOWN AS AT 1 FEBRUARY 2018



Source: Seneca; AdvantageIQ

As of February 2018, there were 15 opportunities in the pipeline, with total investment size of £16.15 million, which are currently undergoing due diligence, the details of which cannot be disclosed. We note that the pipeline will be shared with the EIS Evolution Fund. However, Seneca expects the pipeline, if fulfilled, to be divided into the following sectors:

CHART 7: SECTOR BREAKDOWN OF PIPELINE



Source: Seneca; AdvantageIQ

If the pipeline indicated above is fulfilled, it will further reduce the overall portfolio's exposure to biotech/pharmaceuticals.

In addition to new investments, Seneca expects to provide follow-on finance to some of its investments. There is no explicit target for what proportion of funds invested will be allocated to follow-on investment, and instead it will be decided on a case-by-case basis. Based on Seneca's fundraising record, strengthening position in the regions, and the growing portfolio, we conclude that deal flow should be ample.

Investment Process

The Manager has described their investment process as follows in AdvantageIQ:

TABLE 5: INVESTMENT PROCESS

INVESTMENT PROCESS	DETAILS
Deal sourcing/origination	Deal origination is a core strength at Seneca and a large proportion of our deal flow comes to us "off market". We have a dedicated member of the team, recruited from BDO where he was the UK head of research, who focuses on developing our network of professional intermediaries and market and sector analysis and performance –this is also highly relevant when preparing investments for exit. The senior members of the team are also tasked with originating deals from their personal and long established networks. Finally we also source deals from the Seneca Partner Network which is made up of the Region's most successful entrepreneurs and where there is often the opportunity to co invest alongside existing sector specialism.

Deal filtering and selection	As Portfolio Manager to the Service, Seneca see over 500 opportunities a year and will filter to meet c200 management teams. Before a deal reaches to the first stage of our investment process it must first pass an initial due diligence process. Whilst this is not exhaustive process it does require a potential investee company to meet certain criteria before advancing to the next stage of the selection process. If a company meets the initial criteria then the next step will be management meetings and requests for further information to allow for deeper due diligence .This process alone can typically be 4-6 months duration. If a company still meets our criteria and is recommended by the investment team as one to progress then the investment case is formally presented to the Equity Investment Committee. The committee is made up of very experienced investment professionals and they agree the terms and valuation upon which the investment can be progressed to completion.
Due diligence process	Stage one consists of producing a summary of the potential deal including key features, market analysis, possible entry price, exit strategy, potential returns and key Due Diligence (DD) issues. These initial high level findings are discussed with the senior Seneca Partners team, at which point the opportunity is either declined or it is agreed to move to stage two. Stage two consists of a more detailed investigation of the investment opportunity, preparation of an investment paper supported by applicable DD findings (areas of DD may include legal, commercial, management and financial), finalisation of deal structure and agreement of terms. Usually, Advance Assurance is applied for at this stage.
Deal approval	Following approval by the Investment Committee, a summary of the approved 'Terms of Investment' is provided to the Portfolio Manager. These terms reach beyond the provision of funding. They will include voting, dragging and swamping rights to ensure we can influence the investment journey for our investors and these terms will be crucial to our level of influence and control, especially where minority stakes are held. Ultimately, this Investment Agreement will be the key driver in how we protect investors. Once agreed and accepted by the investee company the deal will move to legal completion.

We have reviewed the investment process of the Service, and were impressed with their structure and clarity. Overall, Seneca adopts a sufficiently comprehensive investment process, with a strong level of governance. The intensive due diligence process, which includes a member of the network working alongside the investee company management for a few days, operates as a robust filtering system, as well as playing a key role in risk management.

Risk Management

Seneca does not rely on traditional financial gauges and instruments, such as stop losses, correlation matrices, as it believes that they are not applicable to SMEs. Instead, it emphasises the risk mitigation value of ensuring that the shares of the investee company are bought at good valuations. The rigour of initial due diligence is therefore critical to effective risk management. Red flags that Seneca looks out for include inexperienced management, unrealistic valuations and revenue projections. Seneca relies strongly on qualitative judgement of management.

The Manager also stresses the risk mitigation value of providing portfolio companies with ongoing support, and added value during their important growth stages, and the monitoring of each company, from their board downwards. Hence, monitoring through a board position or observer rights are stipulated at outset, carefully watching to see that milestones are met. Seneca will also seek to protect itself against boards acting outside the interests of its investors by asking for written shareholder agreements. However, it is worth noting out that Seneca has less clout over AIM-quoted companies when it comes to influencing board decisions[2]. Through its monitoring role, Seneca will watch for threats to revenues such as the loss of major customers, disruptions to the management team, supplier issues, or regulatory changes. All such issues would instigate a more formal review of the investment.

At the portfolio level, the Service has guidelines for diversification. The minimum number of holdings per shareholder subscription is four, preferably six. At least four of the holdings should be trading in different sectors. Preferably, the holdings will demonstrate other disparate characteristics that might suggest diversification benefits, such as being at different stages of their development, or trading in different geographical areas. The investment committee manages the risks of individual client portfolios; it aims to limit the exposure to a single company to 10% to 25% of the invested amount and diversify subscriptions across various sectors.

Regarding the unquoted company portfolio, applying British Venture Capital Association Guidelines ("BVCA"), Seneca values unquoted companies under management at cost, unless there is a recognised impairment to warrant a reduction or a valid reason to revalue upwards.

[2] Seneca informed us that it aims to meet AIM-listed investee companies once a quarter.

Key Features

1. INITIAL AND ONGOING FUND MANAGEMENT FEE

TABLE 6: FEES TO THE MANAGER

INITIAL FEES (FUND SETUP FEES)	ONGOING ANNUAL MANAGEMENT FEES	FEES PAID TO CUSTODIAN
2.5% of investor subscription (plus VAT)	2% of net investments (plus VAT)	£55 plus VAT per investor*

Source: Seneca/AdvantageIQ

*Net Investment is the amount left after deducting initial, custodian and financial adviser fees

**Upon an Investor subscribing to the Fund, an amount of £275 plus VAT will be set aside from the initial Subscription and held in cash to cover this fee for the first five years.

The annual management fee is calculated based on the investor's net investment amount (i.e. the amount available after deduction of initial, custodian and advice fees). The annual management fee will only become payable after investors have received back their net investment amount. If returns are insufficient from the gains, Seneca will forfeit its fees. This is a commendable feature, aligning Seneca's interests with those of its investors, at least in part.

2. EARLY BIRD FEES AND OTHER DISCOUNTS

There are no early bird fees offered from this Service.

3. SUBSCRIPTION/APPLICATION FEES

TABLE 7: SUBSCRIPTION/APPLICATION FEES

TYPE OF INVESTOR	INITIAL APPLICATION FEE (AND INITIAL COMMISSIONS/INITIAL ADVISER CHARGES)	ONGOING MANAGEMENT CHARGES (AND ONGOING COMMISSIONS/ONGOING ADVISER CHARGES)
Direct Application (investors who make an application, without using a financial advisor or 'execution-only intermediary)'	5% of investor subscription (plus VAT)	2% of net investments (plus VAT)
Application through an adviser (investors who make an application through a registered financial adviser with an ongoing fee)	2% of investor subscription (plus VAT)	2% of net investments (plus VAT)

Source: Seneca; AdvantageIQ

4. PERFORMANCE FEE

Seneca charges a performance fee of 20% (plus VAT) on capital returns in excess of 100% of net investments. While we acknowledge that this is common across the industry, we would prefer a higher performance fee trigger to reflect the opportunity cost for investors and the erosion of the value of capital due to time. It is worth noting that a performance of 30% (including VAT) is levied on the investor if the Service achieves a full or partial exit from an investee company before the fourth anniversary of investment.

The deferred annual management fees will be paid after investors receive back 100p per share but before they receive excess distributions beyond this.

5. PRODUCT FEES

The detailed fees are listed in the following table.

TABLE 8: FEE DETAILS

FEES	DETAILS
Arrangement Fee (% of deal)	0-4% (plus VAT)
Monitoring Fees	0-2% (plus VAT)

Source: Seneca; AdvantageIQ

Seneca charges arrangement fees on investee companies on a case-by-case basis. This has been as high as 4%, though the weighted average arrangement fee charged has been 1.7%, because these fees are not charged to AIM-listed companies. In addition, the Managers charges a monitoring fee and the average rate so far has been 0.64%.

Performance

The Seneca Portfolio Service was launched in 2012, making its first investment in spring 2013. Since then, the Service had made 66 investments into 36 companies, of which half are listed on the AIM. We have segregated the performance of the Service in three buckets as described in the Investment Strategy Section above and have analysed the exits and the valuation of the underlying investments accordingly.

1. INVESTMENTS IN PRIVATE COMPANIES

The Service had achieved only two exits, albeit these investments were fully written off. FJ Holdings entered into administration on May 2016 as it was unable to service its debt payments. Seneca informed us that the company took on debt capital to expand its operation, however, it was unable honour the payments which led to a deterioration in its working capital position. JS Commissioning become insolvent owing to withdrawal, cancellation and delay of contract which was due to the continued suppression of oil prices in 2015 and 2016.

We note that a majority of the investments currently in the portfolio were valued at cost except for a few investments that have experienced a significant change in value.

TABLE 9: VALUATION OF THE UNLISTED INVESTMENTS AS AT 1 FEBRUARY 2018

							NUMBER OF INVESTMENTS		
SECTOR	NO. OF DEALS	COST (£000'S)	AS A % OF OVERALL COST	VALUE (£000'S)	AS A % OF OVERALL VALUE	CHANGE IN VALUE	ABOVE COST	AT COST	BELOW COST
Basic Materials	6	1,701	9%	1,701	8%	0%	-	6	-
Business Services	3	1,900	10%	1,900	9%	0%	-	3	-
Consumer Services	4	4,050	22%	4,050	19%	0%	-	4	-
Healthcare	8	2,898	15%	2,820	13%	-3%	-	6	2
Industrial	1	400	2%	0	0%	-100%	-	-	1
Oil and Gas	1	150	1%	0	0%	-100%	-	-	1
Technology	8	5,906	31%	8,894	42%	51%	5	3	-
Telecom.	2	1,750	9%	1,750	8%	0	-	2	-
Total	33	18,755		21,116		13%	5	24	4

Source: Seneca; AdvantageIQ

2. INVESTMENTS IN PRIVATE COMPANIES THAT WERE SUBSEQUENTLY LISTED ON AIM

The Manager made 7 investments in private companies that were later listed on the AIM; this includes the six follow-on investment rounds in Redx Pharma, which is a company focused on discovering drugs for cancer and fibrosis therapeutics. All the investments were performing strongly against their IPO valuations.

TABLE 10: INVESTMENT DETAILS OF PRIVATE COMPANIES THAT WERE SUBSEQUENTLY LISTED ON AIM

NAME OF THE COMPANY	COST	IPO VALUE	CHANGE IN VALUE
Evgen Pharma	500	708	42%
Redx Pharma 6	1,088	1,651	52%
Redx Pharma 5	91	154	70%
Redx Pharma 4	127	216	70%
Redx Pharma 3	194	330	70%
Redx Pharma 2	425	722	70%
Redx Pharma 1	446	758	70%
Total	**2,871**	**4,540**	58%

Source: Seneca; AdvantageIQ

3. AIM-LISTED INVESTMENTS

Seneca made 27 investments including three follow-on rounds in Redx Pharma and two in Evgen Pharma post IPO. The Manager was able to secure three exits from the AIM portfolio, which were all profitable. Two out of three were partial exits. We note the overall portfolio has risen in value by circa 26%, albeit a majority of the investment were trading below cost; this is due to the gains in investments in Business Services, Consumer Services and Utilities offsetting the depreciation in Healthcare.

The details of the three exits and status of the AIM-listed portfolio are depicted in the tables below:

TABLE 11: REALISATION DETAILS OF AIM-LISTED INVESTMENTS

NAME	SECTOR	DATE OF INVESTMENT	AMOUNT INVESTED (£000'S)	EXIT PROCEEDS (£000'S)	EXIT MULTIPLE	IRR (%)
Kalibrate Technologies PLC	Technology	Nov-2013	280	303	1.09	2
Optibiotix Health PLC*	Healthcare	Aug-2014	425	4,135	9.74	210 - 310
Premaitha Health	Healthcare	Jul-2014	19	36	1.86	23

Source: Seneca; AdvantageIQ

*Optibiotix shares sold in 57 tranches at a variety of prices over a two-year period.

TABLE 12: VALUATION OF THE AIM-LISTED INVESTMENTS

SECTOR	NO. OF DEALS	COST (£000'S)	AS A % OF OVERALL COST	VALUE (£000'S)	AS A % OF OVERALL VALUE	CHANGE IN VALUE	NUMBER OF INVESTMENTS		
							ABOVE COST	AT COST	BELOW COST
Business Services	1	652	3%	2,487	9%	282%	1	-	-
Consumer Services	1	1,250	6%	5,917	22%	373%	1	-	-
Healthcare	16	13,549	65%	8,127	31%	-40%	4	-	12
Industrial	1	667	3%	646	2%	-3%	-	-	1
Technology	6	3,967	19%	4,012	15%	1%	4	-	2
Utilities	1	881	4%	5,192	20%	489%	1	-	-
Total	26	20,964		26,382		26%	11	-	15

Source: Seneca; AdvantageIQ

Overall, given the small sample size of exits, it is difficult arrive at a meaningful conclusion about the performance of the Service. Nonetheless, it is worth pointing out that the majority of the investments were made between 2015 and 2017, and therefore a large of portion of the companies in the portfolio are still within the three-year obligatory EIS-holding period.

Appendix 1: Key Personnel

Key Investment Professionals

NAME	JOB TITLE	DATE STARTED	BIOGRAPHY
Ian Currie	Director	2010	Ian qualified as a chartered accountant in 1986 with KPMG and has been involved in corporate finance with Peel Hunt & Co, Apax Partners & Co and Altium Capital. He co-founded Zeus Group and at the point of demerger in 2010, the Group had over £350m of assets in a variety of businesses, including corporate finance, private equity, stockbroking and pension administration. Ian sits on the board of Hedley & Co Stockbrokers, is a founder and majority shareholder of Liberty SIPP, is a partner of Palatine Private Equity LLP and is on the board of trustees for the Lowry Arts Centre in Manchester.
Richard Manley	Director	2012	Richard qualified as a chartered accountant with KMPG in 2003. He worked for KPMG for over five years, initially in their audit business and latterly in their corporate recovery division working on financial and operational restructurings and formal insolvencies. In 2007, Richard joined NM Rothschild's leveraged finance team in Manchester before joining Cenkos Fund Managers in June 2008. Richard holds a BSc (Hons) in Mathematics from the University of Birmingham.
Steve Charnock	Director	2011	Steve qualified as a chartered accountant in 1986 before joining Charterhouse Securities as a building and construction analyst, later becoming a managing director and head of research. He was voted number one construction analyst in 2000 and 2001 in the Reuters survey for UK smaller companies. Steve set up a consultancy in 2003, co-founded Cenkos Fund Managers in 2007 and sits on private and public company boards. Steve has managed investments of over £100m into UK SMEs over the last 10 years.
Tim Murphy	Director	2017	Tim is a Director of Seneca Banking Consultants Ltd. He began his finance career with Barclays in 1983 where he undertook corporate and credit roles, before joining County Natwest in 1990 where he worked in structured and acquisition finance. In 1993, Tim joined the Royal Bank of Scotland's fledgling acquisition finance business, initially establishing the Leeds office. He was subsequently responsible for all UK regional teams before, in 2002, founding RBS Corporate & Structured Finance. As joint managing director, he had responsibility for the national

			mid-cap structured finance business, whilst being a member of the Banks Corporate Credit Committee. In 2005, Tim joined Deloitte (Manchester) as a corporate finance partner to establish the National Debt Advisory business, advising on capital raising and stressed debt refinancing. After a successful spell, he joined HBOS as UK Managing Director, Large Corporate in 2008. Tim joined Seneca from NorthEdge Capital, where he was a founding partner. Tim's investment record includes working on an EIS investment into a specialist healthcare manufacturer WS Rothband and the MBO of rented storage company Smart Storage. Tim became a Director in December 2017.
Gordon Lane	Head of Corporate Finance	2012	Gordon heads up Seneca's Corporate Finance Team, who provide development support to both investee and other companies. In addition, the team will help companies with both acquisitions and mergers. The Corporate Finance Team are instrumental in helping source exits for investors in our various tax-advantaged investments. Gordon is a qualified Chartered Accountant and graduated in Accounting and Business Finance.
John Davies	Investment Director	2015	John joined Seneca Partners in June 2015 as Investment Director, assisting in the deal execution of new EIS investments and managing the EIS investment portfolio. John qualified as a chartered accountant in 2006 having worked for PwC and RSM Robson Rhodes for a combined 4 years, initially in their Audit businesses and latterly in Robson Rhodes' Transaction Services team. In 2007, John joined BDO, where he worked in the Transaction Services. In 2012, John joined Clearwater Corporate Finance. John holds a BSc (Hons) in Business and Financial Management from the University of Salford.
Connor Grimes	Portfolio Manager	2014	Connor joined Seneca Partners in September 2014. He actively monitors our existing portfolio, conducts due diligence on potential investee companies and is part of the deal execution team on new investments. He also heads up our internal reporting and monitoring function which forms the basis of all investor portfolio communications. Previously he gained experience at Kleinwort Benson in London working with their Finance and Principal Investment & Advisory teams. Connor is a graduate of the Rotterdam School of Management where he earned an MSc in Finance & Investments. Alongside his academic and professional backgrounds, he has competed at the highest level in field hockey in the Netherlands and represented Canada at the Beijing Olympic Games.

Source: Seneca; AdvantageIQ

NOTE: Please be aware that the Manager mentioned in this report purchased the rights to distribute our report only (no payment was taken to undertake the research which is fully independent). To access full research services, including further tax-advantaged investment research reports, which can be used for the purpose of investment advice, please visit **www.advantageiq.co.uk** where both individual reports and subscriptions are available for purchase.

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