EDISON

Edison themes

Direct tech investors

Waiting for long-term investors to catch on

11 May 2022

With valuations in the technology sector having been substantially reset, following a buoyant 2021, we think it is time to take a fresh look at the direct technology investment sector. This is a broad group of companies and investment trusts that offer meaningful exposure to high-growth private technology companies. As quoted companies, they each offer a differentiated proposition, but with many common characteristics. All are UK-listed, with liquid investment vehicles and mature and diversified portfolios, and all operate established models with a proven track record. The shares of a number of these companies trade at a material discount to NAV despite being well-funded at both the parent company and portfolio level. As the medium-term prospects appear bright, we believe this represents a compelling opportunity for long-term and impact investors.

Cash-rich sector able to weather the storm

The European technology market remains robust and, despite concerns around inflation, the rotation out of technology and the war in Ukraine, Europe offers a deeper investment pipeline than ever before as success has built on success, with investors and entrepreneurs reinvesting from successful exits. This presents a great opportunity for the European ecosystem to catch-up with the United States over the next three to five years. Following the buoyant funding environment in 2021, portfolio companies are generally fully funded, with the parent funds themselves also cash-rich following a year of record exits, realisations and fund-raisings. This leaves the sector well-placed to see out a temporary dip in valuations and potentially even to benefit from reduced valuations for future investments.

Different flavours of impact investor

The reasons we like the direct tech investors is that each offers differentiated exposure to the private company technology sector in the UK and Europe. As recognised by governments across Europe and around the world, these are impact investors that foster innovation, create employment and drive economic growth – fully aligned with the direction of government policy. We also see the majority of their portfolios aligned with ESG goals. As yet, there has been no obvious rotation into the sector from impact funds, but we believe this may be just a matter of time.

Medium-term trends remain strongly supportive

Over the last six to nine months, discounts to net asset value (NAV) have widened (currently 0.8–1.0x historical NAV), driven by the rotation out of tech and concerns over the sustainability of what many investors saw as top-of-the-market valuations in 2021, compounded more recently by the impact of the Ukraine war and growing inflation concerns. However, with much of the froth already taken off valuations (the various special purpose acquisition companies and IPOs in 2021 are all trading materially below issue price: Exscientia, UiPath, Deliveroo, Trustpilot, Babylon Health, Cazoo and Oxford Nanopore) and the sector well capitalised, with portfolios continuing to show strong operational growth, we see no reason why European private technology returns should not hold up in the medium to long term. Rather, we believe, that the long-term investor should buy on share price weakness, confident that the medium-term trends for the sector remain intact.

Edison themes

As one of the largest issuer-sponsored research firms, we are known for our bottom-up work on individual stocks. However, our thinking does not stop at the company level. Through our regular dialogue with management teams and investors, we consider the broad themes related to the companies we follow. Edison themes aims to identify the big issues likely to shape company strategy and portfolios in the years ahead.

Companies mentioned in this report

Augmentum Fintech (AUGM)
Frontier IP (FIPP)
*HgCapital Trust (HGT)
*IP Group (IPO)
*Mercia Asset Management (MERC)
*Molten Ventures (GROW)
Oakley Capital Investments (OCI)
TMT Investments (TMT)

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Why invest in the direct investors?

The reasons we like the direct tech investors is that each offers differentiated exposure to the private company technology sector in the UK and Europe. This is a key sector that governments across Europe are keen to encourage to foster innovation, create employment and drive economic growth. Over the past decade, the United States and, more recently, China have led the way in developing mature private company ecosystems and it now appears that the UK and Europe are on the verge of a step-change of their own.

Following the buoyant funding environment in 2021, portfolio companies are generally fully funded, with the parent funds themselves also cash-rich following a year of record exits, realisations and fund-raisings. This leaves them well-placed to see out a temporary dip in valuations, and potentially even to benefit from reduced valuation expectations for new investments.

From this perspective, we see no reason why European patient capital returns should not hold up in the medium to long term and rather, we believe, that the long-term investor should buy on share price weakness, confident in the knowledge that the medium-term trends for the sector very much remain intact and supportive.

A cocktail of different flavours

Investors still appear somewhat wary of the sector, which, given the newsflow around Woodford Capital in 2019, is understandable. We believe there are compelling reasons to consider investment in the sector, with each company offering a distinct investment proposition:

- Augmentum Fintech: European fintech venture capital
- Frontier IP: equity for services for spin-outs from European scientists and researchers
- HgCapital Trust: European financial software/software-as-a-service (SaaS) private equity (PE)
- IP Group: International university intellectual property (IP) spin-outs, with a focus on ESG
- Mercia Asset Management: enabling technology in the UK regions
- Molten Ventures: leading European venture capital (VC)
- Oakley Capital Investments: European ‘founder-led’ PE
- TMT Investments: venture capital providing an Eastern Europe/US transatlantic bridge

Exhibit 1: Company overview

Company	Theme	Core model	Footprint	Core sectors	Owns FM	Third-party FUM	Dividend	NAV reporting	Listing	Five-year NAV CAGR
Augmentum Fintech	Leading FinTech VC	VC	Europe	Fintech	✘	✘	✘	Semi-annual	Main	-
Frontier IP	UK equity-for-advice IPCC	IPCC	Europe	Software/ Healthcare	✘	✘	✘	Semi-annual	AIM	27%
HgCapital Trust	Leading European Software/SaaS investor	PE	Europe, N America	Software/ SaaS	✘	✘	✓	Quarterly	Main	25%
IP Group	International IPCC	IPCC	UK/US/Aus/China	Deep tech	✓	£540m	✓	Semi-annual	Main	9%
Mercia Asset Management	Leading UK regional investor	SAM	UK regions	Enabling tech	✓	£762m	✓	Semi-annual	AIM	2%
Molten Ventures	Leading European VC	VC	Europe	Software/ Consumer	✓	£400m	✘	Semi-annual	Main	22%
Oakley Capital Investments	European founder-led businesses	PE	Europe	Tech-enabled	✘	✘	✓	Quarterly	Inv Cos segment	19%
TMT Investments	East European VC	VC	USA/Europe	Software/ Consumer	✘	✘	✘	Semi-annual	AIM	38%

Source: Edison Investment Research. Note: VC – venture capital, IPCC – IP commercialisation company, PE – private equity, SAM – specialist asset manager.

The sector is benefiting from 'survivor bias'

The Woodford scandal highlighted the risk of open-ended funds investing in illiquid investments, as private assets could not be liquidated sufficiently quickly when investors all rushed to the doors at the same time. However, each of the companies we review in this note is closed-ended, with listed shares that can be bought or sold as with any other listed company. Further, we would argue that there is now a 'survivor bias', with those models that have survived to reach maturity (ie regular exits and realisations) now battle-hardened and proven.

Common characteristics include:

- **UK listed**: all of the companies under review are UK listed, either on Aim or the main market.
- **Liquid investment vehicles**: shares in the companies can be bought and sold as with any other public market company, with a number of vehicles now valued at over £1bn.
- **Track record**: IP Group has recently celebrated its 20th anniversary, HgCapital Trust can boast a 20-year NAV track record, while all the other companies (save Augmentum) have been listed for at least five years.
- **Established models**: each company has an established investment model built around a proven investment team, with defined investment criteria.
- **Diversified portfolio**: although key investments can represent a significant minority of NAV (with concentration among the top 10 holdings typically 60%+), investment portfolios are broad, stretching from 20–100 assets of different maturities, sizes and sectors.
- **Mature portfolio**: each investor has a mature portfolio, having exited major holdings, with the prospect of ongoing realisations driving NAV per share progression in the years ahead.
- **Impact investment**: as highlighted earlier, the sector naturally plays to impact investment and ESG themes, supporting job creation, economic growth and technological innovation broadly, as well as, for example, education (Oakley Capital), improvements in health (Mercia, IP Group, Molten, Frontier IP), renewables (IP Group, Mercia) and climate technologies (Molten).

Exhibit 2: Sector specialisation and major holdings

Company	Sectors			Portfolio concentration (top 5 holdings)	Number of companies in portfolio
Augmentum Fintech	Digital banking	Wealth management	Fintech enablers	51%	24
Frontier IP	AI/Big data	AgriTech/materials	Pathogens	N/A*	17
HgCapital Trust	SME financial services	Software	SaaS	41%	42
IP Group	Life sciences	DeepTech	Renewable	55%	100
Mercia Asset Management	Life sciences	Enabling-tech	Digital gaming	56%	20
Molten Ventures	Consumer	Enterprise/DeepTech	Digital health	33%	72
Oakley Capital Investments	Consumer	Tech	Education	41%	22
TMT Investments	Big Data/Cloud	SaaS	Marketplaces	75%	55

Source: Edison Investment Research. Note: AI – artificial intelligence, SME – small and medium enterprises. *FIPP's largest holding, Exscientia, represented 52% of fair value as at 31/12/21

Liquid investment in private technology companies

The listed direct investors provide an attractive way to access private European technology companies and participate in the value they create through a diversified holding company, offering attractive liquidity to investors.

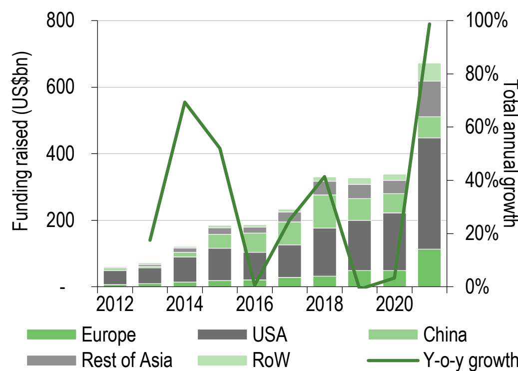
Direct European public market technology exposure remains limited, as SaaS business models and digitalisation mean start-ups are far more capital efficient than they have been in the past. When coupled with better access to private capital in Europe, companies have not faced the same pressure to list to access the capital required to drive growth. This means that companies can stay private for longer, avoiding the cost, governance issues and short-termism that can be found on the public markets. This has allowed private company investors (and entrepreneurs) to retain far more of the value created by Europe's successful start-ups.

Maturing UK and European technology sector

The European technology sector has lagged the United States and China for the past decade. Relative to both markets, Europe has few tech champions and a paucity of technology exposure on the public markets. However, after a period of acceleration, Europe is finally starting to catch-up, with a mature private technology company ecosystem delivering ever more successful businesses. Entrepreneurs are then reinvesting capital from successful exits to support the next generation of founders.

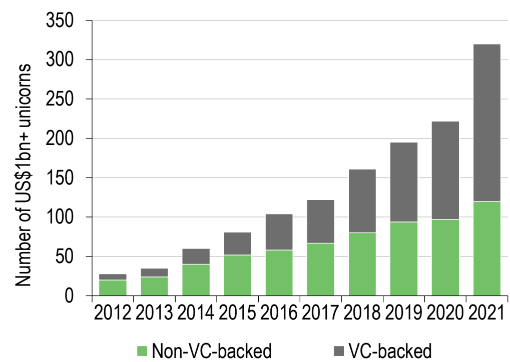
In this context, 2021 was a record year for VC investment globally; Dealroom estimates that over US$675bn was raised globally by start-ups, double the all-time high recorded in 2020. Europe led this surge in growth, growing faster than both the United States and China, with 133% growth y-o-y, with total funds raised in 2021 of US$114bn.

Exhibit 3: Europe-led funding growth in 2021



Source: Dealroom, 2021: the year London tech reached new heights

Exhibit 4: European unicorns multiplying

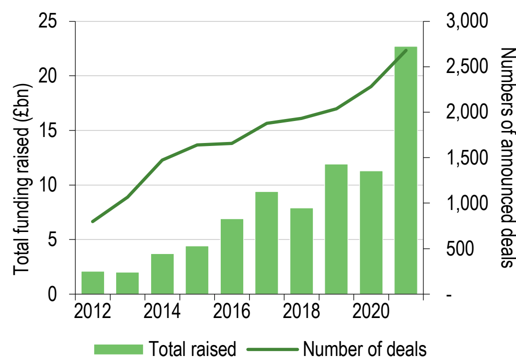


Source: Atomico, The State of European Tech 2021

The success and maturity of the European ecosystem can also be measured in terms of the number of 'unicorns' in Europe, private companies with a valuation above US$1bn. As can be seen in Exhibit 4, there was a surge in European unicorn numbers in 2021, increasing by 98 (over 40% y-o-y growth) to approximately 320 companies. Of the 98 new unicorns, 75 were VC-backed. Although the majority of unicorns are clustered in the UK, Germany, France and Scandinavia, they are becoming more dispersed, with the long tail to be found across 28 European countries, including Italy, Malta, Slovenia, Estonia and Cyprus.

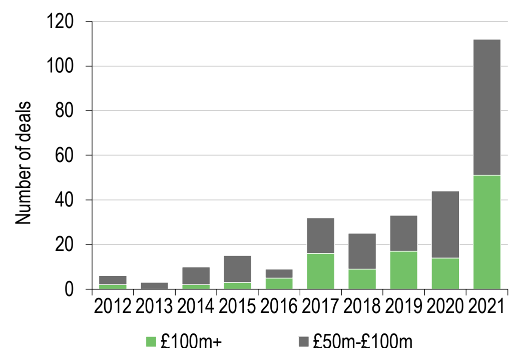
The mobility of talent and the increasing ability for companies to be based anywhere in the region are significant factors behind the success of the European private technology company ecosystem.

Exhibit 5: Announced UK funding deals



Source: Beauhurst, The Deal 2021

Exhibit 6: Growth of UK megadeals



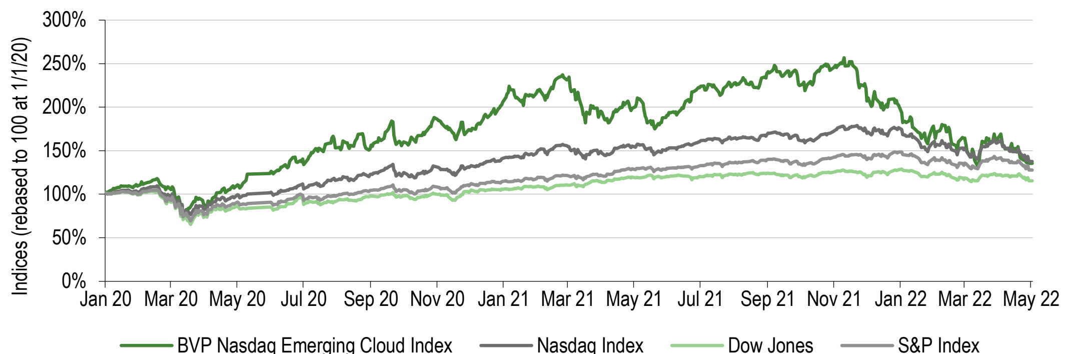
Source: Beauhurst, The Deal 2021

The UK has led this success, with almost US$23bn raised in 2021 according to Beauhurst, a UK private funding data provider. These data include more than 2,600 announced deals, with an average deal size of £8.5m, up from £5.0m in 2020. Exhibit 6 highlights the growth of UK megadeals (£50m+ rounds), which leapt from 44 in 2020 to 112 in 2021 (with even more marked growth for £100m+ rounds), contributing to the significant year-on-year increase in the average funding round size. The UK also claimed approximately 30% of all European unicorns created in 2021.

Technology sector soared in 2021, 2022 off to a bumpier start

Following the onset of the COVID-19 pandemic, technology indices soared, with the digital transition accelerating as consumers and companies were forced to embrace new, online ways of working. This trend is particularly well captured by the performance of the BVP Nasdaq Emerging Cloud Index. Although a US index (given the wide range of quoted SaaS stocks in the US and the paucity in the UK and Europe) of pure SaaS businesses, we believe it provides a good guide to sector performance in this period.

Exhibit 7: The BVP Nasdaq Emerging Cloud Index 2020–22



Source: Nasdaq OMX (10 May 2022)

Having risen to 2.5x its 2020 starting point (and more than 3x the low point in March 2020), the cloud index rose fairly steadily to the end of 2021 (ignoring some valuation-driven jitters in Q221). Then from mid November 2021, the index turned and has subsequently lost over 40% of its value, to a point where the performance of the cloud index is now broadly in line with the Nasdaq index since the start of 2020, although still up by around 35% from the beginning of 2020.

Growth shares for uncertain times

The war in Ukraine, together with the broad sanctions against Russia, have undoubtedly added to global market uncertainty. Together with consumer and price inflation and the rotation out of technology, these events have contributed to heightened share price volatility across equity markets, to which the technology sector has not been immune. Although early signs are that these factors are leading to a slowdown in global growth, the full impact on the global economy and the ultimate effect on the tech sector has yet to become clear.

Based on the BVP Nasdaq Emerging Cloud Index, median valuation multiples for US SaaS businesses (as a proxy for start-ups) have broadly returned to the more sustainable levels seen in 2014–19. While the uncertainty has not persisted long enough to have had a sustained negative effect on technology companies' underlying businesses, the public market correction is starting to be reflected in reduced valuations for earlier-stage privately held start-ups, providing the opportunity for more attractive investment entry points.

An article from *The Economist*, After a fat year, tech startups are bracing for lean times, highlights that early stage start-ups with a need for cash may struggle in the current environment, though later-stage businesses are likely to be better placed to ride out any challenges. Despite recent volatility, investors continue to be interested in high quality technology businesses, although more selectively than previously and at more appropriate valuations. With the direct investors largely well-funded, we believe this leaves them well-placed to benefit from reduced valuations.

In this inflationary environment, together with a tight labour market, the large corporate sector has a strong rationale to continue to invest in technology to generate efficiencies in its cost base. With continued disruption across most, if not all, industries and the growth of new sectors (climate tech, space tech), the ground remains fertile for technology growth to continue. Commercial traction underpins portfolio company valuations and, provided the large corporate sector keeps spending on technology, then underlying portfolio valuations should remain robust, with revenue growth substantially offsetting multiple contraction.

Private company returns provide portfolio diversification

The quoted direct technology investors (IPCC, VC and PE) provide technology exposure that is otherwise largely inaccessible to the public market investor. Valuations of private technology companies have a relatively low correlation to listed equity markets, supporting fund diversification and reducing the overall level of portfolio volatility. However, the investment vehicles themselves, are publicly traded and (as was seen at the start of 2022) subject to wider public market technology valuation trends, suffering as investor appetite has moved to 'risk-off'.

A joint report by Oliver Wyman and the British Business Bank (The future of defined contribution pensions, enabling access to venture capital and growth equity, September 2019) found that private company investment is likely to improve diversification in a multi-asset portfolio because, as an asset class, private company valuations are relatively uncorrelated with listed markets. Although private investments are exposed to broadly similar economic conditions to publicly listed equities, they are likely to be less affected by short-term swings in investor sentiment that lead to volatility in public markets. This partly reflects the time difference between asset valuations and reporting, as well as the illiquid nature of the underlying investments themselves, making them appropriate as longer-term holdings.

The Economist (How unlisted startups' valuations will adjust to falling share prices) highlighted another pillar of support for private company technology valuations, arguing that competition for leading assets, coupled with entrepreneurs using the valuations of other funding round as reference points, will help to support valuations. Even after the repricing of listed tech stocks, valuations are unlikely to fall immediately so long as new funds are being raised, providing continuing cash inflows into the sector.

Valuation: Factors in track record and prospects

Valuations of the direct investors are typically struck relative to NAV, with the shares trading at either a premium (rarely) or discount (more usually) to the latest reported NAV per share. However, management teams see a net asset-based valuation as a limited and conservative methodology, as most companies (prudently) carry assets on the balance sheet at a discount to fair value, with the majority of assets therefore recognising a gain on disposal. In addition, asset values are only reported semi-annually, or quarterly at most, meaning that due to the reporting time lag, portfolio company valuations are historic even before they are announced. Valuations for these fast-growing private company portfolios are therefore struck relative to a prudent view of NAV per share (first discount), based on an historic NAV (second discount). As can be seen through the companies'

individual reporting histories, this should afford investors some comfort that valuations are prudent and realistic, even in a downturn.

Exhibit 8: Valuations for the direct tech investment companies

	Price	Currency	Market cap (m)	Last NAV reported (m)	Net cash/ (debt) (m)	NAV per share	NAV premium/ discount
HgCapital Trust	381	GBp	1,746	1,980	(93)	433	0.88
Frontier IP Group	74	GBp	40	47	6	85	0.87
Augmentum Fintech	121	GBp	218	267	44	142	0.85
Mercia Asset Management	33	GBp	143	186	52	42.4	0.77
Oakley Capital Investments	417	GBp	743	1,020	180	571	0.73
Molten Ventures	589	GBp	902	1,421	53	929	0.63
TMT Investments	5.30	USD	167	283	19	9.00	0.59
IP Group	77	GBp	800	1,738	276	167	0.46
Peer group mean							**0.72**
Peer group median							**0.75**

Source: Company accounts, Refinitiv. Note: Priced on 10 May 2022.

Exhibit 8, shows the spread of valuations across the sector, with HgCapital Trust, Frontier IP and Augmentum Fintech leading the pack with a discount of c 10–15% and IP Group, TMT and Molten outliers on the downside, with investors potentially factoring in the falls in value of their quoted portfolio companies (IP Group – Oxford Nanopore, TMT – Bolt as a close proxy to Uber, and Molten – TrustPilot, UiPath and Cazoo). Broadly speaking, the companies trade in a range of 0.6–0.9x historic NAV. TMT and HgCapital Trust have delivered the strongest five-year NAV per share CAGR and Mercia and IP Group the weakest five-year NAV per share CAGR (Exhibit 1). This weaker track record is at least in part attributable to M&A, with IP Group having completed the acquisition of Touchstone Innovations (October 2017) and Mercia the acquisition of the Northern VCT fund management business (December 2019) over the five-year period. Mercia and IP Group have each delivered a most recent two-year NAV per share CAGR above 20%.

Unsurprisingly, valuations appear to be determined by a blend of factors, including:

- **Historic track record** – measured by the 5y/10y CAGR, using the past track record as a measure of the maturity of the business, the quality of the business model and an indicator of future performance.
- **Level of discount/premium to NAV** – we would expect to see a wider discount to NAV as compensation for a weaker track record, offering the promise of a narrowing discount to boost investment returns as performance picks-up.
- **Scale and liquidity** – with shares often tightly held by long-term investors, securing holdings of an appropriate size can be problematic.
- **Future prospects** – ultimately potential investors are trying to divine the relative prospects of these different businesses, which will include the factors set out above, as well as potentially 'looking under the hood' to assess the key underlying portfolio companies and their individual prospects.

Companies that appear to have relatively stronger future prospects than track record (eg IP Group and Mercia) still seem to suffer from an accentuated discount to NAV, whereas companies such as Frontier IP and Augmentum Fintech, with a shorter track record and limited liquidity, trade at a much narrower discount. HgCapital Trust is the bellwether in the sector, with Molten the pick of the VCs, due to their scale, track record and respective market positions. Having traded at a significant premium to NAV pre-2022, TMT is currently suffering from a widened discount due to its exposure to i) US technology valuations, and ii) Eastern Europe, but its track record is second to none. Although OCI has a relatively strong track record, its discount to NAV remains consistently wider than HgCapital Trust, its closest peer. With continued performance, increasing scale and strong governance, we would expect this discount to close over time.

Alternative approaches to valuation

Managements often argue for alternative valuation measures. Companies that own a fund management company, and therefore receive management fees (eg Mercia, Molten, IP Group) could expect to receive additional recognition once management fees offset central costs, making the business structurally profitable (eg Mercia). As net fees scale, the business can increasingly be viewed as an alternative asset manager, valued on the basis of a predictable earnings stream. Alternatively, HgCapital Trust argues that it is in effect one of the largest European software conglomerates, with the business compared to large quoted European technology companies and valued on the basis of EV/Sales and EV/EBITDA multiples (HgCapital Trust: FY21 portfolio revenues of £6.3bn, EBITDA of £2.2bn, 35% EBITDA margin).

Either way, management teams do not believe that this high-growth sector should be valued simply on the basis of a discount to NAV per share. This thinking is captured by a recent article in *Investment Week* by Steven Tredget from Oakley Capital, If you're focused on the discount, you'll miss the story.

Company profiles (*Edison client)

Augmentum Fintech (AUGM)
European fintech VC

Augmentum aims to generate capital growth over the long term through investing in fast growing and high-potential financial services technology businesses based predominantly in the UK and continental Europe. RIT Capital Partners was a cornerstone investor in the launch of Augmentum in 2018, which raised £94m at IPO. Augmentum last raised £55m by way of a placing and open offer at 135.5p per share in July 2021, with net assets of £267.3m at 30 September 2021.

The company aims to make early or later-stage investments in unquoted fintech businesses, mainly within the UK and Europe and can continue to own investments if they list. Currently the portfolio constitutes investments in 24 companies, loosely grouped into digital banking and lending, wealth and asset management, infrastructure, digital assets, circular economy and proptech.

Frontier IP (FIPP)
Equity for commercialisation services

Frontier IP works with universities, research institutes and academics to identify IP that can be commercialised. Rather than buying equity stakes, Frontier IP earns equity in private technology companies in return for providing IP commercialisation and support services, ranging from ensuring the business mechanics run smoothly to direct, hands-on support for technology development. The group's portfolio includes 17 investments, with equity holdings in four technology clusters: artificial intelligence, robotics and big and sparse data; pathogens and cell imaging; food and agritech; and engineered particles and materials. As of 31 December 2021, Frontier IP had net assets of £46.6m.

HgCapital Trust* (HGT)
Europe's leading software/SaaS investor

HgCapital Trust (the quoted vehicle) provides liquid exposure to Hg's (the fund manager's) portfolio of unquoted software and services businesses, typically providing financial solutions to local or regional SMEs. Hg predominantly seeks controlling interests in businesses headquartered in Europe (weighted towards northern Europe) and North America, although often with an international customer base.

As a PE investor, Hg invests in larger, later-stage businesses with an established client base and revenue model, which is EBITDA positive (pre-investment). This allows HgCapital Trust to achieve diversification across markets and geographies, gaining exposure to fast growing portfolio companies at different stages of their development and size, from an enterprise value (EV) of £100m to over £10bn. The investment team provides active, hands-on management as portfolio companies undergo rapid development. Hg's strategy is to invest in cloud-delivery as part of a transformation from a licensed model to a SaaS model, with operational improvements supported by an active M&A strategy.

HgCapital Trust has a portfolio of more than 40 private software and business services companies with resilient, recurring revenue streams. The group actively leverages Hg's network and sector expertise to support portfolio company management teams. The top 20 businesses (78% by value) reported aggregate sales of £6.3bn and EBITDA of £2.2bn in FY21, a 35% EBITDA margin. The top 20 companies represent c 80% of NAV, which stood at £1.98bn as at 31 March 2022.

IP Group* (IPO)
University IP and thematic investor, with a focus on ESG

As the 'father' of IP commercialisation, IP Group was founded in 2001 to commercialise ideas from partner universities into businesses, by helping to create, build and support IP-based companies. However, IP Group's model has evolved to become more thematic, with a particular focus on ESG investment. IP Group invests primarily in the life sciences, deep tech and renewable sectors but is increasingly focused on companies with products and services that meaningfully contribute to sustainable, healthier and tech-enriched futures. The group has invested in three unicorns to date (Oxford Nanopore, Ceres Power and Hinge Health) and its ambition is to create at least one category-leading business valued at more than US$10bn within the next five years.

IP Group's five-year NAV per share track record was disrupted by the acquisition of Touchstone Innovations in 2017, by way of a share exchange. IP Group has delivered a NAV per share CAGR of c 11% since its IPO in 2003 and a NAV per share CAGR of 24% over the last two years.

FY21 hard NAV stood at £1.7bn, comprising a core of 20 companies amongst a total portfolio of 100 companies. With net cash of £270m as at 31 December 2021, IP Group remains well capitalised to support its portfolio (which raised c £2bn in FY21) and to invest for the future. IP Group also manages c £540m in third-party capital across its Parkwalk, UK [David should this be US rather than UK?] and Australian businesses, with Parkwalk's AUM increasing to £388m.

Mercia Asset Management* (MERC)
A specialist asset manager for the UK regions

Mercia was founded in 2010, after a buyout of WM Enterprise, before listing on AIM in December 2014. Mercia is a specialist asset manager with a stated intent to become the leading UK regional provider of balance sheet, venture, PE and debt capital in transaction sizes typically below £10m. Mercia targets businesses in its regional markets (in England, the North, Northeast, Northwest, Midlands and Scotland) with relatively modest capital needs, typically up to c £20m in total, across multiple rounds.

Mercia offers a blended investment model, with net fee income from its third-party managed funds (FUM of £762m as at 30 September 2021) meaning the group is structurally profitable and able to commit to a progressive dividend policy. Mercia's portfolio of direct balance sheet investments is now mature, with the group having achieved multiple exits. In Q122, it exited its second largest holding (Faradion), as well as concluding a significant third-party investment round for nDreams, its largest holding.

It is worth recognising that Mercia's five-year NAV per share track record has been disrupted by the acquisition of the Northern VCT fund management business in December 2019, when the company placed shares at a discount to NAV to part fund the acquisition. As better indicators of the group's potential until it grows into its five-year CAGR, Mercia has delivered a direct investment portfolio IRR of 14% from its IPO in 2014 to 30 September 2021 and a NAV per share CAGR of 24% over the last two years.

As the only company in our review with a sufficiently large third-party fund management business to generate fee revenue in excess of central costs, we believe that Mercia's fund management business should attract an uplift to NAV. The incremental value of this business should increase further as FUM scales and fee income increases. The portfolio currently comprises 20 investments, although this is likely to expand to 25–30 holdings over the next few years. The group reported FY22 NAV of £186m as at 30 September 2021.

Molten Ventures* (GROW)
A leading European VC

Molten is a VC company dual-listed on the main market of the London Stock Exchange (FTSE 250) and on Euronext Dublin. Founded in 2006 as Esprit Capital, the company was renamed Draper Esprit in 2015, ahead of its IPO in 2016. Management changed the firm's name to Molten Ventures in November 2021. Molten is one of the leading European VCs, competing with private LLPs such as Accel Partners, Balderton Capital, Index Ventures, Northzone and Partech Partners.

Molten's core focus is on Series A and Series B+ funding for leading European start-ups from its own balance sheet, investing in four sectors (enterprise, consumer, hardware and deeptech, digital health and wellness), with the majority of capital targeted at later-stage rounds. As well as investing off its balance sheet, the group includes other investment vehicles, including tax-advantaged EIS and VCT funds, as well as a strategic investment in Earlybird Digital, a German seed and Series A investor. Molten has also implemented a fund-of-funds strategy, through which it has invested in 47 specialist seed funds across the UK and Europe (as at 30 September 2021) since its launch in 2017. To our knowledge, this strategy and its scale are unique.

Molten has a core portfolio of c 17 companies, amongst a total portfolio of 72 companies. Net assets stood at £1.42bn as at 31 March 2022.

Oakley Capital Investments (OCI)
'Founder-led' European PE investor

The fund manager, Oakley Capital, was founded in 2002 and subsequently the investment company, OCI, listed on AIM in 2007, with a remit to invest in the funds managed by Oakley Capital. It is now listed on the specialist fund segment of the main market, with a stated intention to move to a premium listing on the main market in the next few years. Oakley Capital's private equity funds invest in founder-led businesses across Europe in three core sectors: technology, consumer and education. Within these sectors, Oakley Capital targets subsectors and businesses with structural growth opportunities, driven by trends including: the acceleration of e-commerce; cloud-delivery of services; and global demand for quality education and e-learning. Tech-enabled businesses not only enjoy economies of scale but can also access new markets and typically benefit from faster growth and improved downside resilience.

Oakley Capital is also differentiated through its network of entrepreneurs – these individuals support origination and, in aggregate, have committed over €400m to Oakley Capital funds. Oakley Capital has now backed some of its serial entrepreneurs three or four times. Oakley Capital argues that its entrepreneurial heritage makes it the partner of choice for business founders, helping it

secure exclusive dealflow and avoid auctions. It is usually the first institutional investor in a business.

OCI provides access to 22 investee companies managed by Oakley Capital, the majority of which (although not all, eg Time Out, North Sails) deliver their products or services digitally, with 75% of the portfolio having subscription-based or recurring revenues. As of 31 March 2022, net assets stood at £1.02bn.

TMT Investments (TMT)
VC providing an Eastern Europe/US bridge

Founded and listed on AIM in 2010, TMT is focused on earlier-stage technology companies, typically at pre-Series A and Series A stages. However, TMT's current NAV is heavily weighted towards three large and globally established companies: Bolt, Backblaze and PandaDoc, which represent approximately two-thirds of TMT's total portfolio value. The remainder of the portfolio is diversified, with c 50 early and mid-stage companies across the big data/cloud, e-commerce, marketplace, EdTech, FinTech, SaaS and FoodTech segments.

TMT invests in high-growth technology companies with global scale-up ambitions. The group has no restrictions on where it can invest, with significant exposure to US-based tech start-ups. However, a number of smaller investee companies, whose founders originate from the former Soviet Union, have revenue exposure to Russia and Ukraine. In this light, the group identified eight of its earlier-stage portfolio companies that are expected to be negatively affected by the war in Ukraine, with an estimated US$5m impact on NAV. TMT had net assets of US$283m as at 31 December 2021.

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