

oxford
technology

Combined Seed Enterprise Investment and Enterprise Investment Scheme Fund

OT(S)EIS – The Start-up Fund

The case for investing in OT(S)EIS - April 2019

Oxford Technology has specialised in investing in start-up science businesses in and around Oxford for more than 20 years. We enjoy the process of helping to create successful science businesses and we believe that we are good at it. We are based in the Oxford Science Park. All our investment managers are scientists or engineers. Almost all our investments are within an hour's drive so that we can be actively involved with our investees to help them get started.

Investing in start-up science businesses is extremely risky. There are so many things which can and do go wrong. But the other side of the coin is that when new science businesses go well, the gains can be very large. So this is a high risk/high reward activity, not suited for everyone.

In 2012 the Government introduced the SEIS scheme. This scheme offers huge tax benefits to those who are prepared to take the risks of investing in start-ups. The reliefs include 50% income tax relief at the start, capital gains tax write-offs and further loss reliefs if the business fails. All gains are tax free. Also, the investments are outside Inheritance Tax after 2 years, so this is a good way of passing money on to the next generation without tax.

The SEIS scheme transforms the economics of investing in science start-ups. Essentially, the losses on the failures are hugely reduced (in some cases to as little as 12.5% of the original investment) while the gains on the winners are tax free. The maths says that it should work.

So in 2012 we started a fund - the Oxford Technology Combined SEIS and EIS Fund - OT(S)EIS. The fund is open for investment at any time (min £15,000). Our aim is to invest 1/3 of whatever is invested in year 1 in 5 or 6 SEIS start-ups, and then to invest 1/3 in follow-on EIS investments in year 2 in those of the earlier SEIS investments which are showing promise and then the same again in year 3. Although this means that it takes up to 4 years for investors to get their full tax relief and also that the total income tax relief is about 36%, being a mixture of 50% SEIS and 30% EIS, we believe that the benefits of having the money in the bank to be able to make follow-on investments will result in a much better outcome for investors. We have learnt from experience that it is vital to be able to support start-up companies with additional investment, and that not to be able to do this often results in a bad outcome for the early shareholders.

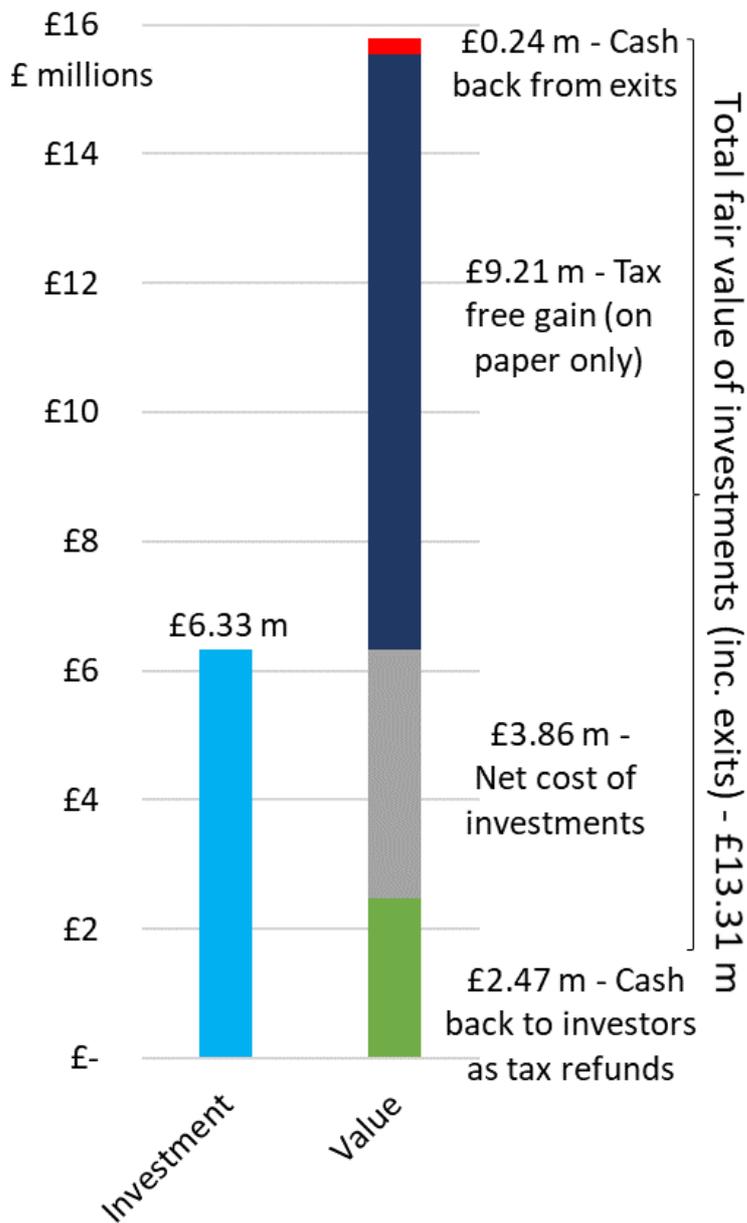
OT(S)EIS made its first investment in December 2012.

The figures for the fund to April 2019 are:

Total invested to date:	£6.33m
No of companies:	39
Tax refunds to investors:	£2.47m
Net cost of investments:	£3.86m
Cash back from exits	£0.24m
Value of investments (1):	£13.31m
Tax free gain (on paper only so far):	£9.21m

(1) Investments are either written down in value if they are not meeting their business plans, or they are valued at the latest share price paid by incoming investors. Even if they are doing well, we do not change the valuation until capital is raised at a higher share price. To this extent, the valuations are conservative.

This table is shown graphically below:



The Details

Of the 39 investments, the ten which are showing the greatest returns so far (mainly on paper only so far) are the following:

	Company	Current value of OT(S)EIS holding / Net cost to OT(S)EIS	Current share price /After tax share price of initial investment
1	Expend	1,912%	4,000%
2	Oxford Nanoimaging	1,734%	1,734%
3	Polycat UK	686%	900%
4	Lightpoint Medical	640%	2,783%
5	Animal Dynamics	582%	1,386%
6	Electrowinning Technologies	533%	1,000%
7	Run 3D	508%	600%
8	Molecular Warehouse	398%	667%
9	Ducentis Biotherapeutics	366%	1,000%
10	Designer Carbon Materials	333%	333%

Brief details of the first five of these companies are given below to give a flavour of the kind of things we invest in.

1. Expend

Initial SEIS investment	£75,000
Date of investment	23/12/2014
Share price	£0.0050
After tax share price	£0.0025
Latest share price	£0.10
Multiple	40

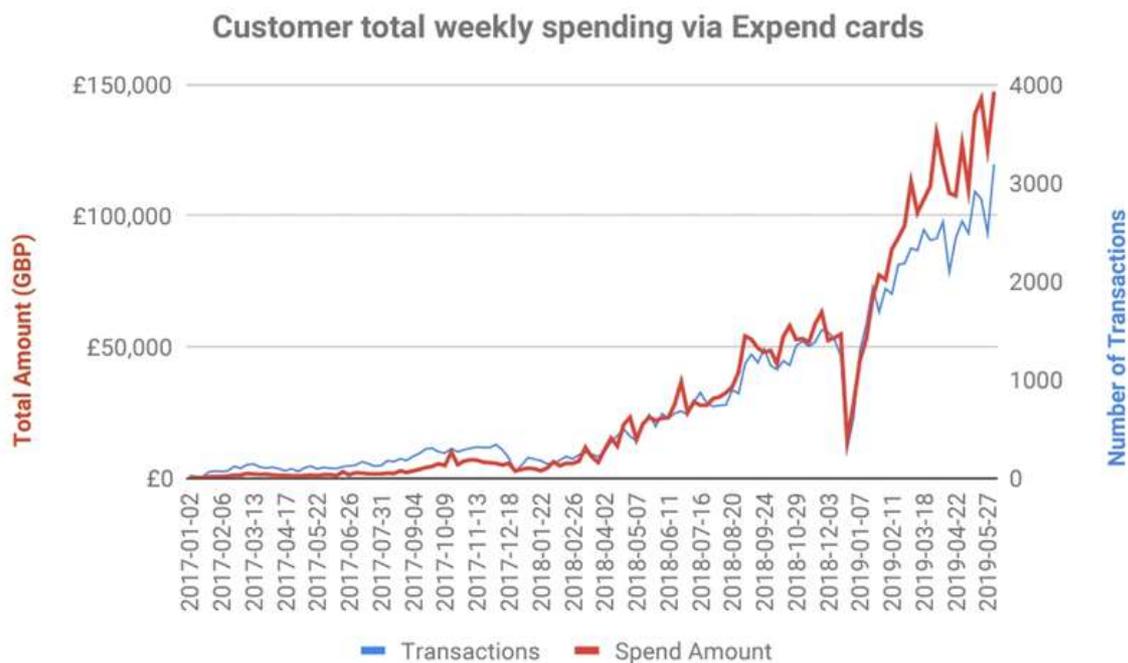
NB. OT(S)EIS made follow-on EIS investments in Expend of £17,131 at £0.06 per share in Feb 2017 and £3,000 at 16p per share in Dec 2017, which results in an overall multiple of 19, as shown in the left hand column of the table above.

Expend is seeking to tackle the problem of expenses. In many companies, this is a monthly headache. Often employees have to use their own cards, keep receipts, make a list of the expenses at the end of each month, together with the receipts, get these approved by their manager, and then wait to be paid. Using the Expend system (which can use either a special Expend Card or a normal card) the expenditure goes into the company's accounting system as soon as the expenditure is incurred, and the user receives an instantaneous message on her phone saying "please photograph the receipt". This too is captured by the accounting system, and that is the end of the paperwork.

The initial investment enabled the two founders to leave their jobs to concentrate on Expend. Expend subsequently raised additional capital to fund expansion.

Sales are now rising rapidly, and major banks are showing interest in promoting Expend to their customers. In one case study, a company found that the time spent on doing their monthly expenses had reduced from 1 day to 20 minutes.

Expend is not yet at breakeven and risks remain, but the company has come a long way and is making excellent progress.



2. Oxford Nanoimaging

Initial SEIS investment	£100,000
Date of investment	29/04/2016
Share price	£20
After tax share price	£10
Latest share price	£173
Multiple	17

Oxford Nanoimaging is a spin-out from the biological physics lab of Oxford University. The purpose of the investment was to manufacture and market a super-resolution microscope, which enables scientists to see and understand certain biological processes which could not be seen by other means.

The company has now grown from 5 people at the start to 98 and raised \$25m at £173.40 per share in Q2 2018 to fund its expansion. Investors came from the US, China, Singapore and London.

3. Polycat

Initial SEIS investment	£50,000
Date of investment	05/10/2018
Share price	£28.33
After tax share price	£14.17
Latest share price	£127.50
Multiple	7

NB. In March 2019 OT(S)EIS invested a further £22,000 at £127.50, part of a round of £85,000.

PolyCat has developed an economic, scalable process to produce metal nanoparticle catalysts on polymer substrates. This allows catalysts such as platinum, palladium, cerium, iron and silver to be combined with the benefits of polymers such as flexibility, toughness, resistance to chemical attack and high surface area.

There are two initial areas of application. The first is for the destruction of chemical weapons which currently pose a big problem when found in the field. The second is for the preservation

of fruit. Trials with a major fruit distributor in which a Polycat disc is placed in a fruit container have demonstrated a three-day extension in shelf life of the fruit. This is of potentially very large commercial value. Fruit worth £ms per year is currently wasted since it rots before it can be sold.

4. Lightpoint Medical

Initial SEIS investment	£75,000
Date of investment	04/06/2013
Share price	£0.047
After tax share price	£0.0235
Latest share price	£0.65
Multiple	27

NB. OT(S)EIS also made the following investments in Lightpoint:

Date	Amount	Share price (before tax relief)	Type
10/03/2014	£75,000	£0.190	EIS
07/11/2014	£10,000	£0.238	EIS
04/12/2014	£125,000	£0.238	EIS
10/03/2016	£100,000	£0.509	EIS
24/03/2014	£20,000	£0.509	EIS
27/03/2019	£27,000	£0.650	EIS

OT(S)EIS was the first external investor in Lightpoint, whose objective is to enable surgeons to be able to see which tissue is cancerous and which is not, during an operation. Before Lightpoint, surgeons had to operate blind - cancerous tissue looks the same as non-cancerous tissue. Patients take a standard (used for 30 years and medically approved) radio-labelled sugar which concentrates in cancer cells. Lightpoint's novel imaging modality then enables surgeons to see which cancer is cancerous and which is not. The first application was in breast cancer surgery, where c.20% of operations have to be repeated (at great financial and emotional cost) because not all the cancerous tissue is excised in the first operation. The second area of use of Lightpoint systems is in prostate surgery. Here the consequences of cutting out too much are dire for the patient. But if the growth is cancerous then it is necessary to cut it out, Lightpoint enables surgeons to know whether to cut or not. Without Lightpoint, they have to guess.

Lightpoint has won numerous awards and numerous grants (more than £10m since we first invested including from the US government), and 'Lightpath' systems are now in daily use in multiple sites in the UK, US and Europe.

5. Animal Dynamics

Initial SEIS investment	£75,000
Date of investment	29/06/2015
Share price	£0.14
After tax share price	£0.07
Latest share price	£0.97
Multiple	14

NB. OT(S)EIS also invested £35,000 at 36p per share in Nov 2017, and £3,000 at 97p per share in July 2018.

Animal Dynamics is a spin out from the Animal Flight Group at Oxford University which studies the way birds and insects fly, and the way fish swim, and seeks to use this knowledge to design better flying machines and better propulsion systems for ships.

The company has been a great success from the start and won a large research contract to design a flapping drone, based on a dragonfly. This development is ongoing, and controlled flight has been achieved. At the 2018 Farnborough Air show, a contract was announced for Animal Dynamics to supply flying machines which will allow large loads (eventually up to 3.5 tons) to be flown autonomously to GPS coordinates. The application is to supply front-line troops. There is also an obvious case for such a vehicle in disaster relief applications where the transport infrastructure has been destroyed.

Animal Dynamics' main problem has been to recruit enough sufficiently qualified engineers and to find new premises to accommodate the rapidly growing staff.

In July 2018, Animal Dynamics raised £6m at 97p per share to fund expansion and the production of the order. The issue was oversubscribed. Animal Dynamics asked that early shareholders offer some or all of their shares for sale (at 97p) so that they could accommodate the desire of some other investors to become shareholders. So this enabled those who chose to do so to exit at 14x the after tax share price of their initial investment. About half opted to do this while the other half opted to stay for the ride.

Failures

Since its inception in 2012, OT(S)EIS has made SEIS investments in 39 start-up companies and then supported those investees who were showing promise with a further 87 mainly EIS investments.

So far there have been three failures. But the combined after tax losses on these failures are only £45,900. This compares with gains (on paper only so far) of £9.21m on those that have gone well. The reason the losses are so small are two-fold.

1. We make small initial investments and then work with the founders (at least one meeting with the management per month, and sometimes much more - almost all the investees are within a hour's drive), so that we get to know the companies and their managements very well, warts and all. If we think there are fatal flaws, we don't invest more.

2. The huge tax reliefs associated with both the SEIS and EIS schemes include 'loss relief' which means that the losses on the failures result in a tax refund to the investor. So this reduces the cash loss on the failures.

Financial Returns to Investors

There has been one exit so far, which generated £240,000 for investors, so the major returns to investors so far have been the tax reliefs, which total £2.47m to date.

The returns to each investor are different since investors get their share of the next crop of investments which are made in the months following their investment. I myself have invested in the fund six times so I have shares in almost all of the investments (I missed out on one of them).

Below is my own financial summary report for my own first investment in the fund. This is as much so that you can see the information contained in the report and the format, as for the numbers.

Financial Summary Report		Lucius	Cary	12/06/2019			
Subscription Number	1	Date of Subscription	06/06/2012	Subscription	£50,000.00	Fund	OTSEIS
Where the money has been spent		Exits		Value of Funds			
Net Commission		Proceeds from Exits	£3,463.87	Total Fair Value of Investments	£110,364.10		
Initial Fees	£500.00	Paid Accrued Management Fee	£2,437.50	Tax Break Return	£18,398.58		
Funds Invested in SEIS	£23,872.03						
Funds Invested in EIS	£21,541.88	Settlement of Investment Roundings	£72.55	Total Cash Back from Exits	£1,079.59		
Funds Invested in Non SEIS/EIS							
Custodian Fee (7 years)	£1,013.54			Remaining to Invest	£0.00		
Management Fees (first 3 years)	£3,000.00			Accrued Management Fee still to be paid	£250.00		
Remaining to Invest	£0.00			Performance Fee	£13,918.45		
Settlement of Investment Roundings	£72.55						
Total of Above	£50,000.00	Total Cash Back from Exits	£1,079.59	Total Return (tax free) after payment of all fees - on paper only until there are exits.	£115,673.81		
Tax Break Return	£18,398.58						
Net Cost of Investment	£31,601.42						

This subscription is more than 3 years old so we have invested your whole subscription. If you would like a share of our new Investments, please make a new subscription.

NB A management fee of 2% is charged for the first three years. Thereafter no further management fees are paid out of the fund, but a fee of 1.5% pa is accrued in years 4-7. This will be paid out of the proceeds of exits if and when these occur. If there are no exits the fees will not be paid. The cum accrued management fee is shown on the right. After year 7, there are no more fees.

The Custodian Fee is the total custodian fee that will be collected over 7 years. If "Remaining to Invest" is negative we have over-invested for you and we will recover the balance from exits. Performance fee: After investors have received back £1.20 including income tax breaks only (assumed to be for a 40% taxpayer) for each £1 invested, Oxford Technology Management will receive a 20% share of all further distributions

I invested £50,000 on 6 June 2012. £23,872 of this was invested in SEIS investments and £21,514 in EIS investments, so £45,386 in total. The balance of the £50,000 was fees. I have so far received £18,398 back in tax refunds, so that my net investment in the fund is now £31,601. I have also received £1,079 from exits. The value of the remaining investments, valued by the latest share price paid by an incoming investor, is now £110,364. The total return, after all fees is £115,673.81.

Below is a summary of my investments in OT(S)EIS:

Investment	Date	Amount Invested so far (inc fees)	Still to be invested	Cash back in Tax Reliefs	Net at Risk	Cash from exits	Value of Investment	Total return after all fees
£50k	Jun 12	£50k	£0	£18.4k	£31.6k	£1.0k	£110.3k	£115.7k
£25k	Nov 13	£25k	£0	£9.3k	£15.7k	£2.6k	£69.4k	£71.0k
£30k	Jan 15	£30k	£0	£10.8k	£19.2k	£14.1k	£59.7k	£74.8k
£50k	Feb 17	£31.5k	£18.5k	£11.6k	£38.4k		£38.1k	£66.6k
£40k	Feb 18	£22.0k	£18.0k	£8.5k	£31.5k		£25.0k	£50.9k

So the returns on the investments in the fund which were made more than 3 years ago and which have been fully invested have been good and I hope will get better as the companies in my portfolio grow and increase in value. The most recent two investments in the fund have not yet been fully invested and there hasn't been enough time for the valuation of these investments to change very much yet - as one would expect. The only return so far has been in the form of a reduced tax bill. I have also made a sixth investment in the fund in May 2019, but no investments have yet been made from this.

Summary

The fund has so far shown a very good return for almost everyone who has invested, regardless of when they invested. Most of this gain is on paper at this stage.

Of course we cannot guarantee that future returns will be as good as the returns so far, but it would appear that the investment strategy has worked just as we hoped and expected, and we hope and expect that it will continue to work just as well in future.

Direct Investments

In almost all cases, if the start-up companies develop well, they raise additional capital. When they do this, our normal practice is to agree to invest more ourselves from OT(S)EIS, but then also offer our investors in OT(S)EIS to make direct further EIS investments in the companies on the same terms and at the same share price at which OT(S)EIS is investing. The investors can also meet the management. Some investors really like this feature of OT(S)EIS and make many such direct investments in addition to their investments through OT(S)EIS. In a few cases such investors have become involved as directors of the investee companies, if they have special skills or knowledge which is helpful to the company concerned.

Please call or email if you have any questions.

Lucius Cary
 0772 0060824
lucius@oxfordtechnology.com

The Information Memorandum and Application Pack for OT(S)EIS are available to download at www.oxfordtechnology.com

April 2019