

# Chairman's Statement



**Gillian Nott** Chairman

The year to 30 September 2009 has been a year of two halves. The value of the unquoted portfolio has remained steady whereas the loss in AIM values in the first half has almost been exactly reversed in the second half. In a year of such extreme volatility in financial markets, the end result is of little change to NAV per share demonstrating the benefits from good diversity across the portfolio and the active management style of the Managers.

I am delighted to welcome Peter Lawrence as the third Chairman of Baronsmead VCT on my retirement at the Company's 14th AGM. Over the last 10 years the Company's performance has consistently been top quartile. In addition, your Company has reached a milestone with the proposed final dividend of 3.5p taking cumulative dividends to over 100p per share, more than the original 100p subscribed by founders in 1995 and, an annual average of 7.2p. The Company has grown substantially over the period with the number of companies in the portfolio having more than doubled and shareholders funds have risen from £22.2m to £54.8m. I believe the Company is well positioned to take advantage of improving market conditions.

## INVESTMENT PERFORMANCE

In the twelve months to 30 September 2009, the Net Asset Value (NAV) per share increased by 0.4% per cent from 75.72p to 76.04p before payment of the 2.5p interim dividend and proposed 3.5p final dividend. These dividends comprise of 0.7p per share of net revenue and 5.3p per share of realised capital profits largely accumulated in previous years. It is pleasing to report that just after the year end ScriptSwitch was sold to UnitedHealth UK for 3.8 times cost equivalent to around 4.0p per share, confirming the underlying value in the portfolio.

The flat NAV per share year on year is made up of a 1.9% advance from the unquoted portfolio and a reduction in the AIM portion by 0.8%. The latter masks a fall of 26% to 31 March 2009, subsequently made up by a gain in the second six months. The FTSE All-Share Index increased 6.1% over the same 12 month period.

At the period end, over 70% of the ordinary capital raised (net of launch costs) prior to 30 September 2007 was invested in VCT qualifying investments and the 5 other VCT qualifying tests had also been met.

## Long term performance

The Company's Investment Objective emphasises the longer term performance of the Company, consistent with shareholders' actual and stated anticipated holding periods. As a result, the Board reviews the long term performance of the Company using a number of different metrics, namely total dividends paid to shareholders and Share Price and NAV total returns.

The proposed final dividend will take the cumulative dividends paid (tax free to qualifying shareholders) for founder shareholders to 100.05p per share, slightly more than their original £1 investment on which income and capital gain tax reliefs were available to qualifying

Shareholders. This is an average annual dividend throughout the 14 year period of 7.2p per year.

There have been five prospectus fund raisings by Baronsmead VCT. All shareholders from these prior offers have to date achieved positive absolute total returns. The ten year performance to 30 September 2009 currently places Baronsmead VCT as one of the leading VCTs. Fuller comparisons have recently been facilitated by the Association of Investment Companies (AIC) who publish monthly data on their website, [www.theaic.co.uk](http://www.theaic.co.uk).

The returns to shareholders are enhanced by the tax benefits available to VCT investors. At a time of lower and sometimes negative investment returns, the proportional benefit from these reliefs is greater.

## ANALYSIS OF THE PORTFOLIO

### Portfolio valuation

The valuation guidelines for unquoted companies have been revised by the International Private Equity and Venture Capital Valuation Board to facilitate compliance with International, US and UK accounting standards. When valuing the unquoted portfolio the Board uses a significant amount of information available to arrive at appropriate valuations. This includes the valuation of recent transactions and the earnings multiples for comparable quoted companies and FTSE sectors, all suitably adjusted for size, liquidity, gearing, growth prospects and business mix. AIM investments continue to be valued at bid price.

Following the sale of four AIM investments, the transfer of two small AIM holdings to the Wood Street Microcap Investment Fund and the write off of another ten investments, which includes one unquoted company, the total portfolio now comprises 51 AIM & Listed companies

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and 20 unquoted. By value, 49 per cent of the NAV of £54.8m was invested in unquoted companies, 21 per cent in AIM & Listed investees and the balance of 30 per cent remained in cash or interest bearing securities. The largest two investments in Reed & Mackay and ScriptSwitch each represent 5.4% of Net Asset Value.

## Unquoted portfolio

The performance of the unquoted portfolio has been robust and its collective valuation has been sustained. This validates the quality of the portfolio and the effectiveness of close cooperation with the investee companies.

On average, the current portfolio of unquoted investments is valued at some 33 per cent higher than original cost. Fifteen companies are valued at a level greater than cost and five are valued below cost, with three of these having a provision against cost of more than 25 per cent.

## AIM-traded portfolio

The AIM portion of the portfolio has bounced back 36% since 31 March 2009 almost recovering the loss in the first six months. Three of the investee companies were sold outright also in the second half indicating that acquirers appreciated that good value resided in these relatively lowly rated situations. This supports the longer term strategy of taking more influential stakes in a smaller number of AIM investments, where a likely exit strategy to a trade buyer can be envisaged.

## Collective Investment Vehicle

£525,000 of cash and small shareholdings in two AIM-traded companies were transferred into the Wood Street Microcap Investment fund in June 2009. This fund, managed by ISIS at no additional cost to the Company, will largely invest in UK non-qualifying AIM and SmallCap companies in order to provide additional diversity in the portfolio and take advantage of attractive but non qualifying opportunities.

## Prospects for new investment

The market for investing in new unquoted transactions has been relatively depressed over the last 12 months with overall M&A volumes significantly down. Four follow on investments were completed during the year under review but no new unquoted investments were made. The quality of investment proposals is now improving as confidence begins to return to the market and the manager is in discussion with a number of companies and hopes to make several investments at advantageous prices. In addition the Manager has an active programme of directly approaching prospective investee companies in selected sectors, and this is building a strong pipeline of entrepreneurs that would like to work with the Manager when the timing is right.

The poor stock market conditions in 2008 and in early 2009 were particularly difficult for companies in our AIM portfolio and the flow of qualifying AIM opportunities was limited. These conditions have now improved substantially. Recent research recognises the importance of AIM as a funding stage for venture backed and entrepreneurial companies, particularly in an environment with lower debt availability. AIM companies typically have no or low levels of gearing and we expect improving prospects in this part of the portfolio.

## SHAREHOLDER ISSUES

### Fund raising

The joint offer with Baronsmead VCT 2 was reported at the interim stage raising net proceeds of £8.4m for each VCT. After the proposed final dividend is paid, the cash resources remain at a good level for investing into the anticipated upswing and yet retain sufficient flexibility to meet any requirements for the existing portfolio, buy backs and future dividends.

### Buy backs

During the 12 months to 30 September 2009, 1.11 million shares were bought back (2008: 1.71 million). The average discount to NAV was 10 per cent and compares well to the rest of the VCT sector where discounts to NAV were generally much wider.

### VAT reclaim on management fees

Following the successful reclaim of VAT as detailed in my statement last year further VAT was recovered in the current financial year. Together with interest this amounted to £0.4m and this has been reflected in the financial statements.

### Company brokers

The Company's former broker, Teathers, ceased to operate as a market maker during March 2009. However, several other firms became market makers during that month thereby minimising the impact this could have had on the discount to NAV at which the Company's shares were traded. Currently the Company's shares have three market makers, namely Matrix Corporate Capital, Winterflood and Singer Capital Markets. Following a review of brokers the Board agreed to appoint Matrix Corporate Capital as the new broker to the Company from the beginning of August 2009.

### Finance Act 2009

In the April 2009 Budget there were only minor changes to the VCT rules and regulations. However, the Finance Act 2009 set out the proposed 50 per cent income tax rate and restriction of tax relief on pension contributions. This means

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the tax relief on VCT investments and the tax free dividends paid by VCTs will become more valuable. Again it is important to stress the need to consult professional advisers regarding such planning and personal investment.

Additionally, your Board believes it will be important to demonstrate the positive benefit of VCT tax concessions to the UK economy. We shall seek to measure the increased employment and consequent increase in tax revenue to the Treasury by investee companies that have benefited from our investment. For example the ten largest investee companies have on average increased the number of employees by over 50 per cent during the first 3 years following our investment.

## Proposed Final Dividend

A dividend of 3.5p will be proposed at the forthcoming AGM and, if approved, will be paid on 30 December 2009 to shareholders recorded on the register on 27 November 2009. The ex-dividend date is 25 November 2009. For those shareholders in the Dividend Reinvestment Plan (DRIP) we remind them that shares purchased by the scheme are existing shares and as such are not eligible for tax relief on subscription.

## BOARD SUCCESSION

Last year I alerted shareholders to the need for changes to the Board as the current Board has been in place for almost ten years. It is very pleasing that Peter Lawrence has accepted the Board's invitation to take on the Chairman's role. He is an experienced Chairman who has built up his own company that was recognised in 2003 when he won the AIM Entrepreneur of the year. He became a director of Baronsmead VCT in 1999 and has also been Chairman of Baronsmead AIM VCT since its launch in 2006.

I became chairman in early 1999 on the death of the first Chairman, Sir William Stuttaford. It is rewarding for me to see the progress of Baronsmead VCT over this period. Our ten year total return performance places us among the top three VCTs in the sector and compares very favourably against larger investment trusts in Private Equity. Much of this return is as a result from the profitable sale of investments which has enabled the distribution of net capital realisations amounting to 70p per share (out of the 100.5p total paid out) over this period. This performance is testament to sticking to our investment policies through two major market reversals, notably the bursting of the technology bubble and now the current global financial crisis.

This has been achieved in part because of a strong focus on risk management which leads the Board to believe that we are lower risk than many other VCTs. Good diversity in the portfolio has been paramount as the present portfolio is still

double in number that of 1999 despite the high level of disposals in recent years. The largest three investments then represented almost 25% of the NAV compared to some 15% now. We have also had successive open offers so that Baronsmead VCT is one of the largest VCTs and has given shareholders choice whether they wish to subscribe, buy, hold or sell.

Shareholder communication and dialogue has always been high on the Board's agenda, greatly helped by shareholder feedback as to their priorities in response to our shareholder surveys and at Annual General Meetings. Our consistent commitment to a buyback policy has provided shareholders with liquidity when they need it and we have enabled choice via a dividend reinvestment scheme.

I am delighted to welcome Valerie Marshall to the Board, which she joined on 12 November 2009. She has wide experience of private equity at 3i and the Scottish Development Agency prior to specialising in corporate finance. She currently holds a number of directorships that are set out on page 16 of this annual report.

I look forward to meeting as many shareholders as possible at our fourteenth Annual General Meeting on the Monday, 14 December 2009 to be held at the London Stock Exchange, 10 Paternoster Square near St Paul's Cathedral. The AGM will be preceded by presentations from the Manager, an investee company and a light lunch commencing at 11.45 am, the AGM will start at 1.15 pm and be followed by a shareholders workshop.

## OUTLOOK

We are very concerned by the proposed European Union Alternative Investment Fund Managers Directive and its impact on the Company and the Manager. It is too early to tell how significant the impact of these measures will be to the way your Company functions, but we are alert to the issues and will comment further on this Directive as its implications become more apparent.

On a more positive note equity markets have rallied in recent months anticipating that the pace of decline in the UK economy over the past 12 months has slowed and is perhaps stabilising. The Board and Manager share the belief that once confidence has returned to UK financial and industrial markets our Company is well placed to capitalise on a potentially more favourable investment environment.

**Gillian Nott**  
Chairman

16 November 2009