Nottinghamshire County Council

**Report to Pensions Sub-Committee**

**13 December 2012**

**Agenda Item:**

# REPORT OF SERVICE DIRECTOR – FINANCE & PROCUREMENT

# NOTTINGHAM & NOTTINGHAMSHIRE INVESTMENT FUND

## Purpose of the Report

1. To report on discussions at the Pensions Working Party on progress in establishing a venture capital fund to invest in Nottingham and Nottinghamshire and to seek agreement to a recommendation to commit £10 million to the fund once established.

## Information and Advice

2. Nottingham City and Nottinghamshire County Councils have been working together on a proposal to create a venture capital fund to invest in small and medium sized enterprises (SMEs) within Nottingham and Nottinghamshire with the aim of making commercial returns for investors. The original proposal was jointly to procure a fund manager to set up and run the fund after securing commitments from the pension fund and high net worth individuals.

3. This original aim was overtaken by the announcement of the City Deal for Nottingham in which the government agreed to invest £25m in a venture fund if additional funding could be secured. Following further discussions with the City Council, it is clear that the government would prefer to make the investment through an Enterprise Capital Fund (ECF) co-ordinated by Capital for Enterprise (CfEL).

4. CfEL is the government's equity investment vehicle. Their website states that it is 'a fund management company which designs, delivers and manages venture capital and debt guarantee schemes on behalf of the public and private sectors'. It is wholly owned by the Department for Business, Innovation and Skills and is 'the largest single investor in UK venture capital'.

5. ECFs are designed to increase the availability of growth capital to SMEs through fixed term private equity funds, largely structured as English limited partnerships. ECFs are awarded by CfEL following a defined selection process and detailed commercial, financial and legal checks. Government funding in an ECF is normally limited to a third with the manager required to raise the additional capital from other sources. This means that an additional £12.5m would need to be raised to match the £25m government funding. The manager will need to

convince CfEL of their ability to raise this capital and is normally allowed 6 months from the award of an ECF in which to complete the fundraising.

6. The City Council sought proposals from a number of existing venture capital managers in order to select a preferred manager to put forward to CfEL for the ECF process. Interviews were held on 18 October 2012 at which four prospective managers presented and were questioned on their proposals. Foresight Group has been selected as the preferred manager.

7. Foresight Group has been raising and managing investment funds for over 25 years and currently has assets under management of over £650m. It employs 46 professionals and currently manages 60 portfolio companies. Since 2007, it has sold 19 portfolio companies realising an average cash multiple of 4.1x the original investment.

8. The fund’s strategy will be to develop a diversified portfolio of unquoted investments to enable the fund to deliver commercial returns to investors. It will be regionally focused on companies based within Nottingham and Nottinghamshire but will not have a regional constraint. The risk adjusted returns will be key in deciding where to invest.

9. The preferred manager is now in discussions with CfEL regarding their proposals. Appendix A shows extracts from CfEL’s *Guidance for Prospective Managers* giving brief details of the information required and the assessment criteria used by CfEL.

10. The Fund currently has an agreed target allocation to private equity of 10% of the Fund (which equates to about £300m) and has made commitments totalling approximately £125m. These are shown in the table below. Within this is an existing commitment of £4m to an ECF. The majority of individual commitments are between £5m and £15m in closed funds with terms from 10 to 14 years. Each fund calls capital only when specific companies are identified for investment and it would be expected that distributions are made following successful exits from investments. In this way, the net exposure to an individual fund is unlikely to reach the full commitment level. Quarterly reports are received on each fund.

| **Fund** | **Vintage** | **Commitment** | **Undrawn** |
|---|---|---|---|
| Wilton Private Equity Fund LLC | 2001 | $14,000,000 | $605,622 |
| Pantheon Europe Fund III | 2001 | € 10,000,400 | € 1,000,400 |
| East Midlands Regional Venture Capital Fund | 2002 | £5,000,000 | £1,253,333 |
| Coller International Partners IV | 2002 | $10,000,000 | $1,400,000 |
| Schroders Private Equity Fund of Funds III (PEFOF III) | 2005 | € 22,000,000 | € 2,750,000 |
| DCM Private Equity Fund II | 2005 | $18,000,000 | $6,552,000 |
| Pantheon Europe Fund V | 2006 | € 15,000,000 | € 4,050,000 |
| Coller International Partners V | 2006 | $18,000,000 | $4,059,000 |
| Catapult Growth Fund LP | 2006 | £4,000,000 | £154,822 |
| Altius Associates Private Equity Fund | 2007 | $10,000,000 | $3,455,656 |
| Partners Group Secondary 2008 | 2007 | € 13,000,000 | € 1,698,357 |
| DCM Private Equity Fund III | 2012 | $16,000,000 | $15,280,000 |
| Coller International Partners VI | 2012 | $16,000,000 | $12,936,526 |

| | | | |
|---|---|---|---|
| Altius Associates Private Equity Fund II | 2012 | $15,000,000 | $14,114,658 |

11. It is proposed that the Fund commits £10m to the new ECF subject to approval by CfEL. Following robust discussions at the meeting on 30 October 2012, the Pensions Working Party recommend that such a commitment be made.

## RECOMMENDATION/S

1) That a recommendation is made to the Nottinghamshire Pension Fund Committee to commit £10m to the ECF to be managed by the Foresight Group once approved by CfEL.

**Report author:**
**Simon Cunnington**
**Senior Accountant – Pensions & Treasury Management**

**Background Papers**
None

## ECF award process – extracts from CfEL's *Guidance for Prospective Managers*

### Mandatory initial information

- Details of the proposed ECF's investment strategy including, target sectors and investment stages, investment structures and any co-investment agreements, length of investment period and proportion of funding reserved for follow on investment.
- Summary CVs (as an annex) of key investment personnel involved in the fund and details of their proposed role within the ECF.
- Details of any investment track record; from the team as a whole and for individuals within the team (supporting information may be included as an annex).
- Details of private investors willing to back the fund (evidence of commitment e.g. letters of support may be attached as an annex).
- Details of management fee, start up costs and any other fees and costs that will be charged to the fund and details of all fees likely to be charged to investee companies by the fund or linked organisations.
- Level of Government funding sought and level of private investment.
- Details of the Government's fixed profit share (this must be a fixed number that will apply throughout any and all distribution of profits) and how any other profits are to be distributed.
- Acknowledgement that the applicant has read and can accept the terms of the Government‟s draft ECF limited partnership agreement.
- Confirmation that the applicant has read this Guidance and accepts the terms herein.

### Assessment criteria

The assessment criteria are broken down under four broad headings:

- strength of investment team, relevant experience and expertise;
- investment strategy;
- sources of private capital; and
- financial terms.

Under each heading, there are certain features that must be present in all proposals, and further criteria that CfEL will take into account when assessing them.

Each of the four broad areas will form an important part of the assessment process, and none will be of overriding importance. This means that the successful proposals will not necessarily be those from teams with most experience, or those offering the most generous financial terms; instead, they will be those that offer the best overall value for money in meeting the Government's objectives.