VENTURING FORTH

Venture capital funding in Northern Ireland is relatively thin on the ground. With Invest NI's having released its development fund tender, Business Month spoke to Crescent Capital to gauge the success of funds for the investors and the companies

DEEP in the Department of Finance and Personnel's Central Procurement Directorate website, wedged between supplier contracts for laundry chemicals and prisoner footwear, is Project 3113. Invest NI is the organisation behind what's known as the Development Fund, one which is intended to invigorate Northern Ireland's early stage companies deemed to have the most potential.

But Invest NI won't be doing the deeming. It will be handing that task over to a venture capital company which will have to take the £10m the agency intends to put into the fund and raise another £20m. That may sound like a tall order, but the venture capital community has been hankering after the release of the tender for months. In fact, some have been worried that the gap between the end of active investing from the last fund of this nature — the Crescent II — in spring 2010 and the likely first investment of the next one in spring this year has been unnecessarily long.

But it's arrived now and there's no doubting that £30m investment is, to put it mildly, quite a lot of money. In fact, given the current tough economic times it's probably not over-egging the pudding to say Northern Ireland PLC will look upon it as manna from heaven. Nevertheless, Invest NI think it's money well spent, or to be more precise, invested.

"Invest NI believes that the creation of these funds will fill a gap in the local venture capital market," William McCulla, corporate finance director at Invest NI said. "They will offer innovative, young, high-growth potential companies a source of equity funding through which to accelerate their development."

There's no doubt the previous fund has done just that. That was managed by Belfast-based

Crescent Capital investment manager Hal Wilson

Crescent Capital and is now in the third phase of its 10-year limited partner structure when the fund unwinds its investments. Of those £22.5m investments (£7.5m provided by Invest NI and £15m raised by Crescent), audio compression specialist Audio Processing Technology has already been sold in two separate tranches to Andemat Group and electronics giant CSR while Lagan Technology, which specialises in customer relationship management, has been sold to Kana Software. More exits are expected in the coming months.

The remaining companies in the fund include Avalon Instruments, Datactics, Fusion Antibodies, MailDistiller, Omiino and Replify. Its previous fund, the £14m Crescent I, backed a dozen companies including scientific camera manufacturer Andor Technology, which listed on the London Stock Exchange in 2004; timber firm Balcas and an earlier funding round for Lagan Technologies.

Crescent looks for NI-based companies operating in the IT, life sciences and manufacturing sectors into which it will invest between £250,000 and £1.5m initially, to a maximum of £2.25m.

But it's not unique in the world investment market and expects to come up against considerable competition for the current Development Fund from other venture capital companies from around the world who are fighting over a smaller pot on the global market.

"We've been instrumental in some of Northern Ireland's best-known technology businesses but we're by no means complacent," chief executive of Crescent Capital Colin Walsh told *Business Month*.

"The fund-raising environment is very tough so I'm expecting a lot of competition. To people that manage regional venture funds around the UK or sizeable venture funds in Scotland or the Republic of Ireland this is an attractive franchise for them to bid for."

Despite this, there's no denying the benefits of being the incumbent manager.

"Our unique selling point is that we've done it before, we've done it successfully and we really know our space," investment manager Deirdre Terrins said. "If it lives and breathes in Northern Ireland or has a heartbeat and is entrepreneurial then the chances are we know about it; it'll be on our deal flow list."

Encouragingly, they see the relatively large size of the latest Development Fund to be achievable in the current economic environment in Northern Ireland, both from the point of view of raising cash and from having sufficient companies to back.

"We believe a £30m fund is achievable and investable in the next five years," she said. "Our track record shows we are able to go out there and leverage up from that initial pot of money to a substantial fund."

But what advantage do venture capital funds have over traditional forms of fund raising?

For a start, the credit crunch and subsequent risk averse lending nature of banks has put paid to lending from many different areas, for obvious reasons, and there's a growing feeling venture capital backing will become as prevalent in NI as it is in the rest of the UK and in the US.

But there's a pervading misunderstanding of how venture capital works. Colin Walsh sums up the exact process nicely.

"Venture Capital is cash to finance the growth of your company. It's not a grant, it's not a loan and it's not a debt. In return for cash, the venture capitalist will normally receive a percentage shareholding in your growing company."

With the VC having a share in the company, there also tends to be a lot more hands-on help, so contact between management in an invested company and the VC's investment man-

Crescent Capital's chief executive Colin Walsh and its investment manager Deirdre Terrins ager is close and continual. Afterall, the VC's success depends on the company's success.

From an economy-wide perspective, there have also been proven benefits in the local economic landscape, as Mike Smyth, head of economics at the University of Ulster points out.

"If you look at the performance of Crescent Capital, in their funding round they generated 700 jobs," he said. "They added about £45-£50m to gross value added from an initial investment of only a few million. The multiplier effect is colossal. This is private sector, this is the market working."

Declan Kelly, US Economic Envoy to NI, told *Business Month* that attracting venture capital investment to NI will need a clear signpost from Government. "If you have a private sector dominating the economy or one that's heading in that direction then they (investors) can put their money on black. Then you'll get the money, and it'll be for £400m not £4m. Today people don't have a route map to know whether that's possible or not," he said

Either way, the prevalence of VC funding in NI, such as the Crescent funds and the £10m Viridian Growth Fund run by Clarendon Fund Managers, has already proved its worth. If anything, the tightening of the global credit market over the past few years mean it will become an even more popular method of funding for young companies wanting to take the next step and Project 3113 may be crucial in maintaining the growth of the NI economy.

Colin Walsh, chief executive of Crescent Capital

SOME TIPS FOR COMPANIES IN SEARCH OF VENTURE CAPITAL

THINK that venture capital backing might be right for your company? Here are a few tips from The British Private Equity and Venture Capital Association:

- **Does your company have high growth prospects and are you and your team ambitious to grow your company rapidly?**
- **Does your company have a product or service with a competitive edge or unique selling point?**
- **Do you and/or your management team have relevant industry sector experience? Do you have a clear team leader and a team with complementary areas of expertise, such as management, marketing, finance, etc?**
- **Are you willing to sell some of your company's shares to a venture capital investor?**

If your answers are "yes" to all of these then venture capital is worth considering. However, it is important you do your research before approaching a VC. Not all funds are looking for the same thing — some are generalist, some specialise by sector. The size of the fund will also have a bearing on the types of companies they are willing to invest in.

As a rule of thumb the bigger the fund the more likely they are to want to invest a larger amount. If you are a small company near the beginning of its life, you will want to look towards some of the smaller funds out there.

Of crucial importance is the business plan. Without a good, coherent business plan, you stand little chance of even getting a meeting with a venture capitalist let alone funding.

...and on the other side of the coin

If you fancy getting behind young companies but don't have millions to invest then venture capital trusts might be an option, writes **Julian Knight**

"A GROWN-UP Dragons' Den" is one description of investing in a venture capital trust; "high risk and illiquid" is another.

So what's the truth? What do these heavily tax-incentivised investments potentially offer you? The idea behind VCTs is straightforward. You invest money in a fund which in turn buys into small and medium-sized businesses. In effect, they provide investment and working capital for firms from start-ups to medium-sized businesses looking to make it big.

VCTs stay invested for a while, and if they make a profit they pay this back to their investors in the form of dividends.

But it's not just the prospect of making big profits from getting in on the ground floor that appeals. There are big tax breaks that come with VCTs.

It doesn't stop there. "There is the opportunity to put a substantial sum into VCTs one tax year, garner the tax relief and then reinvest that," said Keith Taylor, managing director of TaylorFrost Wealth Management.

But there is a big proviso with the tax relief: the money has to stay invested for five years or it will all have to be paid back.

However, so lucrative is the tax relief that some investors buy into VCTs on the back of it. "You can divide the VCT market into two," said Simon Rogerson, CEO of VCT provider Octopus.

"There are VCTs which look to run for five years and then pay their investors back who would have the full benefit of the tax relief. And then there are those which use the money for long-term growth and to produce dividends. These tend to be more adventurous in their outlook: a bit like a grown-up *Dragons' Den* they try to spot the market leaders of tomorrow."

However, the mix of tying up your money for five years minimum and the risks associated with any sort of investment in start-ups and small business makes VCTs a heady cocktail probably best sampled by those with large amounts to invest.

"First make sure it matches your risk profile. If you're cautious it may not be for you. Find a good manager with experience of picking the right firms to invest in, and only then does tax relief play a part in the decision," Mr Taylor said.