



## **Our first Newsletter comes with sincere apologies**

Within the few days you should receive the first two of seven certificates for EIS investments made by the t1ps Smaller Companies EIS Fund. About time too I hear you say. And you are correct. I can only apologise and say that as someone keen to settle my UK tax affairs for the last time which relates to the year ended this April, I share your pain. That is especially so given that I think I might get a rebate and a cheque from the taxman is always welcome.

The reason for the delay is that we had hoped to save admin costs and send out a bunch of certificates together. Companies can take rather longer than one might expect in filling in paperwork and liaising with the HMRC. Anyhow the first two EIS3 certificates are now on their way and we have made 4 other investments. As soon as we get those certificates they too will be dispatched. And our final investment is imminent. And then we wait.

We have a second apology which is lack of communication. You will now get a newsletter once every three months by email with updates on where your money has gone and how it is doing.

One thing we do not apologise for is where we have invested. We are very happy indeed with where your cash has gone. Oddly we have spent the past week looking at 5 EIS funds whose managers have gone bust and where the administrators are looking for new managers. Cripes it is not hard to see why EIS has got such a bad name. One manager ran 2 funds. The first fund invested in 6 companies two years ago. Three have already gone bust, one is teetering and there are two whose value is 'a matter of opinion'. The second fund invested in 5 companies. Its record is 3 bust, 1 teetering, 1 value uncertain. The other ran three funds launched in 2008 and 2009. Of the 12 companies backed 2 are already bust and of the 5 we managed to speak to last week none was exactly bullish and 1 'fessed up' that a rescue rights issue was on the way. Truly my cat could not do worse at picking investments than most EIS managers. It is a horror story.

I cannot explain why this should be the case. I think that lured by tax breaks some managers just let all ideas of fundamental research go out of the window. We believe that we have not done that. We cannot guarantee success across the board but we have tried to assemble a portfolio that is de-risked (in as much as any small cap equity portfolio can be) but also offers real upside. We will keep you posted as this portfolio develops during the next 3 to 5 years. Of the 5 stocks which we can reveal that we have backed (one placing has yet to be announced) one is private and 4 public. Three are already operating profitably and, we believe, that the other two are close to that inflexion point where they will be profitable.

Have shares in the companies we backed motored ahead yet? No. Investment (especially in microcaps) is a long term game and our objective is to make very respectable returns on a 3-5 year view which (when combined with the tax breaks EIS offers) should make you all happy enough. I suspect that why some EIS funds are so useless is that they back a series of high risk/high reward plays in the hope that at least 1 comes off. Frankly 100-1 is great when you win but the problem is that you lose 99% of the time and in a 5-10 stock portfolio that is a recipe for disaster. Nothing we invest in will be a 100 bagger. Don't get us wrong - we see reason to believe that within 5 years all of our investments could double and one or two might do a hell of a lot better than that. We shall see. So far - at an operational level - we have seen nothing to change our view of those companies we have backed.

## The Famous Five - Our Investments To Date

In no particular order.

**Sutherland Health Group** (known as Shag to its friends) is a PLUS quoted supplier of condoms but also a range of other products from razors to pregnancy testing kits, to the NHS. The company has historically struggled for four reasons. Firstly it has always been a bit tight on cash. Secondly it has only in the past year generated sufficient gross profits to cover its fixed costs but now it is past that point operational gearing kicks in its favour. Thirdly until now it has been solely reliant on boss George Sutherland and his Mrs (Sheena) to do all the marketing. And finally there have been those pushing it to try to do over-ambitious paper funded acquisitions rather than just growing its core business to profitability.

On condition that all daft acquisition plans are on hold we invested your money at 2.5p (the shares are now 2.75p) in order to allow George to hire in a sales resource and also to launch a couple of new products. The more products one has to shift to existing customers the better. So we are now on track. Results for the year to March 31st came out on 28th July and showed sales up by 6% to £956,000 and a pre-tax profit of £29,000. This year I see no reason why sales could not hit £1.2 million and £1.5 million next year. On a maintained level of margins that should see Sutherland deliver a £100,000 pre-tax profit this year and perhaps £200,000 next time. Within five years profits (where there will be no tax to pay for ages thanks to historic losses) should be heading well past £500,000 as cash generated from operations is re-invested in broadening the prospect range so accelerating sales growth. The market capitalisation is £1.75 million. I hope you can see the strong investment case.

**Beautiful Books** is our only privately held investment. We got in at 5p which valued the company at £1.2 million. The company publishes a really very interesting range of books (my current fave is Their Trade is Treachery) - check out the whole range at <http://www.beautiful-books.co.uk>. The CEO Simon Petherick looks a bit odd (I guess that is the book world) but he knows his onions and is a good businessman. BB is loss making at present but heading the right way and should break into profit early next year - again the five year goal is profits of £500,000 and a trade sale. We invested £100,000 as part of a £300,000 funding which is almost completed. But if anyone wishes to help get that over the line and would like to see an investor presentation drop me an email at [tom.winnifrith@t1ps.com](mailto:tom.winnifrith@t1ps.com). For what it is worth I have signed a contract this week to knock out a little stocking filler in time for Christmas. My author's fees (modest) will of course go to RSH.

**Intandem Films** is an AIM listed film production company. I wrote this about it the other day on [www.ShareCrazy.com](http://www.ShareCrazy.com):

*Let me be upfront and say funds we manage own a good slug of these shares. And we plan to add to our holdings. I spent yesterday evening with the management team and three things struck me.*

- 1. The three many chaps (Gary, Billy and Andrew) have worked together for ages, genuinely seem to like each other and obviously get on well. What makes a good management team? There are clearly a number of factors but the ability to get on well out of work as well as in work, to enjoy each other's company and to have a common goal is - in my view - critical.*
- 2. They did not worry about the share price. The goal is to deliver at a business level. Some CEOs can tell you their company's share price at any time. They clearly fret about little else. Such men are usually less able to tell you the company's exact cash position or to give an accurate view of trading prospects. I was reassured that the Intandem board had to guess at the share price and (it's 2.25p) they all got it wrong. But they are pretty on the ball in terms of the trading position.*
- 3. As a result of a number of factors, including the recent divorce of the CEO, pretty much the entire board's wealth is tied up in Intandem shares. The CEO could have more cash and fewer Intandem shares. He opted for cash poverty and maintaining his holding. That was also the choice I made with RSH. And that tells you everything you need to know. This is a company where my interests as a shareholder are 100% aligned with that of the key managers. The only way these chaps will make real money is via their shares. So there will be no dilutive cash calls. There will be no risky deals which risk the whole show. And management remuneration is cut to fit the corporate cloth. On that basis as a shareholder you can sleep soundly.*

*So, I hear you ask, was that a good call by the CEO? Yes it was. At 2.25p Intandem is valued at c£2.4 million. In the year to 30th June 2010 it should pretty much breakeven at an underlying level. But this is a company with a cracking pipeline of films it is trying to finance and a number are already underway where the revenues will be booked this year. Costs are largely fixed so what will June 2011 post tax profits be? Well it all depends on what deals close and go into production during the next three months. There is already some visibility but my guess is that profits will be between £500,000 and £1 million (with my view at this stage tending towards the upper part of the range. Next year I would be looking for a clear advance on the 2010 result as the current pipeline works through. If my lower number is achieved a current year PE of 10 would see the shares 50% undervalued. If the higher number is achieved 10p a share looks about right (for now) with more upside as visibility for the June 2012 year starts to emerge. The balance sheet shows net cash so there is limited downside risk.*

*Investment analysis is subjective. I may or may not be right about Intandem. But I feel confident. The point of part 1 of my tale of two companies is that at least the ingredients of the management cocktail are in place.*

The shares are now 2.375p. Frankly they go up and down like Ashley Cole's underpants. We bought in at 4p. But in five years time these shares will easily be in double figures - 20p is achievable. We are relaxed.

**Resources in Insurance** (RiiG) has had a turbulent history but seems to be on an even keel. We bought in at 0.45p and the shares are 0.5p valuing the company on a fully diluted basis at c£1.2 million. It provides a range of outsourced services for the UK insurance industry. It is growing. It has net cash. It has huge tax shelter from historic losses. This year it should achieve £50,000 pre-tax. Next year I am looking for £200,000 with similar advances year in year out thereafter. The once thing that could stop this being a great slow burning long term investment is the fact that PLC costs are c£350,000 (if one assumes that the FD, chairman, NEDs etc would be replaced by a predator). So a bidder might look at this and reckon he could do £500,000 plus by next year. For we shareholders it is a win/win situation. For the board it is a... er win/lose situation. We will examine this more in a subsequent newsletter.

**Webb Capital** is a Plus quoted financial services group. Heaven only knows how it is EIS qualifying but it is and we invested at 25p. The shares are 22p but the £1.6 million market cap is more than 50% backed by cash. Peter Webb was the man behind Unicorn. A cheeky Essex boy he is not everyone's cup of tea. He is a fund manager who will tell CEOs who are hopeless where to go - such honesty is rare in the City and I like his style. He is a true value investor. Right now Webb is doing some small scale corporate finance but a move into fund management cannot be that far away. Webb has enough fans that if he does 1/10 of what he did at Unicorn we will prosper greatly.

We will run an interview with Peter in the next newsletter which we plan to publish in mid September. Thereafter we will report back once a quarter.

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