

Electra Priv. Equity Response to Sherborne's letter of 16 October 2015

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Electra Private Equity PLC
21 October 2015

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Response to Sherborne Investors (Guernsey) B Limited (Sherborne)'s letter published on 16 October 2015 (Sherborne's letter)

The board of Electra Private Equity PLC ("Electra" or "the Company") notes Sherborne's letter published on 16 October 2015 and wishes to respond to a number of statements in that letter for the benefit of its shareholders, in particular to address the multiple inaccuracies contained in it.

Commenting on Sherborne's letter, Electra's Chairman, Roger Yates, said:

"It is deeply disappointing that Mr Bramson has shown such wilful ignorance concerning the success of Electra and how we operate. He has made a series of ill-judged, ill-informed and ill-founded claims about the company and its board - we cannot let this stand. It is also high time Mr Bramson spelt out his plans for Electra. Despite being invested for 21 months, he has consistently refused to do so. Shareholders and the public markets deserve better than this. Once again, we urge investors not to put our successful formula at risk and to vote against the Sherborne resolutions."

The board of Electra ("the Board") would draw shareholders' attention to the following key points:

1. Electra's short and long-term performance is excellent

Electra has demonstrated outstanding performance over both the short and long term. Sherborne in its letter has tried to undermine this using selective timeframes or using opaque and unclear analysis. The opaque presentation of returns from the FTSE 250 index adjusted for the effects of gearing is a case in point: it can have no credibility without an explanation. It is appropriate to compare Electra's share price performance to FTSE 250 and FTSE All Share indices, and to compare Electra's NAV performance to its UK listed private equity peer group. These relevant comparisons illustrate exceptional performance over the last ten years. The following table demonstrates this short and long-term outperformance:

NAV total return to 16 October 2015

	1 year	2 years	3 years	4 years	5 years	6 years	7 years	8 years	9 years	10 years
Electra	22%	40%	56%	74%	88%	124%	114%	95%	156%	236%
Morningstar Private Equity Index (excluding Electra)	10%	21%	39%	39%	45%	71%	(21%)	(18%)	6%	35%
Electra Better / (Worse)	12%	18%	17%	35%	43%	54%	135%	114%	150%	201%

Share price total return to 16 October 2015

	1 year	2 years	3 years	4 years	5 years	6 years	7 years	8 years	9 years	10 years
Electra	47%	54%	89%	147%	133%	175%	236%	105%	158%	210%
FTSE All Share	9%	6%	26%	42%	40%	60%	127%	37%	52%	87%
Electra Better / (Worse)	38%	47%	63%	105%	92%	114%	109%	68%	107%	123%
FTSE 250	20%	17%	53%	82%	79%	111%	224%	86%	109%	191%
Electra Better / (Worse)	27%	37%	37%	65%	54%	64%	13%	18%	50%	19%
FTSE Small Cap	16%	14%	52%	81%	71%	83%	173%	49%	62%	96%
Electra Better / (Worse)	30%	40%	37%	66%	62%	92%	63%	55%	97%	114%
Morningstar Private Equity Index (excluding Electra)	23%	23%	71%	97%	76%	93%	34%	(26%)	(15%)	16%
Electra Better / (Worse)	24%	31%	19%	50%	57%	82%	202%	130%	173%	194%

Source: Morningstar UK Limited as at 16 October 2015

Electra has achieved a share price total return of 38% (from the "undisturbed" price as at 27 February 2014, the day before Sherborne's ownership of Electra stock was publicly disclosed, to 16 October 2015) and a NAV total return of 39%. Sherborne, as a shareholder of Electra has, of course, no influence over NAV performance, which is the primary driver of share price performance.

In discount terms the Company's shares are at almost the same discount now (10.9% discount as at 16 October 2015) as they were prior to Sherborne's entry into the stock (10.1% discount as at 27 February 2014).

We would urge shareholders to remember that Electra's existing proven model, executed by Electra Partners under the supervision of the Board, has delivered this exceptional track record of price and NAV performance. It does not need Sherborne's turnaround strategy.

2. Sherborne has still made no case for changing Electra's successful and proven model

In its announcement published on 18 September 2015, Sherborne stated that "[Sherborne] will be writing a letter to the shareholders of Electra, in due course, setting out in detail [its] views on the opportunities to manage and mitigate risks, strengthen governance, and increase shareholder value". In Sherborne's 16 October letter there is no such detail - only a void of substance as well as multiple inaccuracies.

We reiterate that in the light of Electra's strong long-term investment performance, it is for Sherborne to make a case for why other shareholders should support its proposals. After 21 months as a shareholder no such case has been made. In the absence of any credible plan to consider from Sherborne, there is no reason for the Board to change its view that a wholly independent and non-executive Board is best for all shareholders.

3. Sherborne's letter reinforces the Board's view that Sherborne's definition of "non-executive director" includes the active involvement of the Sherborne nominees in portfolio management

Sherborne's letter indicates that, contrary to Edward Bramson's "non-executive director" overtures, Sherborne is pursuing an agenda which includes interfering in the management of the portfolio. This is contrary to the exclusive discretionary mandate of Electra Partners. This is evidenced in Sherborne's letter, in the section entitled "Operating improvement opportunities" where Sherborne states "Updating the operating performance data in last year's letter has not changed our conclusion that a review is warranted".

4. Sherborne is an activist investor with a short-termist and cost-cutting focus - this is patently misaligned with the Company's strategy; Sherborne's letter does not change this

As we explained in Electra's shareholder circular dated 8 October 2015 - the appointment of the nominees of this activist investor would risk introducing confusion to existing and prospective portfolio businesses over Electra's investment strategy, which is potentially value destructive.

The Board of Electra is particularly concerned at Mr Bramson's apparent misunderstanding of Electra's business and portfolio, highlighted by what appears to be confusion around portfolio margins. For example Sherborne claims that the companies in Electra's portfolio have "*somewhat lower operating profit margins and higher fixed costs than companies [they] have typically found to be good candidates for operating improvement*". This claim offers no supporting evidence and omits any acknowledgement of Electra's very strong EBITDA margin for direct unlisted investments (excluding real estate investments) - an average of 21%¹.

Moreover, Mr Bramson has exhibited a similarly concerning level of misunderstanding with regard to the use of Electra's credit facility. He appears to misunderstand the difference between an available facility (i.e. a commitment by a bank to provide finance if needed) and drawn debt. The Board's independent decision to renew the credit facilities this year de-risked the business since it locked in longer term, lower cost facilities which are available should the Company require them.

5. Sherborne's claim that its nominees will only represent a minority on the Board is misleading

Sherborne currently holds a 29.75% stake, and so the Sherborne nominees would wield disproportionate power on the Board, leading to it and its own shareholders (some of whom are also Electra shareholders)² potentially obtaining creeping control over Electra, without paying a bid premium.

6. Sherborne's claim that Electra Partners controls the Board is wholly inaccurate

The Nominations Committee of the Board of Electra identifies suitable Board candidates using external recruitment consultants. This process of identification is not, contrary to what is implied by Sherborne, driven by Electra Partners. On the contrary, the process is controlled by the Nominations Committee, and shareholders vote on the re-election of directors annually.

7. Sherborne's criticisms of the review are inaccurate

Electra announced the results of its latest fee review on 11 February 2015. Sherborne claims this review "*fell significantly short of market expectations*" but this is incorrect. The review produced a more favourable fee structure for the Company which is wholly aligned with its strategy, a reduction in financing costs, a reduction in gearing and a policy to distribute a targeted 3% of NAV per annum. We note that Sherborne has at no stage disclosed to the Board what its "*preferred*" dividend distribution structure would be. Following the review, there has not (contrary to Sherborne's allegations) been an increase in portfolio risk - the portfolio assets remain diversified by vintage and sector.

The investor reception of the review is evidenced not in one day's market movement (which inescapably is influenced by wider factors in market sentiment) but by subsequent share price total return performance, which has been 15% between 11 February 2015 and 16 October 2015.

8. Electra's disclosure is award-winning³, and whilst the Board welcomes constructive comments on improved disclosure, it considers that Sherborne's comments are without merit

As previously announced on 20 October, the Company's full year results will be published on 26 October 2015, which the Board expects will again provide a full and meaningful analysis of portfolio activity and the financial condition of the business.

On specific points raised by Sherborne:

- (a) Weighted averages are a useful method of demonstrating simply and meaningfully key aspects of the portfolio. As Sherborne recognises they are accepted practice in private equity disclosure.
- (b) Sherborne's analysis of Electra's performance on a gearing adjusted basis is not clearly explained and is opaque. Electra does clearly disclose the gearing levels in the portfolio on a weighted average basis. Sherborne has suggested that Electra is reliant on gearing beyond index levels to generate returns, however as at 30 September 2015, the Electra portfolio's gearing was at similar levels to the FTSE 250's net debt/EBITDA⁴.
- (c) Fees payable to Electra Partners are clearly stated in Electra's circular to shareholders published on 19 September 2006: "*The Manager is entitled to retain monitoring fees and directors' fees which may be generated on the Company's investments. All transaction fees must first be applied to repay abort costs on uncompleted transactions from the current financial year and abort costs in excess of transaction fees from the prior financial year (if any). Any transaction fees in excess of such abort costs will be divided equally between the Company and the Manager.*" The monitoring, directors' and transactions fees paid to Electra Partners are reported monthly to the Board.

Electra communicates regularly with shareholders in order to provide valuable information and insight through annual and interim reports, quarterly update reports, web disclosure covering key shareholder documents and key portfolio information, as well as recently holding an inaugural Capital Markets Event presentation by Electra Partners and senior management at selected portfolio companies.

9. Finally, the number of inaccuracies in Sherborne's letter are surprising to the Board

Sherborne's letter contains a number of statements which are incorrect. Certain of these inaccuracies are set out more fully in the appendix to this announcement.

In a letter to Mr Bramson on 29 September 2015, the Electra directors explained that no person has ever joined the Board of Electra making such an extravagant claim as he had regarding the value he could create for shareholders, with such insufficient justification. The Board would now add that no director has ever joined the Board of Electra having made so many inaccurate public statements in support of his or her nomination.

The Sherborne letter to Electra shareholders has strengthened the Board's view that Sherborne's nominees, Mr Bramson and Mr Brindle, are not suitable candidates to join the Board.

Conclusion

In the light of Electra's strong long-term investment performance, it was for Sherborne to make the case for why other shareholders should support its proposals. Sherborne's letter again failed to meet this requirement.

The Board promotes "reasonable questioning" of portfolio performance. As stated in the Company's recent circular of 8 October 2015: "*Electra Partners has been and will continue to be subject to robust and constructive challenge from a fully independent and non-executive Board and the Board should be allowed to continue to perform this role without interference from the Sherborne Nominees*".

In the opinion of the Board, Sherborne is an activist investor seeking control by the backdoor.

The Board of Directors unanimously considers that the resolutions to appoint Edward Bramson and Ian Brindle to the Board of Directors of Electra are not in the best interests of the Company's shareholders as a whole.

Your Board once again urges ALL SHAREHOLDERS TO VOTE AGAINST BOTH RESOLUTIONS

Roger Yates

Chairman

1 For the 12 months to 31 August 2015.

2 Aviva Investors, Fidelity International Limited and Insight Investment Management (Global) Ltd are all shareholders of Electra and Sherborne Investors (Guernsey) B Limited (SIGB). Together, they hold 9.3% in Electra (as at 15 October 2015), and 34.8% in SIGB (as at 12 August 2015, according to SIGB's website).

3 Electra won the AIC "Best Report and Accounts - Specialist" award as announced on 5 June 2015.

4 Electra Partners and Bloomberg. The Electra portfolio gearing referred to includes all direct unlisted investments over £5 million with the exception of CALA, Promontoria, PINE, Sentinel and Park Resorts.

Timetable

Latest time and date for receipt of Form of Proxy from shareholders

11.00 a.m. on
Tuesday 3 November 2015

Voting record time for the General Meeting

6.00 p.m. on
Tuesday 3 November 2015

Time, date and location of the General Meeting

11.00 a.m. on
Thursday 5 November 2015
at Allen & Overy LLP, One Bishops
Square, London, E1 6AD

Appendix

Set out below are a number of key inaccuracies within Sherborne's letter which the Board wishes to draw to the attention of shareholders:

Sherborne's Letter	Rebuttal
<i>"Our nominees are exclusively aligned with the interests of all shareholders and their independence from the investment manager would not affect their desire to work collaboratively and constructively with the board and with Electra Partners."</i>	MISLEADING <ul style="list-style-type: none">■ Sherborne nominees are aligned with Sherborne, not all shareholders, as evidenced by comparing Sherborne's short-termism, with Electra's long term growth strategy.■ Edward Bramson is a founder and a partner of Sherborne Investment Management (Guernsey) LLC and its associates. Ian Brindle has a long standing working relationship with Edward Bramson and was the Chairman of Sherborne Investors (Guernsey) B Ltd until May 2013.
<i>"Before we made any request for board representation, Electra wrote to certain of its shareholders threatening retribution if they were supporting us."</i>	NOT TRUE <ul style="list-style-type: none">■ No "retribution" has been threatened to any shareholder.
<i>"During the same period Electra attempted, unsuccessfully, to hinder our regulatory approvals. Had these approvals been denied, we could have been compelled to divest our Electra shares at a loss."</i>	NOT TRUE <ul style="list-style-type: none">■ Under FSMA 2000 Sherborne was obliged to seek FCA consent to its becoming a controller of regulated entities in Electra's portfolio PRIOR TO increasing its Electra holding above 10%. Sherborne did not do so.■ If the FCA had required Sherborne to sell its holding, this would have been as a consequence of Sherborne's regulatory breach.■ Once Sherborne had realised that it did need FCA consent, Electra provided it with appropriate and timely assistance.
<i>"In order to persuade us to drop our request to nominate directors, the board suggested that Sherborne Investors should make a proposal to become the Alternative Investment Fund Manager of Electra's assets."</i>	NOT TRUE <ul style="list-style-type: none">■ This discussion of regulatory issues relating to management of Electra's portfolio has been taken completely out of context. Sherborne refers to a letter from Roger Yates to Edward Bramson on 30 April 2015 which states:■ <i>"In summary, the Board believes that it would be wrong to invite [Mr Bramson] to join the Board to execute and implement [his] proposal without three important items first being in place: 1. A clear and detailed understanding of [Sherborne] plans to add value. 2. A belief from the Board that these plans are credible. 3. A road map for implementing these plans that is consistent with regulatory and contractual responsibilities and that can be achieved at a cost and risk that does not eliminate any potential upside. We are happy to engage with [Sherborne] around each of these points."</i>
<i>"After many months of discussions with Electra, the directors finally admitted in their letter of 12 August 2015, that the board will not appoint directors who are not acceptable to the Investment Manager as it: "risks...the relationships at both the Electra Partners and the portfolio company levels.""</i>	NOT TRUE <ul style="list-style-type: none">■ The letter does not say that the board will not appoint directors who are not acceptable to Electra Partners - it says that <i>"a departure from the wholly non-executive and independent board risks destabilising the current successful partnership between the Board and Electra Partners."</i>

"Sherborne Investors is not proposing to become the investment manager and is nominating only two non-executive directors to a board of eight, six of whom are current members of the board and would continue to be the dominant majority. We are aware of no excuse in the UK Corporate Governance Code or elsewhere for the board's admission of discrimination in its letter to us of 29 September 2015 that:

"[Sherborne Investors'] nominees are being treated differently to any other appointment made to the Electra Board."

TAKEN OUT OF CONTEXT

- The Board's letter of 29 September 2015 stated: *"There is no "rule" as to the qualifications required to join the Electra Board. In your letter to Electra Shareholders of 17 September 2014, you said "Sherborne Investors believes that, with certain changes in approach, the aggregate value of shareholdings in Electra could be increased by more than £1 billion with lower risks and less volatility than under the current strategy". For over a year we have been asking you to explain what these changes are, but despite meetings and correspondence you have not done so. No director has ever joined the Board of Electra making such an extravagant claim, with such insufficient justification. That is why your nominees are being treated differently to any other appointment made to the Electra Board."*

"Mr Yates told us that the contract with Electra Partners contained provisions that precluded our nominees from joining the board."

NOT TRUE

- Mr Yates has made no such statement.

"The board... abandoned this claim and other diversionary... obstacles that they had raised, leaving the Investment Manager's control of the board's nominating process as their only substantial issue."

NOT TRUE

- In the context of Electra Partners' mandate, there are regulatory and contractual obstacles to interference by the Board in the management of the portfolio. The Board explained these to Sherborne for discussion purposes, not as a diversion.
- Electra Partners does not control the nomination process.