A different type of investing - understanding direct secondary transactions

Azini Capital is a UK based private equity firm that specialises in acquiring shareholdings in private and small-cap public technology companies from historical investors and shareholders

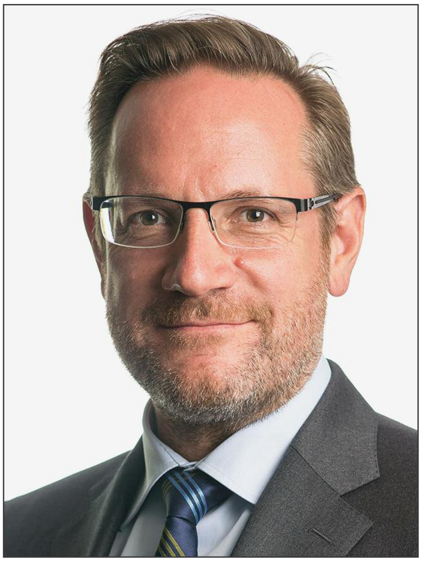
We talk with Co-Founder Nick Habgood.

When and why did you form Azini?
We formed Azini in 2004 but really got started with the current business model in 2007. We'd been investing and involved in the venture market since 1998 and seen that the lack of liquidity was inhibiting the growth of the market.

The issue is that investments in private companies are, by definition, very illiquid. It's very difficult for an individual shareholder, to achieve an exit unless they can persuade all of the other shareholders to sell the entire business. Even then, there can be points in the cycle when it's just not possible to sell a business, or the business may not be ready for sale. Given that it might take 10 or even 15 years for a company to reach maturity, that's a big problem.

We decided that offering liquidity in this otherwise illiquid market was an opportunity and thankfully we had some great backers who agreed. We set up Azini Capital to acquire minority shareholding in private and small cap public technology companies.

The interesting thing is that there are many different reasons why somebody would want to sell their interest in a business before a natural trade sale or IPO exit. The classic is a venture capital fund that has come to the end of its defined fund life. However, we have also acquired interests from private equity funds, corporate investors, small-cap fund managers, hedge funds, high net worth investors, and founders. The seller could be as straightforward as a founder who, for example, still owns 25% of the business and has decided to leave to pursue other interests or start something new.



Nick Habgood
Co-Founder Azini Capital

One school of thought on this model is that it is buying distressed assets from other investors, but from what you're saying, that's absolutely not the case.

It's absolutely not the case. We look for strong and healthy companies with good growth prospects. We're looking for shareholders who, for some rational reason, are looking for liquidity.

When we evaluate opportunities, we look at the growth prospects of the company, just as any venture investor would. In many cases our returns don't come from buying at a discount but from the growth prospects of the company over the next three to five years.

In October 2010 we bought a portfolio of holdings in 18 companies from Apax Partners. Apax wanted to focus on their very successful buyout activities and decided that it made strategic sense to sell their portfolio of growth-stage technology investments. These were really good quality businesses located across the UK, USA, Scandinavia, Germany, Ireland and Israel. I think that the fact that top quality organisations, such as Apax, 3i and JPMorgan, are engaging in secondary transactions shows that it has become an accepted and respectable part of the industry.

What is the sector focus for Azini?
We focus on growth-stage, technology, and technology enabled businesses. Companies which have proven products and demonstrable commercial traction. There is no absolute cut-off but typically we

work with companies with at least £5m of revenue. The largest company in our business has £50m of revenue.

Most of the time when we're putting additional investment into the companies, it's not because they're burning lots of cash on a day-to-day basis, but because they are investing in sales and marketing, opening new international offices or making bolt-on acquisitions. It's more about driving growth and helping the company get to the next level.

Finding and creating a balanced team is really important . . . I have gone away from trying to find that superstar striker - the individual entrepreneur CEO who purports to be the perfect all-rounder

Is it a competitive market?

Not really – and that has its advantages and disadvantages. Not many people know that there is an option to sell a minority shareholding in a private company. However, on the other hand there aren't very many people who will buy a 20% or 30% stake in a business.

We sometimes describe our position in the private equity market as sitting between, but away from, the venture capital players and the buy-out firms. The venture community are principally looking to invest fresh capital into relatively early stage businesses. The buyout community are normally looking to acquire control of more mature, cashflow positive businesses. We sit in the middle where we'll acquire a 20%, 30%, 40% stake in a growth-stage company, and if required also put additional capital into the company. We're borrowing a little bit from both the venture and the buyout communities.

Tell us about the various funds.

Our first fund, creatively named Azini 1, was invested between September 2007 and September 2008. We acquired a small portfolio from a property company, some holdings in individual AIM listed companies and an entire fund from JPMorgan.

In our second fund we acquired the portfolio of companies from Apax Partners.

Then from the end of 2010 we had a series of very successful exits, selling more than a dozen companies with more than $1.25bn of value in a three-year window. That was quite nice because that meant that our funds were fully returned and into profit.

Earlier in the year (2014) we raised our third fund. Azini 3 is a $100m fund that allows us to address portfolios or individual company opportunities. We completed the first investment a few weeks ago; acquiring an interest in an AIM listed business called Kalibrate.

We meet lots of individuals who want to move from exec to non-exec and become chairman or non-exec directors. Obviously within your business you'll have non-execs. Any advice as to how to make the transition, as it is quite difficult to make the breakthrough into the non-exec world?

It sounds obvious but it is firstly really important to understand the difference between executive and non-executive roles. To use a sports analogy, it is the difference between being a player and being the manager or coach. These are fundamentally different roles and it is a surprisingly difficult transition. Perhaps think about taking on a non-executive position in a smaller business and allow yourself some time to get comfortable with the role.

In terms of securing a role - I think it's a question of trying to think about what differentiates you. Which are the two or three skills or experiences that make you uniquely valuable to a business? Weirdly, it's not necessarily just about things like your contacts database or the fact you know an industry sector. Actually, many of the good non-execs are really good at things like recruiting - probably one of the more important things that we do in our jobs, frankly.

To extend the sporting analogy - one key to success is getting the right players on the pitch, each playing in the right position and ideally to the same game plan. Finding and creating a balanced team is really important. In smaller companies in particular I have gone away from trying to find that superstar striker – the individual entrepreneur CEO who purports to be the perfect all-rounder. I've had the privilege of working with plenty of really talented people, and there is no doubt that the right CEO makes a huge difference, but very few people can play every position. As a business grows and the needs of the business changes, there is a risk that the individual superstar player becomes the constraint on the business. It's often better to work at trying to build a balanced, team of talented people who actually work together as a team – and I would include the non-execs as a part of that team.