# Herald Investment Trust plc

# 2018

Annual report & financial statements
31 December 2018

# Herald's objective is to achieve capital appreciation through investments in smaller quoted companies in the areas of technology, media and telecoms.

Investments will be made throughout the world. The business activities of investee companies will include information technology, broadcasting, printing and publishing and the supply of equipment and services to these companies.

# HIGHLIGHTS

NET ASSET VALUE PER SHARE 31 DECEMBER 2018*

**£13.08**

CHANGE IN NAV PER SHARE IN 2018*

**-4.9%**

TOTAL NAV RETURN SINCE INCEPTION

**+1,309%**

| NAV AT 31 DECEMBER 2017 | | TOTAL RETURN 2018 | SHARE BUY-BACKS 2018 | | NAV AT 31 DECEMBER 2018 |
|---|---|---|---|---|---|
| £966.7m | + | -£48.3m | -£17.2m | = | £901.2m |

* See page 72: Alternative Performance Measures.

TOTAL RETURN SINCE INCEPTION
(FIGURES HAVE BEEN REBASED TO 100 AT 16 FEBRUARY 1994)

- Fully diluted NAV
- Share price
- Numis Smaller Companies Index plus AIM (excluding investment companies)
- Russell 2000 (small cap) Technology Index (in sterling terms)

Source: Refinitiv (Thomson Reuters)

TOP FIVE WINNERS AND LOSERS 2018
TOTAL GAIN/LOSS IN 2018 IN STERLING TERMS (MILLIONS)

| TOP 5 LOSERS | TOP 5 WINNERS |
|---|---|
| Bango | Attunity |
| IQE | Craneware |
| Frontier Smart Technologies | ZOO Digital |
| BE Semiconductor Industries | BATM Advanced Communications |
| Ceva | Five9 |

## COMPANY SUMMARY

### Company data at 31 December 2018

| SHAREHOLDERS' FUNDS | MARKET CAPITALISATION |
|---|---|
| **£901m** | **£741m** |

| | |
|---|---|
| POLICY AND OBJECTIVE | Herald's objective is to achieve capital appreciation through investments in smaller quoted companies in the areas of telecommunications, multimedia and technology ('TMT'). Investments may be made across the world. The business activities of investee companies will include information technology, broadcasting, printing and publishing and the supply of equipment and services to these companies. The Company's investment policy is contained within the strategic report on page 32. |
| COMPARATIVE INDICES | The portfolio comparative indices are the Numis Smaller Companies Index plus AIM (ex. investment companies) and the Russell 2000 (small cap) Technology Index (in sterling terms). Though we consider these indices to provide reasonable bases for measuring the Company's performance, the portfolio is not modelled on them and outcomes may diverge widely. |
| MANAGEMENT DETAILS | Herald Investment Management Limited ('HIML') is the appointed investment manager to the Company. The management contract can be terminated at 12 months' notice. Administration of the Company and its investments is delegated to The Bank of New York Mellon and company secretarial duties to Law Debenture Corporate Services Limited. |
| CAPITAL STRUCTURE | The Company's share capital consisted at 31 December 2018 of 68,901,568 ordinary shares of 25p each which are issued and fully paid.<br><br>The Company has been granted authority to buy back a limited number of its own ordinary shares for cancellation. During the year 1,406,217 ordinary shares were bought back and cancelled. The directors are seeking to renew this authority at the forthcoming annual general meeting. |
| MANAGEMENT FEE | HIML's annual remuneration is 1.0% of the Company's net asset value based on middle market prices, calculated on a monthly basis payable in arrears. |
| CONTINUATION VOTE | At the annual general meeting of the Company held in April 2016, shareholders voted in favour of the Company continuing to operate as an investment trust. The next continuation vote will be at this year's annual general meeting on 16 April 2019 and every third year thereafter. |
| AIC | The Company is a member of the Association of Investment Companies. |
| LEGAL ENTITY IDENTIFIER ('LEI') | An LEI is a 20-digit code which allows entities involved in financial transactions to be identified. This is a global transparency measure endorsed by the G20.<br><br>The Company's LEI is: 213800U7G1ROCTJYRR70 |
| ALTERNATIVE PERFORMANCE MEASURES | A glossary of alternative performance measures used in the annual report and financial statements is on page 72. |

None of the views expressed in this document should be construed as advice to buy or sell a particular investment.

Investment trusts are UK public listed companies and as such are required to comply with the listing rules of the UK Listing Authority, which is a division of the Financial Conduct Authority.

# YEAR'S SUMMARY

| | 31 December 2018 | 31 December 2017 | % change |
|---|---|---|---|
| Total net assets | **£901.2m** | £966.7m | |
| Shareholders' funds | **£901.2m** | £966.7m | |
| Net asset value per ordinary share | **1,307.9p** | 1,374.9p | -4.9 |
| Share price | **1,075.0p** | 1,171.0p | -8.2 |
| Numis Smaller Companies Index plus AIM (ex. investment companies) | **4,917.9** | 6,001.8 | -18.1 |
| Russell 2000 (small cap) Technology Index (in sterling terms) | **2,597.2** | 2,480.2 | 4.7 |
| Dividend per ordinary share | **–** | – | |
| *Profit per ordinary share (revenue)* | ***0.08p*** | *0.68p* | |
| Ongoing charges* | **1.07%** | 1.08% | |
| Discount to NAV | **17.8%** | 14.8% | |

| **Year to 31 December** | **2018** | **2018** | 2017 | 2017 |
|---|---|---|---|---|
| **Year's high and low** | **High** | **Low** | High | Low |
| Share price | **1,370.0p** | **1,055.0p** | 1,200.0p | 881.5p |
| Net asset value per ordinary share | **1,579.9p** | **1,276.8p** | 1,376.5p | 1,082.8p |
| Discount** | **19.4%** | **9.5%** | 22.1% | 11.2% |

| **At 31 December** | ***2018*** | *2017* |
|---|---|---|
| Profit/(loss) per ordinary share | | |
| Revenue | **0.08p** | 0.68p |
| Capital | **(69.67p)** | 283.44p |
| Total | **(69.59p)** | 284.12p |

* Ongoing charges calculated in accordance with AIC guidelines: see page 72: Alternative Performance Measures.
** The discount is the difference between the share price and the NAV, divided by the NAV.

1 YEAR CHART OF NAV, SHARE PRICE AND COMPARATIVE INDICES
(FIGURES HAVE BEEN REBASED TO 100 AT 31 DECEMBER 2017)

— Fully diluted NAV
— Share Price
— Numis Smaller Companies Index plus AIM (excluding investment companies)
— Russell 2000 (small cap) Technology Index (in sterling terms)

Source: Refinitiv (Thomson Reuters)

# Investment report

> After our strong performance in 2017, 2018 has been a year of consolidation.

**KATIE POTTS**

## COMPANY OVERVIEW

# Achieving capital growth

Herald invests, generally on a long term basis, using fundamental analysis. The technology, media and telecommunications sector globally comprises over 5,000 quoted companies, and many more unquoted.

The manager, Herald Investment Management Limited (HIML), focuses on investment within the technology, media and telecoms sector.

Focus on the sector enables a significant degree of cross-referencing across competitors, customers and suppliers globally. Using this mosaic of information and industry knowledge combined with strong financial analysis, we endeavour to add value. The evolving nature of technology means there is a wide divergence of performance between winners and losers, but the winners can be spectacular.

**WHAT WE DO**

### WHAT WE DO

Analysis entails a prolific number of meetings with companies, either at Herald's offices, site visits or at conferences globally, as well as broker hosted meetings. In addition, Herald relies on independent industry research and published company filings, statements, presentations, websites and broker research.

The trust has consistently invested in early stage companies, often providing primary development capital, then holding investments for long periods, regularly providing further capital when needed.

Many of these holdings have a high stock specific risk and the fund aims to offer investors a low risk way to gain exposure to these exciting opportunities through broad diversification in the number of holdings and the maturity of the businesses.

**HISTORY OF FUND**

### HISTORY OF FUND

The fund was established in 1994 raising £65m to invest in UK and European smaller TMT companies.
In 1996 a further £30m was raised to globalise the fund with the recognition that TMT is a global sector and cross-referencing across geographies is a prerequisite for investing intelligently within the sector.
Since 1996 no further capital has been raised, but share repurchases totalling £118m have been made.

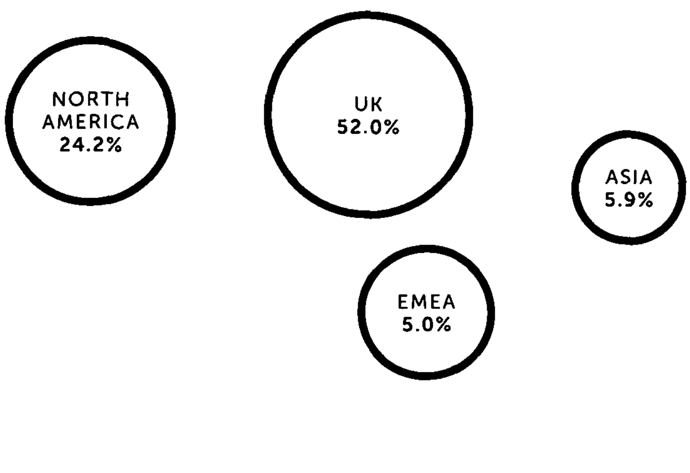
Over the history of the fund the NAV per share, on a total return basis, has compounded at an annualised rate of 11.2%.

# GEOGRAPHICAL ANALYSIS

## GEOGRAPHICAL RETURNS

*Costs are accounted for at the Company level.

## GEOGRAPHICAL SPREAD OF EQUITY INVESTMENTS FOR THE YEAR ENDING 31 DECEMBER 2018[†]




[†]As a percentage of total assets.

## CHAIRMAN'S STATEMENT



# A year of consolidation

At the half-year stage, the net asset value per share ('NAV') had risen by 9.6%. However, the final quarter of 2018 saw a sharp correction in markets, which more than eliminated earlier gains and the NAV had fallen by 4.9% by the year end. Likewise, the share price total return fell 8.2% for the year. It is always disappointing to report negative returns, but the portfolio had been positioned defensively, reflecting the manager's belief that some valuations had become somewhat too ambitious. The performance relative to the wider market is quite pleasing, since the wider market (captured by the FTSE All Share Index) depreciated by 9.5%. We enter 2019 more comfortable that valuations now offer scope for good absolute performance once again.

At the year end, UK listed companies accounted for 52% of the net assets, which is down from 60% a year ago. This was influenced by a deliberate reduction of £54.6 million in the exposure to AIM stocks because valuations had become stretched and we were concerned about the sustainability of inheritance tax relief on AIM stocks. Having represented 47% of the portfolio at the end of 2017, AIM stocks were just 35% by the end of 2018. This reduction proved timely. The UK portfolio returned minus 8.7%. In comparison, the Numis Smaller Companies Index plus AIM (ex. Investment Companies) declined by 18.1%.

The North American portfolio accounts for 24% of net assets, unchanged from the prior year. The positive return of 11.7% in sterling terms is satisfactory in both an absolute and relative sense. Although US technology has offered better returns than most equity indices in 2018, by the year end the Russell 2000 (small cap) Technology Index (in sterling terms) returned only 4.7% in sterling, and declined marginally in dollars.

The technology correction in the US had been much anticipated. However, the markets in Asia and Europe (5.9% and 5.0% of the portfolio respectively) were more challenging. The environment for profits in our sector has generally been benign in the UK and US. This has not been the case in technology manufacturing in Asia. The maturity of the smartphone and PC market was predictable, but the Trump trade battles with China on top created a difficult environment.

The KOSDAQ Korean IT Index declined 22.8% in 2018, the Taiwan Electronics Index declined 6.8% and the Chinese indices have been worse. The decline in Herald's Asian portfolio of 10.9% was therefore relatively good. The return on the small European portfolio was the most disappointing, with a decline of 23.8% in sterling terms. In the long run the returns on the European portion of the portfolio have been the best, but valuations had become extended.

2018 has been the sixth year in succession in which sales of investments in the portfolio have exceeded purchases. Net sales were £40m in the first half and a further £18m in the second half. Over the last six years, sales have exceeded purchases by £218m. Over that time there have been 80 takeovers of portfolio companies with an aggregate value of £347m, of which 16 occurred in 2018 with an aggregate value of £74m from completed deals and a further £5m which has yet to complete.

Over this six year period, £89m has been used to repurchase over 10.4m of the Company's shares. In 2018 alone, we repurchased 1.4m shares, at a cost of £17m. At the end of 2012 there was modest net debt of £18m; by the end of 2018 there were net liquid assets (cash and Government bonds) of £116m. The return in sterling during 2018 on short-dated US Government bonds, held as a proxy for cash, was 8.8%, which was better than the return on equities.

Last year was an extraordinarily busy one for primary offerings. Our manager endeavoured to resist these, except to support existing investments or where there was exceptional value. A number of the larger IPOs were exits for private equity and venture capital where there was limited value. These were mainly in the US. In the UK there was better value, but some potential IPOs did not make it to market because there was insufficient demand, which was disappointing.

There have been dire predictions in the media about the risks in the technology sector and the high valuations. From our perspective the valuations seem high in the private markets, but we are encouraged that valuations seem more sensible in public markets, particularly following the recent correction. There are no parallels to the TMT sector in 2000, when valuations were universally too high.

The most pressing issue today is the trade and tariff war between the US and China. It appears that President Trump's aggressive stance is supported by the US electorate, and even more by the US security departments, so tensions are unlikely to abate. We may be seeing the start of major structural changes with a Western US centric sector diverging from China, and China developing an indigenous self-contained sector. This has already become apparent in the telecoms sector where it appears that Ericsson and Nokia will dominate supply of 5G in the West, versus Huawei and ZTE in China.

The challenge will be for hardware companies dependent on a China supply chain, such as Apple. China is currently a big importer of semiconductors from Taiwan, Korea and the US and is clearly intent on developing indigenous capacity, which will present other challenges.

It is already evident that sub-contract manufacturing is moving out of China at the commodity end for cost reasons, and further up the value chain for tariff and political reasons. Herald focuses on investing in small companies, so we are only marginally exposed to this dynamic: we have a modest weighting in Asian manufacturing and no exposure to the large semiconductor companies.

The only effect will be secondary, if the US/China tensions inhibit global growth. Trump might be an unpredictable mouthpiece to trade negotiations, but it is certain that there is a wider 'US establishment' alarm at the growing strength of the Chinese technology industry, and the US dependency on it as a supplier, for security reasons more than the balance of trade. It seems wise to assume that this will be an evolving issue for months and years to come. If China still has to develop leading edge semiconductor technology, it is already leading edge in many internet technologies.

Although some valuations are discounting considerable growth, and are stretched when adjusted for share-based payments, the sector is still dynamic, and small companies continue to emerge at sensible valuations. The UK has entrepreneurial creativity and continues to be an interesting market. It is constrained by a shortage of institutional co-investors, but that helps Herald in terms of value at the point of entry. Valuations remain more challenging in North America, but the economy and sector remains world-leading.

The implementation of MiFID II has clearly not helped. Successful institutional small company investment managers tend to move up the size scale ignoring microcaps, and illiquidity is increasing due to market breakdown. This is a greater concern for open-ended funds with unpredictable cash flows.

The focus of the fund is capital appreciation, but the Company has again delivered a small profit in income terms, although insufficient to pay a dividend.

**BOARD COMPOSITION AND GOVERNANCE**
I will retire as your chairman at the conclusion of the AGM on 16 April 2019. It has been a great privilege to have been a director of Herald since 2008 and its chairman since 2009. The Company has delivered outstanding returns to shareholders since it was formed in 1994. Herald is unique among investment trusts in playing a vital role in the funding and development of start-ups and small businesses in the TMT sector and there have been many examples where this has delivered value for our shareholders, and for the sector. In addition it has made an invaluable contribution to the UK.

I would like to pay tribute to the contribution of Katie Potts and her team, who have delivered a near four-fold increase in NAV per share since I became chairman. I would also like to thank all of my fellow directors, past and present, for their wise counsel and unswerving support while I have been chairman.

Your board has carefully considered board composition for the period ahead. We were very pleased to recruit Ian Russell as a director from August 2018 and, subject to his election by shareholders at the AGM, he will succeed me as chairman. Ian has extensive and varied NED experience, including on the boards of other investment trusts. He is well placed to lead the Company into the future.

We also recognised that it would be appropriate to increase the size of the board to five directors in order to recruit an independent director with specific experience in accounting. We are delighted that Stephanie Eastment, who is a qualified chartered accountant with great experience in fund management, joined the board in December 2018 and she has succeeded James Will as chair of the audit committee.

**REGULATION**
My tenure as chairman has coincided with a huge increase in regulation in the fund management sector. Every new piece of legislation has added cost and complexity to the industry and ultimately to shareholders. The effects are exemplified by the increase in the length of the annual report and accounts. This has grown by 25% since 2008. The additional 14 pages comprise regulatory disclosures which were not deemed necessary in 2008 but are now required to satisfy all the regulatory bodies.

The industry has had to contend with, among others, MiFID, AIFMD, UCITS V, CRD, SRD, Benchmark regulations, PRIIPs, GDPR and most recently MiFID II. Most of these have emanated from the European Union and have been required to be incorporated in UK law. Every one of these directives has required management time and the great majority have added directly to the costs borne by shareholders and investment managers.

The most recent legislation, MiFID II has fundamentally altered the balance in the broking and investment banking industry in a very worrying way.

The smaller broking houses, which are essential to the health of the smaller companies sector, have been put under great pressure by the new environment which has been forced on them by the changed requirements in relation to the payment of commissions and for research.

**AGM AND CONTINUATION VOTE**
The forthcoming AGM, to which all shareholders are invited, provides shareholders with an opportunity to vote on the continuation of the Company, as the articles of association require every third year. Herald is one of the largest investment trusts specialising in TMT and has performed very well since its launch in February 1994. It is the only specialist technology orientated investment trust with a material exposure to the United Kingdom.

The Herald board believes that the investment manager's focus on smaller capitalisation companies provides exposure to some of the most rapidly growing companies within the Company's targeted sectors and that this should continue to provide attractive long term investment opportunities.

The directors believe that the prospects for investment in the TMT sectors remain positive and that we are fortunate to be managed by Katie Potts. She is one of the most experienced and successful managers in the sector. Your board strongly recommends that shareholders vote in favour of the resolution to continue as an investment trust – as the directors intend to do in relation to their own shareholdings.

We remain enthusiastic about the TMT sector in which we operate.

**JULIAN CAZALET**
**CHAIRMAN**
19 February 2019

## INVESTMENT MANAGER'S REPORT



# The technology sector offers exciting emerging companies

KATIE POTTS FUND MANAGER

In 2018 we were intent on maintaining cash and even accumulating higher cash levels. This was helpful in the fourth quarter when there was a correction, which led to a decline in net assets per share of 4.9%. We are beginning to believe that cash may be a drag moving forwards, albeit there remain some macro imponderables. The intention is to slowly reinvest as opportunities arise, and to maintain the borrowing facility in case a good buying opportunity emerges.

There has been a wide divergence in performance between stocks. A few have disappointed at the trading level, while others have just been de-rated. The subset of the technology sector that has experienced downgrades has mainly been exposed to volume markets, such as mobile phones and automotive. This has hit the semiconductor sector in particular where increases in capacity combined with lower growth in demand have led to price cuts and margin pressure. This has affected holdings such as IQE and BE Semiconductor Industries, both of which performed outstandingly in previous years. We had reduced our positions, but not enough. However, the appeal of the sector is that it is not homogeneous, and in all markets, there are some that grow. For most of our holdings there has been no discernible weakness versus expectations.

The US economy, and consequently the global economy, has benefited from tax cuts which have provided a tailwind to corporate profits. However, this has been offset by the Federal Reserve moving towards normalising interest rates, which the market worried about in the fourth quarter. This, as much as the tariff war, has spooked the markets. Of concern is that the UK has hardly started to normalise interest rates with the Bank of England fearful over slowing the economy around Brexit uncertainty. The housing market already recognises that easy money will not endure forever. However, the macroeconomic environment is less relevant to the technology sector than almost all others. We continue to be in an exciting phase where companies have to adapt or be disrupted. In addition, cybersecurity, data protection (GDPR) and regulation all require compulsory expenditure for Governments and businesses alike.

Technology disruption is also seeing winners and losers within the sector. The legacy companies are evident – IBM, HP, Oracle, Blackberry to name a few. In particular, processing power and storage is migrating to the big datacentre companies dominated by Amazon Web Services and Microsoft Azure, followed by Google and Alibaba. These companies are disintermediating the branded companies such as HP and IBM.

There was a twenty-year period when food retailers outperformed food manufacturers as powerful buying chains squeezed manufacturers margins compared to the weaker buying power of the corner shop. This is happening in computer infrastructure. For Waitrose see Microsoft, for Tesco see Amazon Web Services and for Aldi see Alibaba?

Interestingly IBM was the legacy mainframe computer company that survived the move to client server PC based computing, but is now floundering. Microsoft and Intel were the winners in the PC world. Microsoft has conspicuously succeeded in being the legacy PC company to survive the transition to the datacentre world. The jury is out on Intel, only because its near monopoly position in microprocessors for PCs and servers is now being challenged by AMD and GPUs, and it is being squeezed by the 'supermarket' buying power of the big four datacentre companies.

Furthermore, with the growth in server applications powerful computing can be accessed on battery powered phones and tablets, which do not use X86 architecture, but are ARM based. The companies mentioned here are all larger than this Company's small capitalisation remit, but they are hugely relevant to the small company world. The ability to rent scalable processing power, storage and software is collapsing the cost, and more importantly the capital requirements for small companies. We see this as a driver to global economic growth akin to collapsing oil prices.

It is only in the last few years that the consumer, the enterprise and Government have all been networked, and soon vehicles will be too. The network roll-out for higher speeds continues but is ex-growth. The applications used on the network are far from mature. Faster, cheaper processing power is enabling artificial intelligence to be used commercially, which will have further profound disruptive effects.

### UK

The UK portfolio declined 8.7% on a total return basis. The two worst performing stocks were IQE and Bango, which last year were the best. In 2017 IQE appreciated £29.8m and in 2018 it declined £11.5m. Fortunately, we had been aggressively taking profits on rising prices so that during 2017 we had realised cash of £19.2m and profits of £15.3m, and a further £5.1m of cash and £3.8m of profit in the first quarter of 2018 in 27 separate trades, albeit offset by an investment of £2.9m to support the fundraising to ensure they could invest in additional capital equipment for demand expected from Apple.

The level of expected demand from Apple has reduced, however, and so has IQE's share price. The business remains the world leader in manufacturing compound semiconductor wafers, and now has a strong balance sheet. These wafers will be used in the forthcoming 5G phones and infrastructure,

### REGIONAL ALLOCATION CHANGES (STERLING THOUSANDS)

| | Valuation at 31 December 2017 | Net acquisitions/ (disposals) | Appreciation/ (depreciation) | **Valuation at 31 December 2018** |
|---|---|---|---|---|
| **Equities*** | | | | |
| UK | 582,632 | (59,549) | (54,695) | **468,388** |
| EMEA | 55,616 | 4,640 | (14,892) | **45,364** |
| North America | 207,475 | (13,116) | 23,379 | **217,738** |
| Asia Pacific | 50,373 | 9,695 | (6,663) | **53,405** |
| **Total equities** | 896,096 | (58,330) | (52,871) | **784,895** |
| Government bonds | 29,445 | 14,905 | 2,435 | **46,785** |
| **Total investments** | 925,541 | (43,425) | (50,436) | **831,680** |
| Net liquid assets | 41,109 | 26,317 | 2,048 | **69,474** |
| **Total assets+** | 966,650 | (17,108) | (48,388) | **901,154** |

* Equities includes convertibles and warrants.

\+ The total assets figure comprises assets less current liabilities.

# INVESTMENT MANAGER'S REPORT CONTINUED





and we expect the demand for VCSELs, which are used in the iPhone's facial recognition product, to grow albeit at a slower rate now that Apple has demonstrated that the market for £1,000 smartphones is more limited than hoped.

As a user I am a convert to the belief that facial recognition will be more widely adopted, but the overall phone price must lower, and it will do so as component prices such as DRAM fall. As an investor focussed on smaller companies in the supply chain of large companies such as Apple, it is evident that it is brutally tough in requiring the supply chain to build capacity in excess of any potential demand, and then subsequently has the whip hand on pricing.

Bango appreciated £15.4m in 2017, and fell £13.7m in 2018. Unfortunately, we were not as successful at taking profits realising only £0.5m. The shares were too high, but there were not willing buyers. It is a microcap company with only two customers of significance – Google and Amazon, but very valuable ones they are.

The potential scale of those players makes it difficult to value. We were surprised by how strong both shares were, but in IQE's case there was massive private client buying. Not only did that enable us to sell shares too expensively, but it concerned us that a new phenomenon became more evident – that of private client buying influenced by internet chat boards. This buying was not across the board but very stock specific. But private investor demand of this nature, combined with the disappearance of the institutional investor, had made us cautious for the market overall.

There were also some positive returns. There were five stocks that appreciated in excess of 100% collectively returning £10m. Two of these were struggling companies where the return came from the takeover premium. In both cases, Lombard Risk and Earthport, we were losing faith in management's ability to deliver, and were happy to see them go.

In addition, Elektron, Brave Bison and Versarien rose 145%, 144% and 121% respectively. In terms of materiality Versarien is the most relevant. It appreciated £4.5m during the year. We have significantly reduced the position having started to sell in 2017, and have now realised £9.5m in cash and £8.2m in gains. The company has a graphene product, and an energetic entrepreneurial management team, but again private clients have elevated the price to a level that we could not resist selling.

Craneware appreciated £6.4m with an encouraging rise in revenue and profit expectations. This has been a good long term performer but after upgrades at over £30 per share we were torn between wanting to own the shares long term, and worrying about the valuation being ahead of itself. We sold a little, but the market has resolved the issue with the share price markedly correcting in the fourth quarter.

ZOO was a star performer in 2017 and appreciated a further £6.8m in 2018. When the company was in financial difficulties, we increased Herald's stake to 20% and provided funds through a convertible loan to provide survival funding. It is therefore rewarding to have been able to reduce our holding materially towards a more normal percentage ownership withdrawing £4.6m, and still having a material unrealised gain. BATM has been a sleeper for a while, but has an exciting ARM based networking solution so appreciated 80% and £4.9m.

There were several IPOs that we were prepared to participate in towards the end of the year, but there were insufficient co-investors. On the other hand, we did not participate in the Avast IPO because it exceeded our size threshold of $3bn market capitalisation, but it subsequently fell sufficiently, and we were pleased to take the opportunity to acquire a stake.

We remain committed to AIM but have purposefully reduced the weighting in the portfolio from a high of 44% of the Company's net assets at the end of 2017 to 35% at the end of 2018. The attraction is that there are some dynamic companies, and new ones continue to appear, but our caution emanates from the withdrawal of so many institutional investors. Index tracking funds are growing but do not invest in small companies and, in particular, they do not make the capital allocation decisions in order to provide primary funding of companies requiring capital, which is an important raison d'etre for public markets, and requires judgment and not machines.

We are proud of the fact that we have invested £417m since the Company's inception in primary capital in the UK, and an additional sum of £52m overseas, to provide development capital which is about 5x the outside capital ever raised by the Company, so capital has been productively recycled. The market has become too dependent on marginal buying from private clients, some of which is speculative and some IHT exemption driven. Liquidity is an issue; fund managers of scale cannot get adequately sized positions, particularly when coping with cash inflows and outflows. This has led to takeovers exceeding new issues, and shrinking the addressable market.

The other cloud that has made us so cautious and led to us withdrawing money from the UK is the unknown effects of the numerous regulatory changes. In 2018 sales from the UK exceeded purchases by £60m. The exercise stimulated me to consider the long term cash flows, and overall sales in the UK portfolio exceed purchases by £167m from inception in 1994, with a market value of £468m at the year end.

**NORTH AMERICA**

The North American total return in sterling terms was 11.7% versus the Russell 2000 (small cap) Technology Index (in sterling terms) return of 4.7%, and the NASDAQ return of 3.1% in sterling terms. At one point in the year the return exceeded 30%, so the fourth quarter correction was as vicious as any region but North America had performed better previously. The US is a particularly momentum driven market with gyrations more extreme than elsewhere. Nevertheless, the outcome is satisfactory.

We were net sellers in the UK, and we were also net sellers in North America by £13m in 2018 and by £44m over the last three years. This reflects in part takeovers of £27m in North America in 2018, £61m over the last three years and £131m over the last six years, which is material in relation to a portfolio valued at £218m at the year-end.

This year there have been six takeovers in the North American portfolio, of which the significant ones have been Barracuda, Callidus and Web.com. There have been a healthy number of IPOs in the US. We have tracked thirty one. We do not normally participate in NASDAQ IPOs led by the global players, because we are irrelevantly small clients, and get poor allocations in hot IPOs and filled in the difficult ones, and prefer to look in the aftermarket. We do however want a vibrant public market, and remain frustrated that institutional

SECTOR PERFORMANCE
(STERLING, MILLIONS)

| | Market value equity portfolio 31 Dec 2018 | % of equity portfolio 31 Dec 2018 | Total return equity portfolio 31 Dec 2018 | Total return equity portfolio 31 Dec 2017 |
|---|---|---|---|---|
| Software | 227.7 | 29.0 | 29.8 | 45.2 |
| Computer Services | 88.1 | 11.2 | -8.8 | 38.8 |
| Semiconductors | 86.0 | 11.0 | -39.4 | 56.9 |
| Media Agencies | 65.9 | 8.4 | -16.1 | 20.3 |
| Telecommunications Equipment | 47.3 | 6.0 | 4.9 | -0.4 |
| Internet | 41.8 | 5.3 | -13.9 | 24.2 |
| Publishing | 39.6 | 5.0 | -0.4 | 3.7 |
| Electrical Components & Equipment | 30.9 | 3.9 | 3.3 | 4.5 |
| Fixed Line Telecommunications | 17.1 | 2.2 | 5.2 | 0.7 |
| Business Support Services | 14.7 | 1.9 | 0.1 | -4.1 |
| Computer Hardware | 13.0 | 1.7 | -3.0 | 0.3 |
| Other | 112.8 | 14.4 | -4.7 | 27.1 |
| **Total** | 784.9 | 100.0 | -43.0 | 217.2 |

cash flows continue to move in the direction of private equity, and their valuations seem higher than public ones. We prefer to be in the cheaper market, but do not want the move to private equity and tracking funds to strangle markets to death.

The star performer of the year was Attunity, which appreciated 199% during the year, from a good-sized position, so the appreciation was £10.2m. We acquired a small position in 2014, and bought some more in 2015, but the shares languished although regular meetings with the company reassured that underlying progress was better than the share price. When they had a secondary offering in December 2017 we were the cornerstone of a $23m fund raising, investing $4.75m in a share issue that was a struggle.

Value is more evident in the smaller companies with offerings made by smaller brokers. We are better networked into these brokers following the opening of our New York office three years ago. Alteryx and ACM Research appreciated 149% and 120% respectively. Alteryx's IPO was in 2017, but we invested six months after the IPO following a meeting with management at which we were impressed. We did participate in the IPO of ACM Research from a smaller broker. In both cases the position was small because we are always resistant to committing large amounts of capital until we have got to know the company and its management over a period of time.

By value Five9, Mellanox, Fabrinet and LivePerson were all strong contributors.

The smaller brokers in the US were hit by Sarbanes Oxley, which raised the cost for a small company to be public, and the fact that venture capital is providing follow on rounds to a much later stage.

The latest twist is MiFID, which has hit them hard. Although MiFID has not been implemented globally, some of the large multinational players are applying the same rules. It is evident that some of the technology boutiques important to us have been hit hard. As in the UK it is difficult to know quite how great the pain is, because nobody wants to say they are losing for obvious reasons, but the number of quality individuals choosing to leave the industry, and the continuing drift of lay-offs, tells its own story.

“

The North American portfolio was strong in 2018 having lagged other regions in 2017.

**KATIE POTTS,** FUND MANAGER

# INVESTMENT MANAGER'S REPORT CONTINUED



Tracker funds are even more significant in the US market but do not make the investment judgement required for investing in IPOs. It was interesting to see Spotify come to the market by way of an introduction without the expense of fund raising fees to investment bankers, because venture capital had provided sufficient capital, and index trackers can provide an exit. The price has subsequently performed poorly.

**ASIA**

The Asian portfolio declined 11.2% (IRR, total return in sterling terms). In comparison, the Kosdaq IT Index in Korea declined 22.8% and the larger company TWSE Electronics Index in Taiwan declined 6.8%. Generally, the Asian indices across the region had a difficult year, with some of the smaller companies indices particularly impacted, for instance the Tokyo Stock Exchange Mothers Index being amongst the weakest falling 28%.

In the first half the momentum in Asian stock markets remained very strong, continuing the trend from the prior year. Globally, monetary policy remains loose with interest rates very low. In this environment any areas where there was good newsflow proved irresistible, and there was a great deal of excitement amongst retail technology investors. This was most clearly illustrated by the euphoria (particularly widespread in Asia) that surrounded Bitcoin which peaked close to £18,000 in December 2017, but then collapsed to lows near to £3,000.

Asian technology companies in general were highly sought after with great excitement in the press regarding concepts such as cloud computing, artificial intelligence, machine learning, robotics, autonomous vehicles and 3D machine vision. We believe that the continuing advances in computing power, sensing and networking are increasing the opportunity for technology to become ubiquitous and alter the working and leisure environment for a growing proportion of the world's population.

However, at the end of the first half the excitement had clearly run ahead of the reality and markets were vulnerable to bad news – this was duly delivered in the form of the accelerating US-China trade war, fears of monetary policy tightening, softer demand for smartphones, pc's and servers and weakness in semiconductor prices – particularly memory. Given the hardware skew and cyclical nature of the Asia technology sector, the business models of Asian technology companies were particularly vulnerable.

The worst performing stocks within the Asian portfolio were generally semiconductor companies or capital equipment suppliers to semiconductor companies, for example Wonik IPS, RichWave Technology, Eugene Technology, PSK and Innox saw declines of between 38-54%. The better performing names came from a broader range of business models including software, hosting, payment and internet platforms with four holdings rising over 50%, the best being Bravura – an Australian financial software company – up over 110%. There has been a deliberate effort to diversify the portfolio from an over reliance on the volatile hardware business models prevalent in Korea and Taiwan with an increased emphasis on unearthing new opportunities in other markets such as Australia and Japan.

**EMEA**

The European element of the portfolio has always been small, but over the long term has performed well. Unfortunately, this year has been challenging. BE Semiconductor has provided a total return of £17.4m and remained the biggest holding in the portfolio at the start of 2018, but in 2018 the return was a £5.7m loss. However, the position had been significantly reduced with £17.4m cash and £7.8m profit already realised on share sales by the beginning of April 2018, which significantly reduced the damage. BE Semiconductor is an extremely well-managed company, but is a capital equipment supplier to a cyclical semiconductor industry. There was a major cancellation of an order believed to be in excess of $20m from Apple, but that is the nature of the sector. The stock accounted for a third of the European portfolio at the start of the year, and declined 42%.

The best performing stock in the year was Link Mobility, which benefited from a takeover by private equity. Management are staying with the business, but believe funding for acquisitions will be easier to find through private equity owners. The private equity power has even extended to this Norwegian company.

**OUTLOOK**

Several references have been made to regulatory changes. Metaphorically this is what keeps me awake at night, not the quality of the portfolio, not the US/China trade war, not Brexit, not politics, but the trends in public markets.

If recent trends persist then quoted markets, for small companies anyway, will cease to exist. The private investor will be marginalised, and private equity will own everything. We discuss this challenge ad nauseum. Wise elder counsel tells me the darkest hour is always just before dawn.

*"Asset allocators will realise that P-E valuations have become too high and their returns will deteriorate, and that there might be volatility in public markets but at least there is liquidity and regulated public scrutiny. They will become forced sellers, and public market investors will get bargains. Remember hedge funds were flavour of the month at one time."*

*"The market will adapt to regulatory changes and realise commissions or spreads have to be higher, so that the market can function again and provide liquidity and provide capital for companies. The regulator will realise that it has heaped too much cost throughout the chain of financial advisors, fund managers and brokers at the expense of the poor old private investor that they are trying to protect and become more practical."*

We can but hope.

Nevertheless, we are considering allocating a small portion of the portfolio to private companies because we are aware the market is changing and want to ensure access to the best opportunities.

The good news is that you can make money out of shrinking markets, as has been demonstrated in this fund over the last decade if not the last year. Most importantly of all, the sector continues to offer exciting emerging companies. It is evident to all how pervasive technology change is for the consumer, corporates and Governments alike.

**KATIE POTTS**
19 February 2019

# CLASSIFICATION OF INVESTMENTS

| Classification* | UK % | EMEA % | North America % | Japan & Asia Pacific % | 2018 Total % | 2017 Total % |
|---|---|---|---|---|---|---|
| **OIL & GAS** | **0.4** | **–** | **0.4** | **–** | **0.8** | **1.2** |
| Alternative Energy | 0.4 | – | 0.4 | – | 0.8 | 1.2 |
| **BASIC MATERIALS** | **0.3** | **–** | **–** | **0.2** | **0.5** | **1.1** |
| Chemicals | 0.3 | – | – | 0.2 | 0.5 | 1.1 |
| **INDUSTRIALS** | **7.4** | **–** | **1.7** | **1.1** | **10.2** | **10.1** |
| Construction & Materials | 0.2 | – | 0.1 | – | 0.3 | 0.1 |
| Aerospace & Defence | 0.6 | – | – | – | 0.6 | 0.6 |
| Electronic & Electrical Equipment | 2.9 | – | 1.1 | 0.3 | 4.3 | 4.1 |
| Industrial Engineering | – | – | – | 0.1 | 0.1 | 0.1 |
| Support Services | 3.7 | – | 0.5 | 0.7 | 4.9 | 5.2 |
| **CONSUMER GOODS** | **0.7** | **–** | **0.4** | **–** | **1.1** | **1.7** |
| Household Goods & Home Construction | – | – | – | – | – | 0.2 |
| Leisure Goods | 0.7 | – | 0.4 | – | 1.1 | 1.5 |
| **HEALTH CARE** | **0.9** | **0.1** | **–** | **–** | **1.0** | **1.0** |
| Health Care Equipment & Services | 0.8 | 0.1 | – | – | 0.9 | 0.8 |
| Pharmaceuticals & Biotechnology | 0.1 | – | – | – | 0.1 | 0.2 |
| **CONSUMER SERVICES** | **11.7** | **–** | **0.3** | **0.9** | **12.9** | **13.6** |
| General Retailers | – | – | – | 0.5 | 0.5 | 0.4 |
| Media | 11.6 | – | 0.3 | 0.2 | 12.1 | 12.8 |
| Travel & Leisure | 0.1 | – | – | 0.2 | 0.3 | 0.4 |
| **TELECOMMUNICATIONS** | **1.8** | **–** | **0.6** | **–** | **2.4** | **2.3** |
| Fixed Line Telecommunications | 1.6 | – | 0.3 | – | 1.9 | 1.9 |
| Mobile Telecommunications | 0.2 | – | 0.3 | – | 0.5 | 0.4 |
| **UTILITIES** | **0.3** | **–** | **–** | **–** | **0.3** | **–** |
| Electricity | 0.3 | – | – | – | 0.3 | – |
| **FINANCIALS** | **1.6** | **–** | **0.1** | **0.3** | **2.0** | **0.9** |
| Financial Services | 0.4 | – | 0.1 | 0.3 | 0.8 | 0.3 |
| Equity Investment Instruments | 1.2 | – | – | – | 1.2 | 0.5 |
| Non-equity Investment Instruments | – | – | – | – | – | 0.1 |
| **TECHNOLOGY** | **26.9** | **4.9** | **20.7** | **3.4** | **55.9** | **60.8** |
| Software & Computer Services | 21.8 | 3.1 | 13.0 | 1.8 | 39.7 | 41.7 |
| Technology Hardware & Equipment | 5.1 | 1.8 | 7.7 | 1.6 | 16.2 | 19.1 |
| **TOTAL EQUITIES** (including convertibles and warrants) | **52.0** | **5.0** | **24.2** | **5.9** | **87.1** | **–** |
| Total equities – 2017 (including convertibles and warrants) | 60.3 | 5.7 | 21.5 | 5.2 | – | 92.7 |
| **BONDS** | **–** | **–** | **5.2** | **–** | **5.2** | **3.0** |
| **NET LIQUID ASSETS**** | **3.7** | **1.1** | **2.7** | **0.2** | **7.7** | **4.3** |
| **TOTAL ASSETS** | **55.7** | **6.1** | **32.1** | **6.1** | **100.0** | **–** |
| Total assets – 2017 | 61.8 | 6.2 | 26.7 | 5.3 | – | 100.0 |
| **SHAREHOLDERS' FUNDS** | **55.7** | **6.1** | **32.1** | **6.1** | **100.0** | |
| Shareholders' Funds – 2017 | 61.8 | 6.2 | 26.7 | 5.3 | | 100.0 |
| Number of equity investments (including convertibles and warrants) | 149 | 21 | 69 | 46 | 285 | 271 |

* FTSE Russell Industry Classification Benchmark.
** Cash, current assets and liabilities.

# TOP 20 EQUITY HOLDINGS AS AT 31 DECEMBER 2018

| | |
|---|---|
| £23.1m | VALUATION |
| 2.6% | OF TOTAL ASSETS |
| 3.6% | OF ISSUED SHARE CAPITAL HELD |
| £1.5m | BOOK COST |

GB Group (GBG) offers a series of solutions that help organisations quickly validate and verify the identity and location of their customers. GBG's products are built on an unparalleled breadth of data obtained from over 200 global partners which in conjunction with GBG's innovative technology leads the world in location intelligence, detects fraud and enables GBG to verify the identity of 4.4 billion people globally. GBG is headquartered in the UK, with over 900 team members across 18 countries. They work with clients in 79 countries, including some of the best-known businesses around the world, ranging from US e-commerce giants to Asia's biggest banks and European household brands.

| | |
|---|---|
| £20.6m | VALUATION |
| 2.3% | OF TOTAL ASSETS |
| 1.5% | OF ISSUED SHARE CAPITAL HELD |
| £1.2m | BOOK COST |

Diploma is a group of specialised distribution businesses serving industries with long term growth potential and with the opportunity for sustainable superior margins through the quality of customer service, depth of technical support and value-adding activities. The three sectors the company focuses on are life sciences, seals and controls.

| | |
|---|---|
| £18.4m | VALUATION |
| 2.0% | OF TOTAL ASSETS |
| 4.6% | OF ISSUED SHARE CAPITAL HELD |
| £2.4m | BOOK COST |

Next Fifteen Communications is a family of 18 marketing businesses spanning digital content, PR, consumer, technology, marketing software, market research, public affairs and policy communications. Founded in 1981, Next 15 are centred on the technology of marketing: data, insight, analytics, apps, content platforms and content itself.

| | |
|---|---|
| £15.4m | VALUATION |
| 1.7% | OF TOTAL ASSETS |
| 4.6% | OF ISSUED SHARE CAPITAL HELD |
| £5.1m | BOOK COST |

Attunity is a leading provider of data integration and big data management software solutions that enable availability, delivery and management of data across heterogeneous enterprise platforms, organisations and the cloud. Attunity's software solutions include data replication and distribution, test data management, change data capture (CDC), data connectivity, enterprise file replication (EFR), managed file transfer (MFT), data warehouse automation, data usage analytics and cloud data delivery. Attunity has supplied innovative software solutions to its enterprise-class customers for over 20 years and has successful deployments at thousands of organisations worldwide. Attunity provides software directly and indirectly through a number of partners such as Microsoft, Oracle, IBM and Hewlett Packard Enterprise.

| | |
|---|---|
| £14.6m | VALUATION |
| 1.6% | OF TOTAL ASSETS |
| 2.3% | OF ISSUED SHARE CAPITAL HELD |
| £1.8m | BOOK COST |

Craneware is the leader in automated Value Cycle solutions that help US Healthcare provider organisations discover, convert and optimise assets to achieve best clinical outcomes and financial performance. Founded in 1999, Craneware is headquartered in Edinburgh, Scotland with offices in Atlanta and Pittsburgh employing over 320 staff. Craneware's market-driven, SaaS solutions normalise disparate data sets, bringing in up-to-date regulatory and financial compliance data to deliver value at the points where clinical and operational data transform into financial transactions, creating actionable insights that enable informed tactical and strategic decisions.

| | |
|---|---|
| £12.9m | VALUATION |
| 1.4% | OF TOTAL ASSETS |
| 0.3% | OF ISSUED SHARE CAPITAL HELD |
| £2.0m | BOOK COST |

Mellanox Technologies is a leading supplier of end-to-end Ethernet and InfiniBand smart interconnect solutions and services for servers and storage. Mellanox interconnect solutions increase datacentre efficiency by providing the highest throughput and lowest latency, delivering data faster to applications and unlocking system performance capability. Mellanox offers a choice of fast interconnect products: adapters, switches, software and silicon that accelerate application runtime and maximise business results for a wide range of markets including high performance computing, enterprise data centres, Web 2.0, cloud, storage and financial services.

| | |
|---|---|
| £12.8m | VALUATION |
| 1.4% | OF TOTAL ASSETS |
| 1.6% | OF ISSUED SHARE CAPITAL HELD |
| £4.5m | BOOK COST |

Radware is a global leader of cyber security and application delivery solutions for physical, cloud, and software defined data centres. Its award-winning solutions portfolio secures the digital experience by providing infrastructure, application, and corporate IT protection and availability services to enterprises globally. Radware's solutions empower more than 12,500 enterprise and carrier customers worldwide to adapt to market challenges quickly, maintain business continuity and achieve maximum productivity while keeping costs down.

| | |
|---|---|
| £11.9m | VALUATION |
| 1.3% | OF TOTAL ASSETS |
| 0.4% | OF ISSUED SHARE CAPITAL HELD |
| £1.6m | BOOK COST |

Pegasystems is the leader in software for customer engagement and operational excellence. Pega's adaptive, cloud-architected software – built on its unified Pega Platform – empowers people to rapidly deploy and easily extend and change applications to meet strategic business needs. Over its 35-year history, Pega has delivered award-winning capabilities in CRM and digital process automation (DPA) powered by advanced artificial intelligence and robotic automation, to help the world's leading brands achieve breakthrough business results.

| | |
|---|---|
| £11.9m | VALUATION |
| 1.3% | OF TOTAL ASSETS |
| 3.0% | OF ISSUED SHARE CAPITAL HELD |
| £6.1m | BOOK COST |

Future is an international media group, organised into two divisions, Media and Magazines. The Media division focuses on being at the forefront of digital innovation with three complementary revenue streams: eCommerce, events and digital advertising. It operates in a number of sectors, including the growing technology and games markets, and has a number of leading brands, including TechRadar, PC Gamer, GamesRadar+, The Photography Show, Generate and Golden Joysticks. The Magazine division creates specialist magazines and bookazines, with 60 magazines and over 430 bookazines published a year, with a total global circulation of over one million. The Magazine portfolio spans technology, games and entertainment, music, creative and photography, field sports, knowledge and home interest verticals. Its titles include T3, Total Film, How It Works, Edge and All About History.

| | |
|---|---|
| £11.8m | VALUATION |
| 1.3% | OF TOTAL ASSETS |
| 4.8% | OF ISSUED SHARE CAPITAL HELD |
| £4.6m | BOOK COST |

M&C Saatchi is a global marketing services business working for clients across a wide variety of industry sectors. The company was founded in 1995. Starting with a strong base in the UK and Australia, M&C Saatchi have added new agencies and disciplines in Asia, USA and Europe.

| | |
|---|---|
| £11.7m | VALUATION |
| 1.3% | OF TOTAL ASSETS |
| 1.0% | OF ISSUED SHARE CAPITAL HELD |
| £2.3m | BOOK COST |

Telecom Plus, which owns and operates the Utility Warehouse brand, is the UK's only fully integrated provider of a wide range of competitively priced utility services spanning the communications, energy and insurance markets. Customers ('Members') benefit from the convenience of a single monthly bill, consistently good value across all their utilities and superior levels of customer service. The company does not advertise, relying instead on 'word of mouth' recommendation by existing satisfied Members and a network of part-time distributors ('Partners') in order to grow its market share.

# TOP 20 EQUITY HOLDINGS AS AT 31 DECEMBER 2018 CONTINUED

| | |
|---|---|
| £11.4m | VALUATION |
| 1.3% | OF TOTAL ASSETS |
| 2.8% | OF ISSUED SHARE CAPITAL HELD |
| £3.0m | BOOK COST |

YouGov is an international data and analytics group. The core offering of opinion data is derived from a participative panel of 5 million people worldwide. This continuous stream of data is combined with deep research expertise and broad industry experience into a systematic research and marketing platform. The suite of syndicated, proprietary data products includes YouGov BrandIndex, the daily brand perception tracker, and YouGov Profiles, a planning and segmentation tool. YouGov Omnibus provides a fast and cost-effective service for obtaining answers to research questions from both national and selected samples. With 30 offices in 20 countries and panel members in 38 countries, YouGov has one of the world's top ten international market research networks.

| | |
|---|---|
| £11.1m | VALUATION |
| 1.2% | OF TOTAL ASSETS |
| 5.9% | OF ISSUED SHARE CAPITAL HELD |
| £5.9m | BOOK COST |

BATM Advanced Communications is a leading provider of real-time technologies with two divisions providing networking and cyber solutions and biomedical systems. These two divisions have been built on the creation of strong intellectual property backed by strong patents. This is the foundation for the development of BATM's market-leading innovative and cost-effective solutions in the divisions' respective fields. The Bio-Medical Division is focused on becoming a leading provider of diagnostic laboratory equipment as well as innovative products to treat biological pathogenic waste in the medical, agricultural and pharmaceutical industries. BATM is growing its Networking and Cyber Division to be the worldwide leader of Carrier Ethernet and MPLS access solutions, mainly targeting Tier 1 telecom operators in developed markets. This industry is undergoing a transition to more cloud-based solutions and software defined products, and BATM's Networking and Cyber Division has shifted its product focus to address these trends.

| | |
|---|---|
| £10.5m | VALUATION |
| 1.2% | OF TOTAL ASSETS |
| 2.1% | OF ISSUED SHARE CAPITAL HELD |
| £5.8m | BOOK COST |

IQE is the leading global supplier of advanced compound semiconductor wafers. These wafers are atomically engineered to provide IQE's customers with the materials from which they produce high performance wireless, photonic and electronic devices or 'chips'. It is IQE's epitaxial layer processes that enable chips to operate at the high frequencies (radio frequencies or RF) that are used for all forms of wireless communications. IQE's 'epi' processes also manufacture materials that enable the conversion of energy to light or light to energy for sensing, lighting and power generation technologies. IQE produces materials which can emit or detect/receive light from the infrared, through the visible and into the ultraviolet range of wavelengths. IQE's products cover a diverse range of applications, supported by an innovative outsourced foundry services portfolio that allows the Group to provide a 'one stop shop' for the contract wafer manufacturing needs of the world's leading semiconductor manufacturers.

| | |
|---|---|
| £10.0m | VALUATION |
| 1.1% | OF TOTAL ASSETS |
| 1.5% | OF ISSUED SHARE CAPITAL HELD |
| £3.0m | BOOK COST |

Boingo Wireless' footprint of distributed antenna systems (DAS), Wi-Fi and small cells reaches more than a billion people annually, making Boingo one of the largest providers of indoor wireless networks. Boingo connects people at airports, stadiums, military bases, convention centres and commercial properties.

| | |
|---|---|
| £9.9m | VALUATION |
| 1.1% | OF TOTAL ASSETS |
| 0.6% | OF ISSUED SHARE CAPITAL HELD |
| £0.9m | BOOK COST |

Descartes Systems is a leader in providing on-demand, software-as-a-service solutions focused on improving the productivity, performance and security of logistics-intensive businesses. Customers use Descartes' modular, software-as-a-service solutions to route, schedule, track and measure delivery resources; plan, allocate and execute shipments; rate, audit and pay transportation invoices; access global trade data; file customs and security documents for imports and exports; and complete numerous other logistics processes by participating in the world's largest, collaborative multimodal logistics community. Descartes' headquarters are in Waterloo, Ontario, Canada and they have offices and partners around the world.

| | |
|---|---|
| £9.9m | VALUATION |
| 1.1% | OF TOTAL ASSETS |
| 1.0% | OF ISSUED SHARE CAPITAL HELD |
| £1.7m | BOOK COST |

Silicon Motion Technology is a global leader and pioneer in developing NAND flash controller ICs for solid-state storage devices. Key products are controllers used in embedded storage products such as SSDs and eMMC+UFS, as well as in expandable storage products such as memory cards and USB flash drives. Products are widely used in consumer devices such as smartphones, tablets and PCs and for industrial, enterprise, commercial and other applications. Silicon Motion ship over 750 million NAND controllers annually and have shipped over five billion NAND controllers in the last ten years. They also supply specialised high-performance hyperscale data centre and industrial SSD solutions. Customers include most of the NAND flash vendors, storage device module makers, and leading OEMs. Silicon Motion was founded in 1995 in San Jose, California and now operates from corporate offices in Hong Kong, Taiwan and the US, with design centres and sales offices in Taiwan, Korea, China, Hong Kong, Japan and the US.

| | |
|---|---|
| £9.8m | VALUATION |
| 1.1% | OF TOTAL ASSETS |
| 0.8% | OF ISSUED SHARE CAPITAL HELD |
| £1.6m | BOOK COST |

Euromoney Institutional Investor was founded in 1969 by Sir Patrick Sergeant, then City editor of the Daily Mail. Since that time, the business, which was launched to reflect the growth in global capital flows, has flourished alongside the development of financial markets. Euromoney Institutional Investor PLC ('Euromoney') is a global, multi-brand information business which provides critical data, price reporting, insight, analysis and must-attend events to financial services, commodities, telecoms and legal markets. The portfolio includes brands such as Euromoney, Institutional Investor, BCA Research, Ned Davis Research, Metal Bulletin, American Metal Market, Insurance Insider, Mining INDABA and IJ Global among others. Euromoney's strategy is to recycle capital towards ever-higher-quality businesses. Euromoney is now mostly what they describe as a 2.0 information business, focused on customer-centric, digital, subscription businesses and networking events. These types of business will continue to be important but Euromoney are also looking to invest in B2B 3.0 businesses which are defined as operating at the centre of a customer's industry, offering products deeply embedded in its customers' workflow and helping customers to become more efficient and to find solutions to opportunities and threats they face.

| | |
|---|---|
| £8.9m | VALUATION |
| 1.0% | OF TOTAL ASSETS |
| 11.5% | OF ISSUED SHARE CAPITAL HELD |
| £1.9m | BOOK COST |

ZOO Digital is a leading provider of localisation and media production services for the entertainment industry. Using its own revolutionary technology, ZOO delivers cloud-based subtitling and dubbing solutions to simplify the management of global distribution operations for creative organisations.

| | |
|---|---|
| £8.3m | VALUATION |
| 0.9% | OF TOTAL ASSETS |
| 7.4% | OF ISSUED SHARE CAPITAL HELD |
| £4.9m | BOOK COST |

Idox is the leading applications provider to UK local government for core functions relating to land, people and property, such as its market leading planning systems and election management software. Over 90% of UK local authorities are now customers. Idox provides public sector organisations with tools to manage information and knowledge, documents, content, business processes and workflow as well as connecting directly with the citizen via the web, and providing elections management solutions. Idox delivers engineering document control, project collaboration and facility management applications to many leading companies in industries such as oil & gas, architecture and construction, mining, utilities, pharmaceuticals and transportation in North America and around the world.

# DETAILED LIST OF INVESTMENTS

## At 31 December 2018

Ordinary or common shares unless otherwise stated.

| Classification | | Name | Value £'000 | % |
|---|---|---|---|---|
| **UNITED KINGDOM** | | | | |
| Alternative Energy | ● | Ilika | 834 | |
| | ● | ITM Power | 2,691 | |
| | | | **3,525** | **0.4** |
| Chemicals | ● | Applied Graphene Materials | 1,568 | |
| | ● | Haydale Graphene Industries | 108 | |
| | ● | Versarien | 980 | |
| | | | **2,656** | **0.3** |
| Construction & Materials | ● | Accsys Technologies | **1,530** | **0.2** |
| Aerospace & Defence | ● | Cohort | 5,004 | |
| | ● | Velocity Composites | 329 | |
| | | | **5,333** | **0.6** |
| Electronic & Electrical Equipment | | Discoverie | 6,151 | |
| | ● | Elektron Technology | 4,145 | |
| | ● | Feedback | 160 | |
| | ● | Gooch & Housego | 2,278 | |
| | ● | Microsaic Systems | 274 | |
| | | Oxford Instruments | 1,112 | |
| | ● | ProPhotonix | 175 | |
| | ● | Thruvision | 4,062 | |
| | ● | Volex | 4,929 | |
| | | Xaar | 1,418 | |
| | | XP Power | 1,713 | |
| | | | **26,417** | **2.9** |
| Support Services | ● | 1Spatial | 1,304 | |
| | ● | Boku | 1,448 | |
| | | Diploma | 20,584 | |
| | ● | Freshwater UK | 113 | |
| | ● | Maintel | 3,619 | |
| | ● | Science Group | 1,998 | |
| | ● | Spectra Systems | 3,072 | |
| | ● | Synectics | 666 | |
| | ● | Water Intelligence | 893 | |
| | | | **33,697** | **3.7** |
| Household Goods & Home Construction | ● | PhotonStar LED | **7** | **0.0** |
| Leisure Goods | ● | Focusrite | 2,576 | |
| | ● | Frontier Developments | 3,153 | |
| | ● | Team17 | 475 | |
| | | | **6,204** | **0.7** |
| Health Care Equipment & Services | ● | Deltex Medical | 168 | |
| | ● | Kromek | 3,574 | |
| | ● | LiDCO | 700 | |
| | ● | Scientific Digital Imaging | 2,580 | |
| | | | **7,022** | **0.8** |
| Pharmaceuticals & Biotechnology | ● | C4X Discovery | **975** | **0.1** |
| General Retailers | ● | 7Digital | **231** | **0.0** |
| Media | ● | Audioboom | 671 | |
| | ● | BE Heard Group | 445 | |
| | | Bloomsbury Publishing | 3,010 | |
| | ● | Bonhill | 2,609 | |
| | | Centaur Media | 2,025 | |
| | ● | Ebiquity | 2,778 | |
| | | Euromoney Institutional Investor | 9,751 | |

● denotes AIM stock

● denotes unlisted security

# DETAILED LIST OF INVESTMENTS CONTINUED

## At 31 December 2018

| Classification | | Name | Value £'000 | % |
|---|---|---|---|---|
| **UNITED KINGDOM** continued | | Future | 11,879 | |
| | ● | GlobalData | 2,803 | |
| | | GoCompare | 834 | |
| | ● | Jaywing | 475 | |
| | ● | M&C Saatchi | 11,830 | |
| | ● | Mirriad Advertising | 158 | |
| | ● | Mission Marketing | 3,005 | |
| | ● | Next Fifteen Communications | 18,439 | |
| | ● | OnTheMarket | 533 | |
| | | Quarto | 1,323 | |
| | ● | Reach4entertainment Enterprise | 1,431 | |
| | | S4 Capital | 3,421 | |
| | ● | Taptica | 1,545 | |
| | ● | ULS Technology | 3,230 | |
| | | Wilmington | 4,351 | |
| | ● | XLMedia | 2,847 | |
| | ● | YouGov | 11,444 | |
| | ● | Zinc Media | 1,672 | |
| | ● | Zinc Media Convertible Preference Shares | 673 | |
| | | | **103,182** | **11.4** |
| Travel & Leisure | ● | Ten Lifestyle Group | **709** | **0.1** |
| Fixed Line Telecommunications | ● | Manx Telecom | 2,687 | |
| | | Telecom Plus | 11,678 | |
| | | | **14,365** | **1.6** |
| Mobile Telecommunications | ● | Gamma Communications | **1,415** | **0.2** |
| Electricity | ● | SIMEC Atlantis Energy | **2,751** | **0.3** |
| Financial Services | ● | Fairfx | 1,095 | |
| | | Integrafin | 1,259 | |
| | ● | Tungsten | 1,053 | |
| | | | **3,407** | **0.4** |
| Equity Investment Instruments | | Gore Street Energy Storage Fund | 1,900 | |
| | ● | Herald Venture II | 2,694 | |
| | ● | HIML | 4,047 | |
| | | Hipgnosis Songs Fund | 1,065 | |
| | ● | KRM22 | 1,139 | |
| | | | **10,845** | **1.2** |
| Software & Computer Services | ● | Access Intelligence | 1,992 | |
| | ● | Albert Technologies | 383 | |
| | ● | Appscatter | 383 | |
| | ● | ATTRAQT | 2,569 | |
| | | Avast | 5,073 | |
| | ● | Bango | 6,818 | |
| | ● | Bigblu Broadband | 3,891 | |
| | ● | Blue Prism | 592 | |
| | ● | Brady | 4,946 | |
| | ● | Brave Bison | 420 | |
| | ● | Business Control Solutions | 699 | |
| | ● | Celoxica | 217 | |
| | ● | CentralNic | 4,544 | |
| | ● | Cloudcall | 1,250 | |
| | ● | Corero Network Security | 3,637 | |
| | ● | Craneware | 14,616 | |
| | ● | D4T4 Solutions | 4,932 | |
| | ● | Dillistone | 795 | |
| | ● | Dotdigital | 5,823 | |
| | ● | Eagle Eye Solutions Group | 206 | |

# **DETAILED LIST OF INVESTMENTS** CONTINUED

## At 31 December 2018

| Classification | | Name | Value £'000 | % |
|---|---|---|---|---|
| **UNITED KINGDOM** continued | ● | Earthport | 2,176 | |
| | ● | Eckoh | 5,974 | |
| | ● | eServGlobal | 1,215 | |
| | ● | EU Supply | 470 | |
| | | FDM | 2,660 | |
| | ● | First Derivatives | 5,449 | |
| | ● | Forbidden Technologies | 581 | |
| | ● | Fusionex International | 1,402 | |
| | ● | GB Group | 23,078 | |
| | ● | Getbusy | 857 | |
| | | Gresham Technologies | 2,116 | |
| | ● | Ideagen | 4,263 | |
| | ● | Idox | 8,346 | |
| | ● | i-nexus Global | 891 | |
| | ● | Intercede | 533 | |
| | | Kainos | 3,472 | |
| | ● | Location Sciences | 456 | |
| | ● | LoopUp | 7,140 | |
| | ● | Maestrano | 360 | |
| | | Microgen | 8,155 | |
| | | NCC | 5,259 | |
| | ● | Osirium Technologies | 619 | |
| | ● | Oxford Metrics | 5,388 | |
| | ● | Parity | 212 | |
| | ● | PCI-PAL | 170 | |
| | ● | Pelatro | 1,047 | |
| | ● | Sanderson | 435 | |
| | ● | SciSys | 3,592 | |
| | | SDL | 1,411 | |
| | ● | SimiGon | 606 | |
| | ● | SmartSpace Software | 1,553 | |
| | | Sophos | 3,384 | |
| | ● | Statpro | 8,162 | |
| | ● | Sysgroup | 642 | |
| | ● | Tribal | 3,590 | |
| | ● | Wandisco | 4,500 | |
| | ● | ZOO Digital | 8,902 | |
| | | | **192,852** | **21.4** |
| Technology Hardware & Equipment | ● | Amino Technologies | 1,224 | |
| | | BATM Advanced Communications | 11,092 | |
| | | CML Microsystems | 4,420 | |
| | ● | Concurrent Technologies | 523 | |
| | ● | CyanConnode | 1,153 | |
| | ● | Ethernity Networks | 107 | |
| | ● | Frontier Smart Technologies | 1,263 | |
| | ● | Intechnology | 213 | |
| | ● | IQE | 10,538 | |
| | ● | LightwaveRF | 467 | |
| | ● | MTI Wireless Edge | 506 | |
| | ● | Northamber | 886 | |
| | ● | Quixant | 2,181 | |
| | ● | Seeing Machines | 3,315 | |
| | | Spirent Communications | 4,736 | |
| | ● | Telit Communications | 3,008 | |
| | | | **45,632** | **5.1** |
| | | **TOTAL UNITED KINGDOM EQUITIES** | **462,755** | **51.4** |

● denotes AIM stock

● denotes unlisted security

# DETAILED LIST OF INVESTMENTS CONTINUED
## At 31 December 2018

| Classification | Name | | Value £'000 | % |
|---|---|---|---|---|
| **EUROPE, MIDDLE EAST AND AFRICA (EMEA)** | | | | |
| Electronic & Electrical Equipment | Ekinops | France | **593** | **0.0** |
| Health Care Equipment & Services | EOS Imaging | France | **601** | **0.1** |
| Software & Computer Services | ATEME | France | 568 | |
| | B3 Consulting | Sweden | 1,806 | |
| | CAST | France | 1,727 | |
| | Data Respons | Norway | 3,025 | |
| | Datalex | Ireland | 2,065 | |
| | Devoteam | France | 3,284 | |
| | Efecte | Finland | 867 | |
| | Esker | France | 4,014 | |
| | Invision | Germany | 611 | |
| | Isra Vision | Germany | 2,627 | |
| | MailUp | Italy | 368 | |
| | Oxatis | France | 440 | |
| | Sidetrade | France | 1,794 | |
| | Sword Group | France | 3,123 | |
| | WALLIX | France | 1,573 | |
| | | | **27,892** | **3.1** |
| Technology Hardware & Equipment | ADVA Optical Networking | Germany | 2,827 | |
| | BE Semiconductor Industries | Netherlands | 8,305 | |
| | Nordic Semiconductor | Norway | 3,240 | |
| | X-FAB Silicon Foundries | Belgium | 1,906 | |
| | | | **16,278** | **1.8** |
| | **TOTAL EMEA EQUITIES** | | **45,364** | **5.0** |
| **NORTH AMERICA** | | | | |
| Alternative Energy | Ballard Power Systems | | 1,200 | |
| | Hydrogenics | | 2,136 | |
| | | | **3,336** | **0.4** |
| Construction & Materials | Tecogen | | **914** | **0.1** |
| Electronic & Electrical Equipment | Celestica | | 2,062 | |
| | Fabrinet | | 6,681 | |
| | RADCOM | | 936 | |
| | | | **9,679** | **1.1** |
| Support Services | Asure Software | | 83 | |
| | Imperva | | 2,184 | |
| | Issuer Direct | | 801 | |
| | Pluralsight | | 1,710 | |
| | | | **4,778** | **0.5** |
| Leisure Goods | Akoustis Technologies | | 2,256 | |
| | Fitbit | | 1,462 | |
| | | | **3,718** | **0.4** |
| Media | Yelp | | **2,196** | **0.3** |
| Fixed Line Telecommunications | Pareteum | | **2,715** | **0.3** |
| Mobile Telecommunications | Iridium Communications | | **2,604** | **0.3** |
| Financial Services | Safeguard Scientifics | | **751** | **0.1** |
| Software & Computer Services | Alteryx | | 4,200 | |
| | Amber Road | | 5,869 | |
| | Attunity | | 15,351 | |
| | Boingo Wireless | | 9,990 | |
| | Bottomline Technologies | | 4,849 | |
| | Brightcove | | 2,598 | |
| | CyberArk Software | | 2,384 | |
| | Descartes Systems | | 9,904 | |

# DETAILED LIST OF INVESTMENTS CONTINUED

## At 31 December 2018

| Classification | Name | | Value £'000 | % |
|---|---|---|---|---|
| **NORTH AMERICA** continued | Digimarc | | 113 | |
| | Five9 | | 8,095 | |
| | Gridsum* | | 166 | |
| | Hortonworks | | 4,635 | |
| | Kinaxis | | 1,358 | |
| | LivePerson | | 7,402 | |
| | Manhattan Associates | | 1,512 | |
| | Materialise* | | 1,364 | |
| | Meet Group | | 1,631 | |
| | Mimecast | | 5,275 | |
| | Model N | | 1,152 | |
| | OneSpan | | 2,030 | |
| | Pegasystems | | 11,914 | |
| | Qualys | | 5,116 | |
| | Rapid7 | | 1,272 | |
| | SITO Mobile | | 89 | |
| | SPS Commerce | | 3,229 | |
| | Support.com | | 277 | |
| | TOP Image Systems | | 188 | |
| | Varonis Systems | | 5,096 | |
| | Veritone | | 268 | |
| | | | **117,327** | **13.0** |
| Technology Hardware & Equipment | ACM Research | | 1,273 | |
| | Adesto Technologies | | 1,485 | |
| | Aehr Test Systems | | 228 | |
| | Aquantia | | 1,135 | |
| | AXT | | 512 | |
| | Blackline Safety | | 345 | |
| | ● Blackline Safety Restricted | | 244 | |
| | Ceva | | 5,518 | |
| | Chipmos Technologies* | | 1,095 | |
| | Everspin Technologies | | 1,452 | |
| | Harmonic | | 1,848 | |
| | Inphi | | 3,279 | |
| | Intellicheck | | 529 | |
| | Lantronix | | 1,629 | |
| | Mellanox Technologies | | 12,929 | |
| | Neophotonics | | 712 | |
| | nLIGHT | | 349 | |
| | One Stop Systems | | 277 | |
| | Quantenna Communications | | 3,169 | |
| | Radware | | 12,823 | |
| | Silicom | | 1,364 | |
| | Silicon Motion Technology* | | 9,882 | |
| | Super Micro Computer | | 2,014 | |
| | Tower Semiconductor | | 1,005 | |
| | ViaSat | | 4,624 | |
| | | | **69,720** | **7.7** |
| | **TOTAL NORTH AMERICA EQUITIES** | | **217,738** | **24.2** |
| **ASIA PACIFIC** | | | | |
| Chemicals | SK Materials | South Korea | 711 | |
| | Soulbrain | South Korea | 1,187 | |
| | | | **1,898** | **0.2** |

* American Depositary Receipts – certificates representing shares in the stock, issued by a US bank, denominated and paying dividends in US dollars.

● *denotes unlisted security*

# DETAILED LIST OF INVESTMENTS CONTINUED
## At 31 December 2018

| Classification | Name | | Value £'000 | % |
|---|---|---|---|---|
| **ASIA PACIFIC** continued | | | | |
| Electronic & Electrical Equipment | CyberPower Systems | Taiwan | 587 | |
| | Tripod Technology | Taiwan | 1,697 | |
| | Uju Electronics | South Korea | 628 | |
| | | | **2,912** | **0.3** |
| Industrial Engineering | Rhipe | Australia | **676** | **0.1** |
| Support Services | 51job* | China | 4,598 | |
| | Mainstream | Australia | 564 | |
| | Praemium | Australia | 1,044 | |
| | | | **6,206** | **0.7** |
| General Retailers | China Distance Education* | China | 1,074 | |
| | Momo | Taiwan | 1,488 | |
| | PChome Online | Taiwan | 1,614 | |
| | Redbubble | Australia | 521 | |
| | | | **4,697** | **0.5** |
| Media | Domain Holdings | Australia | 1,479 | |
| | Hong Kong Economic Times | Hong Kong | 399 | |
| | OPT | Japan | 306 | |
| | | | **2,184** | **0.2** |
| Travel & Leisure | Webjet | Australia | **2,070** | **0.2** |
| Financial Services | Afterpay Touch | Australia | 1,302 | |
| | Money Forward | Japan | 917 | |
| | | | **2,219** | **0.3** |
| Software & Computer Services | ARQ | Australia | 208 | |
| | Audinate | Australia | 116 | |
| | Bigtincan | Australia | 775 | |
| | Bravura Solutions | Australia | 2,039 | |
| | Cafe24 | South Korea | 848 | |
| | Chanjet Information** | China | 1,183 | |
| | Family Zone Cyber Safety | Australia | 899 | |
| | Freelancer | Australia | 916 | |
| | Gabia | South Korea | 1,018 | |
| | Kingdee International Software | China | 6,083 | |
| | Kinx | South Korea | 979 | |
| | MSL Solutions | Australia | 425 | |
| | Xref | Australia | 481 | |
| | | | **15,970** | **1.8** |
| Technology Hardware & Equipment | Advantech | Taiwan | 1,297 | |
| | Ardentec | Taiwan | 927 | |
| | Chicony Electronics | Taiwan | 640 | |
| | Eugene Technology | South Korea | 446 | |
| | Hanmi Semiconductor | South Korea | 547 | |
| | Innox Advanced Materials | South Korea | 759 | |
| | Kulicke & Soffa | Singapore | 1,109 | |
| | King Yuan Electronics | Taiwan | 1,381 | |
| | Parade Technologies | Taiwan | 1,339 | |
| | PSK | South Korea | 1,081 | |
| | Realtek Semiconductor | Taiwan | 3,358 | |
| | RichWave Technology | Taiwan | 901 | |
| | Sercomm | Taiwan | 369 | |
| | Wonik IPS | South Korea | 419 | |
| | | | **14,573** | **1.6** |
| | **TOTAL ASIA PACIFIC EQUITIES** | | **53,405** | **5.9** |

* American Depositary Receipts – certificates representing shares in the stock, issued by a US bank, denominated and paying dividends in US dollars.
** H Shares – issued by companies incorporated in the People's Republic of China and listed on the Hong Kong Stock Exchange.

# DETAILED LIST OF INVESTMENTS CONTINUED

## At 31 December 2018

| Classification | | Name | Value £'000 | % |
|---|---|---|---|---|
| **CONVERTIBLE LOAN STOCKS HAVING AN ELEMENT OF EQUITY** | | | | |
| | ● | BE Heard Group 8% Convertible 29 Nov 2023 | 160 | |
| | ● | EU Supply 10% Convertible 31 Dec 2020 | 250 | |
| | ● | Intercede 8% Convertible 31 Dec 2021 | 375 | |
| | ● | Zinc Media Convertible Variable Rate Bank Loan 31 Dec 2020 | 1,000 | |
| | ● | Zinc Media Convertible Variable Rate Loan 31 Dec 2020 | 292 | |
| | ● | Zinc Media 8% Loan 31 Dec 2020 | 600 | |
| | ● | ZOO Digital 7.5% Unsecured Convertible Loan Stock 31 Oct 2020 | 2,956 | |
| | | **TOTAL CONVERTIBLE LOAN STOCKS HAVING AN ELEMENT OF EQUITY** | **5,633** | **0.6** |
| **Total Equity Investments** | | | **784,895** | **87.1** |
| *Fixed Interest* | | US Treasury Stock 1.75% 30 Sep 2019 | 38,972 | |
| | | US Treasury Stock 0.875% 15 Apr 2019 | 7,813 | |
| | | **TOTAL FIXED INTEREST** | **46,785** | **5.2** |
| **Total Investments** | | | **831,680** | **92.3** |
| Net Liquid Assets* | | | 69,474 | 7.7 |
| **Total Assets At Market Value** | | | **901,154** | **100.0** |

* Cash, current assets and liabilities

● denotes unlisted security

## LONG TERM PERFORMANCE

# Steady and sustainable growth

The Company, founded in 1994 by Katie Potts, raised an initial £65m to invest in the UK and continental European TMT sector. Warrants were issued to initial investors on a 1 for 5 basis. In 1996 a further £30m was raised to globalise the fund, thus bringing the total outside capital to £95m. Since 1996 no new capital has been raised, and the warrants have been repurchased or converted into ordinary shares.

The Company has operated an opportunistic buyback policy, which has offered large holders liquidity and helped to create value for existing shareholders. Since inception, the Company has completed buybacks to the value of £118m bringing the net outside capital to negative £23m. Over the history of the fund, net asset value per share on a total return basis has grown by 1,308.6% in capital terms or 11.2% on an annualised basis.

NAV PER SHARE TOTAL RETURN SINCE INCEPTION

**+1,308.6%**

ANNUALISED NAV PER SHARE TOTAL RETURN SINCE INCEPTION

**+11.2%**

### CAPITAL SINCE INCEPTION

| At 31 December | Total assets £'000 | Bank loans £'000 | Shareholders' funds £'000 | Number of shares in issue '000 | Diluted net asset value per share* p | Share price p | (Discount)/ premium † % |
|---|---|---|---|---|---|---|---|
| ≠ Inception | 64,107 | – | 64,107 | 65,000 | 98.72 | 90.90◊ | (7.9) |
| 1994 | 60,823 | – | 60,823 | 65,000 | 93.57 | 94.60 | 1.1 |
| ±1995 | 89,689 | – | 89,689 | 65,000 | 132.36 § | 127.00 | (4.0) |
| 1996 | 130,055 | – | 130,055 | 82,894 | 150.88 § | 136.00 | (9.9) |
| 1997 | 147,424 | – | 147,424 | 82,896 | 171.80 | 136.15 | (20.8) |
| 1998 | 170,982 | – | 170,982 | 82,901 | 201.70 | 161.50 | (19.9) |
| 1999 | 432,620 | (3,343) | 429,277 | 82,961 | 494.22 | 511.10 | 3.4 |
| 2000 | 378,607 | (3,233) | 375,374 | 83,874 | 431.43 | 491.00 | 13.8 |
| 2001 | 275,624 | (2,892) | 272,732 | 84,454 | 314.53 | 306.00 | (2.7) |
| 2002 | 199,900 | (22,310) | 177,590 | 84,475 | 206.68 | 177.00 | (14.4) |
| 2003 | 350,209 | (29,325) | 320,884 | 87,807 | 365.44 | 325.25 | (11.0) |
| # 2004 | 356,874 | (24,663) | 332,211 | 87,556 | 379.43 | 322.75 | (14.9) |
| 2005 | 358,293 | – | 358,293 | 87,556 | 409.22 | 379.75 | (7.2) |
| 2006 | 401,228 | (20,000) | 381,228 | 86,556 | 435.41 | 383.50 | (11.9) |
| 2007 | 343,497 | – | 343,497 | 86,971 | 394.96 | 312.00 | (21.0) |
| 2008 | 275,789 | (65,079)‡ | 210,710 | 83,408 | 252.63 | 184.00 | (27.2) |
| 2009 | 397,194 | (56,298)‡ | 340,896 | 81,053 | 420.58 | 337.75 | (19.7) |
| 2010 | 533,499 | (58,937)‡ | 474,562 | 79,913 | 593.85 | 483.00 | (18.7) |
| 2011 | 519,656 | (70,357)‡ | 449,299 | 79,698 | 563.75 | 455.00 | (19.3) |
| 2012 | 572,243 | (70,297)‡ | 501,946 | 79,323 | 632.78 | 513.00 | (18.9) |
| 2013 | 662,538 | (38,935)‡ | 623,603 | 77,680 | 802.79 | 685.00 | (14.7) |
| 2014 | 667,450 | (38,534)‡ | 628,917 | 77,340 | 813.19 | 659.00 | (19.0) |
| 2015 | 709,139 | (38,002)‡ | 671,137 | 76,112 | 881.78 | 745.25 | (15.5) |
| 2016 | 816,414 | (25,000) | 791,414 | 73,062 | 1,083.21 | 882.50 | (18.5) |
| 2017 | 966,650 | – | 966,650 | 70,308 | 1,374.88 | 1,171.00 | (14.8) |
| **2018** | **901,154** | – | **901,154** | **68,902** | **1,307.89** | **1,075.00** | **(17.8)** |

* The diluted net asset value per ordinary share figures have been calculated in accordance with FRS 102 (2015-2018), FRS 22 (2008-2014), FRS 14 (1995-2007).
† (Discount)/premium is the difference between Herald's quoted share price and its underlying diluted net asset value.
≠ Inception date 16 February 1994. 100p was shareholders' subscription price before launch costs of 1.3p.
◊ 90.9p is the capital gains tax (CGT) base subscription price for shareholders adjusting for warrants which were issued on a 1 for 5 basis. The CGT base for the warrant is 45.5p.
± Restated for change in accounting policy to account for income on an xd basis.
§ The diluted net asset values at 31 December 1995 and 1996 have been restated with the adoption of FRS 14. The previously reported fully diluted net asset values were 131.65p and 149.45p respectively.
# The figures prior to 2004 have not been restated for the changes in accounting policies implemented in 2005.
‡ Includes derivative financial instruments.

# LONG TERM PERFORMANCE CONTINUED

NET LIQUID ASSETS AND FIXED INTEREST AS PERCENT OF NAV 31 DECEMBER 2018

**12.9%**

5 YEAR COMPOUND ANNUAL GROWTH IN NAV PER SHARE

**+10.3%**

10 YEAR COMPOUND ANNUAL GROWTH IN NAV PER SHARE

**+17.9%**

## REVENUE

| Year to 31 December | Income £'000 | Available for ordinary shareholders £'000 | Earnings per ordinary share net¶ p | Dividend per ordinary share net p | Ongoing charges§ % | Actual gearing^ | Potential gearing** |
|---|---|---|---|---|---|---|---|
| 2008 | 7,629 | 4,742 | 5.59 | 1.55†† | 1.13 | 101 | 131 |
| 2009 | 6,077 | 324 | 0.39 | 0.30 | 1.12 | 105 | 117 |
| 2010 | 7,277 | 42 | 0.05 | – | 1.05 | 101 | 112 |
| 2011 | 9,171 | 947 | 1.19 | 1.00 | 1.10 | 105 | 116 |
| 2012 | 9,164 | 750 | 0.94 | 1.00 | 1.08 | 104 | 114 |
| 2013 | 8,987 | (307) | (0.39) | – | 1.04 | 100 | 106 |
| 2014 | 8,245 | (1,464) | (1.89) | – | 1.07 | 101 | 106 |
| 2015 | 9,136 | (36) | (0.05) | – | 1.08 | 95 | 106 |
| 2016 | 9,541 | 430 | 0.58 | – | 1.09 | 92 | 103 |
| 2017 | 10,799 | 486 | 0.68 | – | 1.08 | 93 | 100 |
| **2018** | **11,250** | **58** | **0.08** | **–** | **1.07** | **87** | **100** |

¶ The calculation of earnings per ordinary share is based on the revenue from ordinary activities after taxation and the weighted average number of ordinary shares in issue (see note 8, page 59).
§ From 2012, calculated by dividing total operating costs by average net asset value (with debt at fair value) in accordance with AIC guidelines. Prior years have not been recalculated as the change in methodology is not considered to result in a materially different figure.
^ Total assets (including all debt used for investment purposes) less all cash and fixed interest securities (excluding convertibles and corporate bonds) divided by shareholders' funds.
** Total assets (including all debt used for investment purposes) divided by shareholders' funds.
†† The 2008 dividend excludes the special dividend of 3.45p.

## CUMULATIVE PERFORMANCE (TAKING 2008 AS 100)

| At 31 December | Diluted net asset value per share | Share price | Numis Smaller Cos plus AIM Index | Russell 2000 Technology Index§§ | Earnings per ordinary share | Dividend per ordinary share net | Retail price index |
|---|---|---|---|---|---|---|---|
| 2008 | 100 | 100 | 100 | 100 | 100 | 100 | 100 |
| 2009 | 166 | 184 | 157 | 143 | 7 | 19 | 102 |
| 2010 | 235 | 263 | 202 | 202 | 1 | – | 107 |
| 2011 | 223 | 247 | 172 | 186 | 21 | 65 | 112 |
| 2012 | 250 | 279 | 205 | 194 | 17 | 65 | 116 |
| 2013 | 318 | 372 | 262 | 268 | (7) | – | 119 |
| 2014 | 322 | 358 | 243 | 306 | (34) | – | 121 |
| 2015 | 349 | 405 | 257 | 325 | (1) | – | 122 |
| 2016 | 429 | 480 | 280 | 487 | 10 | – | 125 |
| 2017 | 544 | 636 | 333 | 522 | 12 | – | 131 |
| **2018** | **518** | **584** | **273** | **548** | **1** | **–** | **134** |

## COMPOUND ANNUAL RETURNS

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| 5 year | 10.3% | 9.4% | 0.8% | 15.4% | – | – | 2.4% |
| 10 year | 17.9% | 19.3% | 10.6% | 18.5% | – | – | 3.0% |

Past performance is not a guide to future performance.
§§ The Russell 2000 (small cap) Technology Index was rebased during 2009 following some minor adjustments to its constituents. The rebased index is used from 31 December 2008 onwards.

DISCOUNT TO NAV 31 DECEMBER 2018

# 17.8%

## PREMIUM/(DISCOUNT) TO FULLY DILUTED NET ASSET VALUE (PLOTTED ON A MONTHLY BASIS)

Source: Refinitiv (Thomson Reuters)

## CAPITAL RETURN SINCE INCEPTION

| | 31 December 2018 | Inception 16 February 1994 | % change |
|---|---|---|---|
| Net asset value per ordinary share (including current year income) | 1,307.89p | 98.72p | 1,224.85 |
| Net asset value per ordinary share (excluding current year income) | 1,307.81p | 98.72p | 1,224.77 |
| Share price | 1,075.00p | 90.90p | 1,082.62 |
| Numis Smaller Companies Index plus AIM (ex. investment companies) | 4,917.91 | 1,750.00 | 181.02 |
| Russell 2000 (small cap) Technology Index (in sterling terms)† | 2,597.21 | 688.70* | 277.12 |

* At 9 April 1996 being the date funds were first available for international investment

† The Russell 2000 (small cap) Technology Index was rebased during 2009 following some minor adjustments to its constituents. The rebased index is used from 31 December 2008 onwards.

## CAPITAL RETURNS SINCE INCEPTION (FIGURES HAVE BEEN REBASED TO 100 AT 16 FEBRUARY 1994)

- Fully diluted NAV
- Share price
- Numis Smaller Companies Index plus AIM (excluding investment companies)
- Russell 2000 (small cap) Technology Index (in sterling terms)

Source: Refinitiv (Thomson Reuters)

# Governance

# STRATEGIC REPORT

### BUSINESS MODEL AND STATUS

The Company is an investment company within the meaning of Section 833 of the Companies Act 2006.

The Company carries on business as an investment trust. It was approved by HM Revenue & Customs as an investment trust under Section 1158 of the Corporation Tax Act 2010 for the year ended 31 December 2017, subject to matters that may arise from any subsequent enquiry by HM Revenue & Customs into the Company's tax return. In the opinion of the directors the Company has subsequently conducted its affairs so as to enable it to continue to seek such approval.

### OBJECTIVE

The Company's objective is described on page 2 (Policy and Objective).

### INVESTMENT POLICY – STRATEGY

While the policy is global investment in smaller quoted companies in TMT, the approach is to construct a diversified portfolio through the identification of individual companies which offer long term growth potential, typically over a five year horizon or more. The portfolio is actively managed and does not seek to track any comparative index. With a remit to invest in smaller companies with market capitalisation generally below $3bn, there tends to be a correlation with the performance of smaller companies, as well as those of the technology sector. A degree of volatility relative to the overall market should be expected.

The risk associated with the illiquidity of smaller companies is reduced by generally restricting the stake in any one company to less than 10% of the shares in issue. A number of investments are in early stage companies, which have a higher stock specific risk but the potential for above average growth. Stock specific risk is reduced by having a diversified portfolio of over 250 holdings. In addition, to contain the risk of any one holding, the manager generally takes profits when a holding reaches more than 5% of the portfolio. The manager actively manages the exposure within the constraint that illiquid positions cannot be traded for short term movements.

The Company has a policy not to invest more than 15% of gross assets in other UK listed investment companies.

From time to time, fixed interest holdings, non-equity or unlisted investments may be held on an opportunistic basis.

The Company recognises the long term advantages of gearing and has a maximum gearing limit of 50% of net assets. Borrowings are invested primarily in equity markets but the manager is entitled to invest in other securities in the companies in the target areas when it is considered that the investment grounds merit the Company taking a geared position. The board's intention is to gear the portfolio when appropriate. Gearing levels are monitored closely by the manager and reviewed by directors at each board meeting.

The Company may use derivatives which will be principally, but not exclusively, for the purpose of efficient portfolio management (i.e. for the purpose of reducing, transferring or eliminating investment risk in its investments, including protection against currency risk).

A detailed analysis of the Company's investment portfolio is set out on pages 20 to 26 and in the investment manager's report.

### PERFORMANCE AND KEY PERFORMANCE INDICATORS ('KPIs')

At each board meeting, the directors consider a number of performance measures to assess the Company's success in achieving its objectives.

The KPIs used to measure the progress and performance of the Company over time are established industry measures and are as follows:

- the movement in net asset value per ordinary share compared to the comparative indices;
- the movement in the share price;
- the discount; and
- the ongoing charges.

A historical record of these measures is shown on pages 27 to 29.

The Company makes reference in this annual report and financial statements to a number of alternative performance measures, as described on page 72.

### SHARE CAPITAL

At 31 December 2018 the Company's capital structure consisted of 68,901,568 ordinary shares of 25p each (2017 – 70,307,785 ordinary shares). During the year 1,406,217 (2017 – 2,754,016) shares were bought back and cancelled. There are no restrictions concerning the holding or transfer of the Company's ordinary shares and there are no special rights attached to any of the shares. On a winding up, after meeting the liabilities of the Company, the surplus assets would be paid to ordinary shareholders in proportion to their shareholdings.

### DERIVATIVE INSTRUMENTS

The Company does not currently have any exposure to derivative instruments.

### BORROWINGS (SEE NOTE 11 OF THE FINANCIAL STATEMENTS)

The Company has a multi-currency revolving loan facility with RBS up to £25m, maturing in December 2019, under which no drawdowns have been made to date. The Company had a sterling term loan facility with RBS of £25m which was repaid at the expiry of its term on 29 December 2017.

### REVIEW OF THE YEAR AND FUTURE DEVELOPMENTS

A review of the year and the investment outlook is contained in the chairman's statement and the investment manager's report on pages 8 to 14.

### BREXIT

The board believes that the UK's decision to leave the EU will not present a threat to the Company's business model, its viability statement or its ability to continue producing accounts on a going concern basis. The UK is a world leader in the development and delivery of – in particular – innovative technological solutions and the board sees no reason why this should change once the UK has left the EU.

**PRINCIPAL RISKS AND UNCERTAINTIES**

The Company's assets consist mainly of listed securities and principal risks to the success of the business model are therefore market related and include market risk (comprising currency risk, interest rate risk and other price risk), liquidity risk and credit risk. An explanation of those risks – which have been subject to robust assessment by the directors – and how they are managed is contained in note 18 to the accounts on pages 62 to 67, and a description of the internal controls operated by the Company is on pages 37 and 38.

Other risks to the Company's model, future performance, solvency or liquidity include the following:

**Regulatory risk** – failure to comply with applicable legal and regulatory requirements could lead to suspension of the Company's Stock Exchange listing, financial penalties by the UKLA or a qualified audit report. Breach of the Corporation Tax Act 2010 could lead to the Company being subject to tax on capital gains. The manager, depositary and administrator provide regular reports to the audit committee on their monitoring programmes. The manager monitors investment positions and the manager and company secretary monitor the level of forecast income and expenditure.

Major regulatory change could impose disproportionate compliance burdens on the Company. In such circumstances representation would be made to seek to ensure that special circumstances of investment trusts are recognised.

**Operational/financial/custody risk** – failure of the administrator's accounting systems or those of other third party service providers could lead to an inability to provide accurate reporting and monitoring or a misappropriation of assets. The manager, administrator and company secretary each have comprehensive business continuity plans which facilitate continued operation of the business in the event of a service disruption or major disruption. The audit committee receives the administrator's report on internal controls and the reports by other key third party providers are reviewed by the manager and company secretary on behalf of the audit committee. The depositary reports six monthly on custody matters, including the continued safe custody of the Company's assets.

**Discount volatility** – the discount at which the Company's shares trade can widen. The board monitors the level of discount and the Company has authority to buy back its own shares.

**Gearing risk** – the Company may borrow money for investment purposes. If the investments fall in value, any borrowings will magnify the extent of this loss. If borrowing facilities are not renewed, the Company may have to sell investments to repay borrowings.

All borrowings require the prior approval of the board and gearing levels are discussed by the board and manager at every meeting. The majority of the Company's investments are in quoted securities.

**VIABILITY STATEMENT**

The UK Corporate Governance Code and Listing Rules require that the Company should publish a longer-term statement on the viability of the Company. The directors consider that three years is an appropriate forward looking time period. This recognises the Company's current position, the investment strategy, which includes investment in smaller companies and start-ups where a three year horizon is a meaningful period over which to judge prospects, the board's assessment of the main risks that threaten the business model and the relatively fast moving nature of the sectors in which the Company invests.

The directors confirm that, based on reviews conducted as part of the detailed internal controls and risk management processes set out on pages 37 and 38, they have a reasonable expectation that the Company will continue to maintain its status as an investment trust, to implement its investment strategy and to operate and be able to meet its liabilities as they fall due for at least the next three financial years. Their consideration also takes into account the Company's gearing and financing arrangements and its projected income and expenditure.

There are no current plans to amend the investment strategy, which has delivered good investment performance for shareholders over many years and, the directors believe, should continue to do so. The investment strategy and its associated risks are kept under constant review by the board.

By definition, investment in smaller and start-up companies carries higher risks, both in terms of stock liquidity and longer-term business viability and this risk is accepted by the board. In addition, it should be noted that under the Company's articles of association, shareholders are required to vote triennially on whether the Company should continue as an investment trust, so the longer-term viability statement is contingent upon shareholders voting to support any continuation vote falling within the relevant three year period. The next continuation vote will be at the AGM on 16 April 2019. The directors strongly support the Company's continuation. They recommend that shareholders should vote in favour of continuation and believe that they will do so.

**EMPLOYEES, SOCIAL AND COMMUNITY ISSUES, GENDER**

The Company has no employees. Its board is made up of six directors, five males and one female.

As an investment trust, the Company has no direct social or community responsibilities. However, the Company believes that it is in the shareholders' interests to consider environmental, social and governance factors when selecting and retaining investments. Details of the Company's policy on socially responsible investment can be found under the section on stewardship later in this report.

# STRATEGIC REPORT CONTINUED

**INVESTMENT MANAGEMENT, STRATEGY IMPLEMENTATION AND ADMINISTRATION**

The management of the Company and the implementation of its investment strategy is contracted to Herald Investment Management Limited ('HIML'). HIML is authorised and regulated by the Financial Conduct Authority both for investment management and as an Alternative Investment Fund Manager (see regulatory compliance in the directors' report).

The management contract is subject to 12 months' notice by either party. The senior director of HIML with prime responsibility for the management of the Company's portfolio is Katie Potts, who is also a substantial shareholder of HIML Holdings Limited, the parent company of HIML. HIML is remunerated at an annual rate of 1.0% of the Company's net asset value calculated using middle market prices. Compensation fees would only be payable in respect of this 12 month period if termination were to occur sooner. Careful consideration has been given by the board as to the basis on which the management fee is charged. The board considers that maintaining an appropriate level of ongoing charges for a specialist trust is in the best interest of all shareholders. The board is also of the view that calculating the fee with reference to performance would be unlikely to exert a positive influence over the long term performance. At 31 December 2018, Katie Potts held 447,184 of the Company's shares.

At 31 December 2018, the Company was the beneficial owner of 15.4% of the ordinary share capital of HIML Holdings Limited.

Administration of the Company and its investments has been delegated by HIML to The Bank of New York Mellon ("BNYM") and company secretarial duties have been delegated to Law Debenture Corporate Services Limited.

The board considers the investment management and secretarial arrangements for the Company on a continuing basis and a formal review is conducted annually. The board considers, amongst others, the following topics in its review: investment performance in relation to the investment policy and strategy; the continuity of personnel managing the assets and reporting to the board; the level of service provided in terms of the accuracy and timeliness of reports to the board and the frequency and quality of both verbal and written communications with shareholders. Following the most recent review the board is of the opinion that the continued appointment of HIML as investment manager, on the terms agreed, is in the interests of shareholders due to the experience of the manager and the quality of information provided to the board.

**STEWARDSHIP – RESPONSIBILITIES AS AN INSTITUTIONAL SHAREHOLDER**

The Company has given discretionary voting powers to the investment manager, HIML. The manager votes against resolutions it considers may damage shareholders' rights or economic interests. The Company believes that it is in the shareholders' interests to consider environmental, social and governance (ESG) factors when selecting and retaining investments and has asked the manager to take these issues into account as long as the investment objectives are not compromised. The manager does not exclude companies from its investment universe purely on the grounds of ESG issues but adopts a positive engagement approach whereby matters are discussed with management with the aim of improving the relevant policies and management systems and enabling the manager to consider how ESG factors could impact long term investment returns. The manager's statement of compliance with the UK Stewardship Code can be found on the manager's website at www.heralduk.com. The manager's policy has been reviewed and endorsed by the board.

**DIVIDENDS**

The ordinary shares carry a right to receive dividends. Interim dividends are determined by the directors and final dividends are subject to shareholder approval. The directors do not recommend a dividend for the period under review.

By order of the board

**Julian Cazalet**
*Chairman*
19 February 2019

Julian Cazalet

# DIRECTORS' BIOGRAPHIES

**JULIAN CAZALET**
Julian Cazalet was appointed to the board in 2008 and became chairman in 2009. He was managing director – corporate finance at JPMorgan Cazenove until his retirement in December 2007. A chartered accountant, he joined Cazenove in 1973 and was made a partner in 1978. From 1989 he worked in corporate finance and advised investment trusts in addition to his work with industrial and commercial companies. He is chairman of The Lindsell Train Investment Trust plc and a director of Deltex Medical Group plc and a number of charitable trusts. Julian will be retiring as a director and chairman at the conclusion of the AGM on 16 April 2019.

**TOM BLACK**
Tom Black was appointed to the board in 2013. He is chairman of Thruvision Group plc (formerly Digital Barriers plc), and is a non-executive director of Adept4 plc. He also has advisory roles with a number of smaller unlisted businesses and sits on the strategy advisory group of Wolfson College Oxford. He is chairman and trustee of the Black Family Charitable Trust, which is focused on supporting disadvantaged young people with their educational needs. He was previously chief executive of Detica Plc, a leading company in the field of large-scale information collection and analysis for intelligence and counter fraud applications. Tom is the senior independent director.

**STEPHANIE EASTMENT**
Stephanie Eastment was appointed to the board in December 2018 and is chair of the audit committee. She qualified as a chartered accountant, moving on to hold various accounting and compliance roles at Wardley and UBS before joining Invesco Asset Management in 1996. When she left Invesco in July 2018, she was Head of Specialist Funds Company Secretariat and Accounts. Stephanie is a non-executive director and audit chair of Murray Income Trust plc.

**IAN RUSSELL**
Ian Russell was appointed to the board in August 2018. He qualified as a chartered accountant, moving on to work in a number of finance roles in industry and banking. He joined Scottish Power plc in 1994, initially as Finance Director, becoming CEO in 2001, a role he held until 2006. Since then, he has concentrated on non-executive roles. Currently he is Chairman of HICL Infrastructure Company Limited and Chair of the Scottish Futures Trust Limited, an independent company established by the Scottish Government with a responsibility for delivering value for money across public sector infrastructure investment. Subject to his election by shareholders at the AGM on 16 April 2019, Ian will succeed Julian Cazalet as chairman of the Company.

**KARL STERNBERG**
Karl Sternberg was appointed to the board in 2015. He was a founding partner of Oxford Investment Partners Limited from 2006 until 2013, when it was acquired by Towers Watson. Much of his earlier career was spent at Morgan Grenfell (which became Deutsche Asset Management), where he rose to become chief investment officer, Europe & Asia Pacific. Karl is a non-executive director of Clipstone Logistics REIT plc, Monks Investment Trust plc, Lowland Investment Company plc, Alliance Trust plc, JP Morgan Elect plc, Island House Investment LLP, Jupiter Fund Management plc and Railpen Investments.

**JAMES WILL**
James Will was appointed to the board in 2015. He was until 2014 chairman and a senior corporate finance partner of law firm Shepherd and Wedderburn LLP. He also headed the law firm's financial sector practice. Over the last 20 years he has been involved in advising smaller quoted technology companies on a range of corporate transactions, including flotations, secondary fundraisings and mergers and acquisitions. James is chairman of The Scottish Investment Trust PLC, and a non-executive director of Edinburgh Dragon Trust plc.

# CORPORATE GOVERNANCE REPORT

## COMPLIANCE
The board is committed to achieving and demonstrating high standards of corporate governance. This statement outlines how the principles of the April 2016 UK Corporate Governance Code (the 'Code'), which can be found at www.frc.org.uk, were applied throughout the financial year. The board confirms that the Company has complied throughout the year under review with the relevant provisions of the Code, except where indicated below. The Company was a constituent of the FTSE250 throughout the period and reports on that basis. The latest version of the Code, as published in 2018, becomes effective for financial years beginning 1 January 2019 and appropriate steps are being taken to ensure compliance.

The Association of Investment Companies has published its own Code of Corporate Governance (July 2016) which provides a framework of best practice for investment companies which can be found at www.theaic.co.uk. The board is of the opinion that the Company has complied with the recommendations of the AIC Code.

## THE BOARD
The board has overall responsibility for the Company's affairs. It has a number of matters reserved for its approval including strategy, approval of the financial statements, investment policy, borrowings, gearing policy, treasury matters, dividend and corporate governance policy. The board also reviews the financial statements, investment transactions, revenue budgets and performance. Full and timely information is provided to the board to enable it to function effectively and to allow directors to discharge their responsibilities.

The chairman is responsible for organising the business of the board, ensuring its effectiveness and setting its agenda. He reviews channels for the provision of information with the company secretary at least once a year. The executive responsibilities for investment management and administration have been delegated to HIML and BNYM respectively, and in the context of a board comprising entirely non-executive directors, there is no chief executive officer. Tom Black is the senior independent director.

The directors believe that the board has a balance of skills and experience which enable it to provide effective leadership and proper governance of the Company. Information about the directors, including their relevant experience, can be found on page 35.

The board historically composed four directors; this was increased to five during the year as explained in the Chairman's Statement, with six directors in place at the year end to ensure a smooth transition. All the directors are non-executive.

The board has reviewed the performance of all directors. In each case, their performance continues to be effective and they remain committed to the Company. Their contribution to the board is valued highly and the board recommends their election or re-election to shareholders.

There is an agreed procedure for directors to seek independent professional advice if necessary at the Company's expense.

## TERMS OF APPOINTMENT
The terms and conditions of directors' appointments are set out in formal letters of appointment which are available for inspection on request.

Under the provisions of the Company's articles of association, a director appointed during the year is required to retire and seek election by shareholders at the next AGM. All directors retire annually and if appropriate, offer themselves for re-election.

## INDEPENDENCE OF DIRECTORS
All the directors are considered by the board to be independent of the manager and free of any business or other relationship which could interfere with the exercise of their independent judgement.

## MEETINGS
There is an annual cycle of board meetings which is designed to address, in a systematic way, overall strategy, review of investment policy, investment performance, revenue budgets, dividend policy and communication with shareholders. The board considers that it meets sufficiently regularly to discharge its duties effectively. The table below shows the attendance record for the board and committee meetings held during the year. All the directors attended the AGM. In addition, the board held an offsite 'strategic awayday' in December 2018, which was attended by all the directors and the investment manager.

| Number of meetings | Board 5 | Audit 2 | Nomination 6 |
|---|---|---|---|
| Julian Cazalet | 5 | 2 | 6 |
| Tom Black* | 4 | 1 | 6 |
| Stephanie Eastment** | – | – | – |
| Ian Russell*** | 2 | – | 3 |
| Karl Sternberg* | 4 | 1 | 6 |
| James Will | 5 | 2 | 6 |

* Tom Black and Karl Sternberg missed meetings in February and July respectively due to pressing family matters.
** Stephanie Eastment appointed 1 December; no meetings after that date, but she attended the awayday.
*** Ian Russell appointed 1 August, attended all meetings after that date.

## NOMINATION COMMITTEE
The nomination committee consists of all the directors and the chairman of the board is chairman of the committee. The committee meets on an annual basis and at such other times as may be required. The committee has written terms of reference which include reviewing the board, identifying and nominating new candidates for appointment to the board, board and director appraisal, succession planning and training. The committee also considers whether directors should be recommended for re-election by shareholders. The committee is responsible for considering directors' potential conflicts of interest and for making recommendations to the board on whether or not the potential conflicts should be authorised. The terms of reference are reviewed annually and are available on request and at www.heralduk.com.

Appointments to the board are made on merit irrespective of race, colour, religion, age, educational/professional background and gender. The committee is working towards a target of one third of female directors. It operates in accordance with the following standards:

— when seeking to recruit, the nomination committee will evaluate the skills, experience, independence, knowledge and diversity of the board and prepare a description of the role and capabilities required to fulfil the appointment and will normally appoint an independent agency to assist in the recruitment process;

- it will ensure that a diverse group of candidates is considered; and
- candidates will be considered on merit and against objective criteria having regard to the benefits of diversity, including gender.

During the year the committee met five times. It undertook a comprehensive update of its plans for succession to the board including identifying the skills of current and future directors, taking into account planned changes to the board. The committee recommended to the board, and the board resolved, to increase the number of directors from four to five and the engagement of Trust Associates, an independent external recruitment firm, to conduct a search to identify suitable candidates for appointment as independent non-executive directors, one of whom would be the future chairman. As a result, two new directors were appointed during the year as detailed in the Chairman's Statement on page 9.

The senior independent director took over the chairmanship of the committee whenever it was dealing with the matter of the chair of the board's successor.

**PERFORMANCE EVALUATION**

The nomination committee met to assess the performance of the chairman, each director, the board as a whole and its committees, after inviting each director and the chairman to consider and respond to a set of questions. The appraisal of the chairman was led by Tom Black. The appraisals and evaluations considered, amongst other criteria, the balance of skills of the board, training and development requirements, the contribution of individual directors and the overall effectiveness of the board and its committees. Following this process it was concluded that the performance of each director, the chairman, the board and its committees continues to be effective and each director and the chairman remain committed to the Company.

A review of the chairman's and other directors' commitments was carried out and the nomination committee is satisfied that they are capable of devoting sufficient time to the Company.

**EXTERNAL EFFECTIVENESS EVALUATION**

The board has not facilitated an external review of its effectiveness since admission to the FTSE 250 in October 2017. Further consideration will be given to this later in 2019, by which time changes in the board's composition and leadership will have had time to settle.

**INDUCTION AND TRAINING**

Training for new directors is tailored to the particular circumstances of the individual appointee. Regular briefings are provided on changes in regulatory requirements that could affect the Company and the directors. Directors receive other relevant training as necessary.

**REMUNERATION**

As all the directors are non-executive there is no need for a separate remuneration committee. Directors' fees are considered by the board as a whole within the remuneration policy limits approved by shareholders, set out on page 42.

**INTERNAL CONTROLS, RISK MANAGEMENT AND INTERNAL AUDIT**

The directors acknowledge their responsibility for the Company's risk management and internal controls systems and for reviewing their effectiveness. The systems are designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable but not absolute assurance against material misstatement or loss.

The board confirms that there is a continuing process for identifying, evaluating and managing the significant risks faced by the Company, in accordance with the guidance on risk management, internal control and related financial and business reporting, published by the FRC.

The directors confirm that they have reviewed the effectiveness of the Company's risk management and internal control systems and they have procedures in place to review their effectiveness on a regular basis. No significant weaknesses were identified in the year under review and in the period up to and including the date of this report.

The practical measures to ensure compliance with regulation and company law, and to provide effective and efficient operations and investment management, have been delegated to HIML, the company secretary and BNYM.

The audit committee and board monitor performance of the functions performed by HIML, the company secretary and BNYM through regular review. Since July 2014, when HIML became the Company's AIFM under the Alternative Investment Fund Managers Directive ('AIFMD'), the audit committee and board also monitor the controls managed by the AIFM.

The AIFM has a risk policy covering the risks associated with its management of the portfolio and it has in place its own risk management procedures, which are periodically reviewed. Risk limits are set by the AIFM and approved by the audit committee taking into account several factors, including investment strategy and risk appetite. The investment policy limits are described in the strategic report and are monitored at each board meeting, taking account of appropriate sensitivity analysis.

HIML has a compliance function in accordance with FCA regulations. The compliance function provides the audit committee and board with a report on its monitoring procedures on a regular basis. Compliance monitoring by HIML includes risk based internal monitoring as well as external monitoring of services that have been delegated to third parties – principally fund accounting and company secretarial services. For fund accounting, monitoring includes reviewing the monthly net asset value produced by BNYM versus HIML's own system, reviewing BNYM's client accounting compliance reports and internal audit confirmations and reviewing KMPG's annual Service Organisation Control (SOC1) and Centrally Managed Information Technology Services (CMITS) reports on BNYM. The audit committee also receives regular compliance reports from BNYM, including performance against service level standards.

# CORPORATE GOVERNANCE REPORT CONTINUED

Under AIFMD, the Company has appointed a depositary, BNY Mellon Trust & Depositary (UK) Limited, whose responsibilities include cash monitoring and safe keeping of the Company's assets. During the year, the appointment was novated to the The Bank of New York Mellon (International) Limited, which also became custodian in place of The Bank of New York Mellon SA/NV, London Branch. The scope of the fund accounting services includes reconciliations to custody records. Provision of custody services by BNYM is covered by a SOC1 report, a copy of which is provided to audit committee members. Finally, a detailed risk map is prepared by the company secretary for the audit committee, identifying the significant risks faced by the Company (summarised on page 33) and the key controls employed to manage those risks.

These procedures ensure that consideration is given regularly to the nature and extent of the risks facing the Company and that they are being actively monitored. Where changes in risk are identified during the year, these procedures also provide a mechanism to assess whether further action is required to manage the changes identified. The board confirms that these procedures have been in place throughout the year under review and that they continue to be in place up to the date of approval of this report.

The audit committee carries out an annual review of the need for an internal audit function. The committee continues to believe that the compliance and internal control systems and the internal audit function in place within the manager and the administrator provide sufficient assurance that a sound system of internal control, which safeguards shareholders' investment and the Company's assets, is maintained. An internal audit function, specific to the Company, is therefore considered unnecessary.

### ACCOUNTABILITY AND AUDIT
The respective responsibilities of the directors and the auditors in connection with the financial statements are set out on pages 45 to 49.

### AUDIT COMMITTEE
A separate audit committee report appears on page 39. Its chair is Stephanie Eastment and all of the non-executive directors are members, including the chairman, Julian Cazalet. Following his retirement, the successor chairman Ian Russell will not be a member of the committee.

### RELATIONS WITH SHAREHOLDERS
The board places great importance on communication with shareholders. The Company's manager meets regularly with larger shareholders and reports to the board. The chairman also meets with shareholders both with the manager and on his own. Shareholders wishing to communicate with the chairman or any other director may do so by writing to him at the registered office of the Company which is shown on page 71.

The Company's AGM provides a forum for communication with all shareholders. The level of proxies lodged for each resolution is announced at the meeting and is published on the manager's website, www.heralduk.com, subsequent to the meeting. The notice period for the AGM is at least 20 working days. Shareholders and potential investors may obtain up-to-date information on the Company from the manager's website.

### PURCHASE OF OWN SHARES
At the AGM of the Company to be held on 16 April 2019, the Company will as usual be seeking authority to make limited purchases of the Company's ordinary shares – see the notice of AGM on page 68. Buy-backs are considered by the board to be a useful tool, where surplus cash is not being utilised for investment, to assist in the maintenance of liquidity in the Company's shares.

### AGM – DIGITAL PROXY VOTING
Shareholders are strongly encouraged to submit proxy votes online by visiting www.signalshares.com. There is a straightforward registration process and a number of our shareholders are using the site already. All you need is your name, address and investor code, which can be found on your share certificate. If you are having trouble locating your share certificate or investor code, please call the shareholder helpline on 0871 664 0300 (or from overseas +44 (0)371 664 0300).

Any shareholder who is unwilling or unable to vote digitally can 'opt-in' to receive a paper proxy card by telephoning the shareholder helpline.

### AGM – CONTINUATION VOTE
In accordance with the Company's articles of association, shareholders have the right to vote on the continuation of the Company every three years – see resolution 10 of the AGM notice on page 68. Your board strongly recommends that shareholders vote in favour of the resolution. The directors intend to vote their own shareholdings in favour.

### AGM RECOMMENDATION
The directors unanimously recommend all holders to vote in favour of all the resolutions to be proposed at the AGM.

### SUMMARY STATEMENT OF COMPLIANCE
The board has concluded that, as demonstrated by the disclosures made in the foregoing, the Company has complied throughout 2018 with all of the applicable requirements of the UK Corporate Governance Code, save that the chairman was a member of the audit committee.

*By order of the board*

**Julian Cazalet**
Chairman
19 February 2019

# AUDIT COMMITTEE REPORT

**AUDIT COMMITTEE**

The audit committee is made up of all the directors, all of whom are independent non-executive directors, and was chaired by James Will until my appointment on 1 December, when I took over as the chair. The board chairman, Julian Cazalet, retires at the forthcoming AGM and from that time the board chairman will no longer be a member of this committee, though will be invited to attend meetings.

The committee considers that at least one of its members has recent and relevant financial experience and that the committee as a whole has competence relevant to the sector in which the Company operates. Its authority and duties are defined within its written terms of reference which are available on request from the Company and on the manager's website: www.heralduk.com.

**ROLE AND DUTIES**

The committee's responsibilities, which were discharged during the year, include:

- monitoring and reviewing of the integrity of the half-yearly and annual financial statements and any formal announcements relating to the Company's financial performance including: ensuring compliance with statutory and listing requirements: appropriateness of accounting policies: and any financial judgements and key assumptions;
- reviewing the adequacy and effectiveness of internal control and risk management systems;
- making recommendations to the board within the context of the EU Audit Regulation and Directive in relation to the appointment of the external auditor and approving the remuneration and terms of their engagement;
- developing and implementing policy on the engagement of the external auditor to supply non-audit services;
- management of the relationship with the external auditor including: the scope, nature and planning of the audit; discussion of matters of audit focus; evaluation of external auditor's results; and review and monitoring the independence, objectivity and effectiveness of the external auditor;
- reviewing the arrangements in place within HIML whereby their staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters insofar as they may affect the Company;
- reviewing the terms of the investment management agreement; and
- considering annually whether there is a need for the Company to have its own internal audit function.

**RISK MANAGEMENT, INTERNAL CONTROL AND INTERNAL AUDIT**

The extensive array of internal controls adopted by the Company are set out in the corporate governance report. The board as a whole is responsible for the effectiveness of internal control mechanisms but it is informed by more specific work carried out by the audit committee.

**EXTERNAL AUDITOR – ASSESSING EFFECTIVENESS**

The committee monitors the independence and objectivity of the auditor, their performance and effectiveness by meeting at least annually with the audit partner to discuss that year's audit. Part of that process requires the auditor to give the committee an assessment of how the audit team identifies and manages the threats to its independence. The committee receives confirmation from the auditor that it has complied with the relevant UK professional and regulatory requirements on independence. It will also take into account any findings in the most recent FRC audit quality inspection report on Ernst & Young. The committee does not believe that there has been any impairment to the auditor's independence.

The committee examines in detail the scope of the audit, ensuring that the auditor's objectives have met the committee's expectations, along with key audit and accounting matters considered that year. The principal findings of the audit are discussed and challenged, particularly in areas where management judgement has been required. The committee will give the auditor an opportunity to comment privately on the quality and standard of the manager's and administrator's performance generally and during the audit. Similarly, the committee will seek the views of the manager and administrator on the effectiveness and performance of the audit team.

**NON-AUDIT SERVICES**

There is not often a need for non-audit services to be provided by the auditor. The committee's policy is that non-audit work should be limited to those matters where the external auditor is most appropriately placed to carry out the work, unless there is a conflict of interest. All non-audit services are approved in advance. No non-audit services were provided by the auditor during the period under review.

**AUDIT TENDERING**

The committee is responsible for overseeing and managing the audit tender arrangements and process. Ernst & Young LLP has been the Company's auditor since before 16 June 1994. Having considered the experience and tenure of the audit partner and staff and level of service provided, the committee remains satisfied with the auditor's effectiveness and accordingly has recommended that Ernst & Young LLP be reappointed at the forthcoming AGM. The audit partner responsible for the audit must be rotated at least every five years and was rotated in 2017. The current audit partner is Ashley Coups. There are no contractual obligations restricting the Company's choice of external auditor. The committee will put the audit to tender in 2019, noting that the current auditor becomes subject to mandatory rotation after the 2020 year end under the terms of the EU Audit Regulation and Directive. This is subject to continuing satisfactory performance in the meantime. The Company believes that it is in compliance with the provisions of the Competition and Markets Authority Order (2014) on statutory audit services and competitive tender processes.

**SIGNIFICANT FINANCIAL ISSUES RELATING TO THE 2018 FINANCIAL STATEMENTS**

The Code requires us to describe any significant issues considered in relation to the financial statements and how those issues were addressed. While there were no significant issues, two matters of risk of particular focus at the balance sheet date were the risks that investments might not have been correctly valued or beneficially owned. No issues were discovered.

**SUMMARY**

Following a detailed review of the financial statements and discussions with the manager, administrator, company secretary and auditor, the committee has concluded that the financial statements themselves, and the annual report as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy. That conclusion has been reported to and confirmed by the board.

**Stephanie Eastment**
**Chair, audit committee**
**19 February 2019**

# DIRECTORS' REPORT

The directors present their directors' report for the year ended 31 December 2018. The strategic report and the corporate governance report on pages 32 to 38 form a part of the directors' report.

**RESULTS AND DIVIDEND**
The net asset value (NAV) of the Company at 31 December 2018 was 1,307.9p per ordinary share (2017 – 1,374.9p). This represented a decrease of 4.9% during the year, compared to a decrease in the comparative indices of 18.1% (Numis Smaller Companies Index plus AIM (ex. investment companies)) and an increase of 4.7% (Russell 2000 (small cap) Technology Index (in sterling terms)). The discount was 17.8% (2017 – 14.8%).

The directors do not recommend a dividend for the year ended 31 December 2018 (2017 – nil).

**DIRECTORS**
The directors are listed on page 35. The names of those directors who will be considered for election or re-election at the forthcoming AGM appear on page 68.

**GOING CONCERN**
In accordance with The Financial Reporting Council's guidance on going concern and liquidity risk, the directors have undertaken a rigorous review of the Company's ability to continue as a going concern. The Company's principal risks are market related and include market risk, liquidity risk and credit risk. An explanation of these risks and how they are managed is contained in note 18 to the financial statements. The Company's assets, the majority of which are investments in quoted securities, exceed its liabilities significantly. All borrowings require the prior approval of the board. Gearing levels and compliance with loan covenants are reviewed by the board on a regular basis. In accordance with the Company's articles of association, shareholders have the right to vote on the continuation of the Company as an investment trust every three years and a resolution to that effect will be proposed at the AGM in 2019. The directors have no reason to believe that the resolution will not be passed.

After making enquiries, the financial statements have been prepared on the going concern basis. There are no material uncertainties that call into question the Company's ability to continue to be a going concern for at least 12 months from the date of approval of these financial statements and the board is confident that the Company will be able to continue in operation and meet its liabilities as they fall due.

**CONFLICTS OF INTEREST**
Each director submits a list of potential conflicts of interest to the nomination committee on an annual basis, or as they arise. The committee considers these carefully, taking into account the circumstances surrounding them, and makes a recommendation to the board on whether or not the potential conflicts should be authorised. Board authorisation is for a period of one year. Having considered the lists of potential conflicts there were no situations which gave rise to a direct or indirect interest of a director which conflicted with the interests of the Company.

**BRIBERY ACT 2010**
The Company has a zero tolerance policy towards bribery and is committed to carrying out business fairly, honestly and openly. The manager, administrator and company secretary also adopt a zero tolerance approach and have policies and procedures in place to prevent bribery.

**GREENHOUSE GAS EMISSIONS**
As the Company's activities are all outsourced to third parties, the Company has no greenhouse gas emissions to report.

**DIRECTOR INDEMNIFICATION AND INSURANCE**
The Company has entered into deeds of indemnity in favour of each of the directors. The deeds cover any liabilities that may arise to a third party, other than the Company, for negligence, default or breach of trust or duty. The directors are not indemnified in respect of liabilities to the Company, any regulatory or criminal fines, any costs incurred in connection with criminal proceedings in which the director is convicted or civil proceedings brought by the Company in which judgement is given against him. In addition, the indemnity does not apply to any liability to the extent that it is recovered from another person.

The Company maintains Directors' and Officers' liability insurance.

**PRINCIPAL RISKS AND UNCERTAINTIES**
These are set out as part of the strategic report.

**MAJOR INTERESTS IN THE COMPANY'S SHARES**
The following table sets out the names of those shareholders holding 3% or more of the issued share capital at 31 December 2018. No notifications have been received since then under DTR5.

| | % of issued share capital |
|---|---|
| Rathbone Investment Management | 13.51 |
| Lazard Asset Management LLC | 6.88 |
| Wells Capital Management Inc | 6.64 |
| Investec Wealth & Investment Limited | 5.21 |
| JM Finn & Co | 4.17 |
| Charles Stanley & Co | 3.39 |
| Speirs & Jeffrey | 3.30 |
| Brewin Dolphin Securities | 3.04 |
| Hargreaves Lansdown | 3.02 |

**REGULATORY COMPLIANCE**
**THE ALTERNATIVE INVESTMENT FUND MANAGERS ("AIFM") DIRECTIVE**
The AIFM is required to provide portfolio management, risk management, administration, accounting and company secretarial services to the Company. The Company has appointed HIML as its AIFM, to undertake these functions on its behalf. As reported elsewhere, HIML has elected to delegate some of these functions. The Bank of New York Mellon (International) Limited is the depositary and is paid 0.015% per annum of the total net assets of the portfolio (adjusted to include any leverage). The depositary is responsible for custody activities.

AIFMs are obliged to publish certain information for investors and prospective investors, which may be found either in this annual report or on the Company's website. Any information on remuneration not already disclosed in the remuneration report will be provided to investors on request.

The AIFMD requires an annual disclosure of 'leverage'. On a 'gross' basis, this is 0.96 against a maximum of 2.00 (2017 – 0.99: 2.00) and on a 'commitment' basis, 1.00 against a maximum of 2.00 (2017 – 1.00: 2.00).

**THE MODERN SLAVERY ACT 2015**
The Company falls outside the scope of the Modern Slavery Act and is therefore not required to make a slavery and human trafficking statement.

**PAYMENT TO SUPPLIERS**
The Company is a signatory to the Prompt Payment Code, which enshrines a 30 day payment term as a norm.

**DISCLOSURE OF INFORMATION TO THE AUDITOR**
The directors confirm that so far as each of them is aware, there is no relevant audit information of which the Company's auditor is unaware and the directors have taken all the steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

**DIRECTORS' RESPONSIBILITY STATEMENT PURSUANT TO DTR4**
The directors confirm to the best of their knowledge:

The financial statements have been prepared in accordance with applicable law and United Kingdom Accounting Standards (UK GAAP) including FRS 102 'The Financial Reporting Standard applicable to the UK and Republic of Ireland' and give a true and fair view of the assets, liabilities, financial position and loss of the Company.

The annual report includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that it faces.

**INDEPENDENT AUDITORS**
The auditors, Ernst & Young LLP, are willing to continue in office and in accordance with sections 489 and 491(1) of the Companies Act 2006 resolutions concerning their reappointment and remuneration will be submitted to the AGM.

By order of the board

**Julian Cazalet**
**Chairman**
**19 February 2019**

Julian Cazalet

# DIRECTORS' REMUNERATION REPORT

## 1 CHAIRMAN'S ANNUAL STATEMENT

Dear Shareholder

I present below (at section 3) the Company's remuneration report for the year ended 31 December 2018.

Our remuneration policy (see section 2 below) was approved by shareholders at the 2017 AGM. The policy must be put to shareholders for approval every three years and the board must only operate in accordance with the approved policy during the three year cycle, unless shareholder approval is sought to amend the policy. I confirm that the board has complied with the policy during the year ended 31 December 2018. Fees were increased with effect from 1 July 2018 to: chairman – £33,750; audit committee chair – £25,500; NED – £22,500. This means that fees have increased by c.8% since our remuneration policy was approved.

The law requires the Company's auditors to audit certain of the disclosures provided. Where disclosures have been audited, they are indicated as such. The auditor's opinion is included in their report on pages 46 to 49.

### SCOPE AND RESPONSIBILITY

As the Company has no employees and no executive directors, the policy relates only to the non-executive directors.

## 2 POLICY ON DIRECTORS' FEES

The board's policy is that the remuneration of directors should be set at a reasonable level that is commensurate with the duties and responsibilities of the role and consistent with the requirement to attract and retain directors of the appropriate quality and experience. It should also reflect the experience of the board as a whole and be fair and comparable to that of other investment trusts that are similar in size. The board has taken account of any views expressed by shareholders in formulating this policy.

| Component | Commentary |
|---|---|
| **Basic fee arrangement** | At the time the policy was approved in April 2017, the directors received fees for their services as follows:<br>– Chairman fee – £31,500<br>– Audit committee chair – £23,000<br>– NED fee – £21,000<br><br>These fees are determined within an aggregate limit set out in the Company's articles of association which stands at £200,000 per annum, increased from £125,000 at the AGM in 2018.<br><br>There is no separate remuneration committee and the board as a whole considers changes to directors' fees from time to time. The company secretary provides advice and comparative information when the board considers the level of directors' fees.<br><br>If the board concludes that it is appropriate to increase fees during the three year period that the policy is in force, such increase (or increases) will be limited to a maximum total increase of 20% of the amounts payable when the policy was approved, as set out above. Any new directors will be paid at the rates set out above (subject to any increase that may have been introduced in line with this policy).<br><br>Under the terms of the directors' appointment letters, there is no notice period and no provision for compensation upon early termination of appointment. |
| **Benefits** | None |
| **Pension arrangements** | None |
| **Bonus arrangements** | None |

### DATES OF DIRECTORS' APPOINTMENTS

| Name | Date of appointment |
|---|---|
| Julian Cazalet | 18 January 2008 |
| Tom Black | 1 May 2013 |
| Stephanie Eastment | 1 December 2018 |
| Ian Russell | 1 August 2018 |
| Karl Sternberg | 21 April 2015 |
| James Will | 21 April 2015 |

### 3 ANNUAL DIRECTORS' REMUNERATION REPORT FOR THE YEAR ENDING 31 DECEMBER 2018 (AUDITED)

The directors who served in the year received the following emoluments in the form of fees and received no other benefits.

| | Fees 2018 £ | Fees 2017 £ |
|---|---|---|
| Directors who served during the year: | | |
| Julian Cazalet | **33,375** | 32,250 |
| Tom Black | **22,250** | 21,500 |
| *Stephanie Eastment (appointed 1 December)* | **2,125** | – |
| Ian Russell (appointed 1 August) | **9,375** | – |
| Karl Sternberg | **22,250** | 21,500 |
| James Will* | **25,000** | 24,000 |
| | **114,375** | 99,250 |

* James Will was chair of the audit committee until 1 December 2018 when he was replaced by Stephanie Eastment.

Board meetings are held at the Company's registered office. Directors are entitled to claim travel expenses for board meeting attendance. The Company has entered into a PAYE settlement agreement with HMRC under which these expenses are accounted for directly with HMRC. The total of travel expenses settled on this basis in 2018 was £2,297.

### DIRECTORS' INTERESTS (AUDITED)

Directors' shareholdings and interests (beneficial unless stated) at the year-end (and unchanged at the date of this report) were as follows:

| Interests as at 31 December | 2018 | 2017 |
|---|---|---|
| Julian Cazalet* | **150,000** | 150,000 |
| Tom Black | **6,900** | 6,900 |
| *Stephanie Eastment*** | **1,000** | – |
| Ian Russell | **7,500** | – |
| Karl Sternberg | **3,578** | 3,578 |
| James Will | **6,000** | 6,000 |

* 50,000 held non-beneficially
** *Non-beneficially; shares held by connected person*

### COMPANY PERFORMANCE

The graph below compares the total return (assuming all dividends are reinvested) to ordinary shareholders compared to the total shareholder return on a notional investment made up of shares in the component parts of the MSCI World Index (in sterling terms). This index was chosen for comparison purposes as it is the most widely used global equity index.

*Source: Refinitiv (Thomson Reuters)*
* Total return (assuming all dividends are reinvested).

# DIRECTORS' REMUNERATION REPORT CONTINUED





### 3 ANNUAL DIRECTORS' REMUNERATION REPORT FOR THE YEAR ENDING 31 DECEMBER 2018 (AUDITED) CONTINUED

**RELATIVE SPEND ON FEES**
The following table shows the total amount spent on payments to directors with a comparator to last year, along with total distributions to shareholders by way of dividend or (where applicable) share buy-back or other distributions.

| | **2018 £'000** | 2017 £'000 |
|---|---|---|
| Total spend – directors' fees | **114** | 99 |
| Total distributed to shareholders – dividends | **–** | – |
| *– share buybacks* | **17,159** | 27,581 |

**VOTING ON REMUNERATION MATTERS AT THE 2018 AGM AND IN RESPECT OF REMUNERATION POLICY**
At the AGM on 19 April 2018 the resolution to receive and approve the directors' remuneration report for the year ended 31 December 2017 received the following votes: for – 99.99%; against – 0.01%. Votes withheld were 0.02% of the total votes cast.

The resolution to approve an increase in the aggregate amount of fees payable to the directors per annum, set out in article 95, to £200,000 received the following votes: for – 99.96%; against – 0.04%; votes withheld – 9.57% of the total votes cast.

The remuneration policy itself was last approved by shareholders in 2017 with 99.88% of votes in favour, 0.12% votes against and 0.03% votes withheld.

**MISCELLANEOUS DISCLOSURES**
The board took no external advice on remuneration matters during the year. No payments were made to former directors during the year, or to any director for loss of office.

The directors' annual remuneration report set out at section 3 above was approved by the board of directors on 19 February 2019 and signed on its behalf by

**Julian Cazalet**
Chairman

# STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland". Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis, unless it is inappropriate to assume that the Company will continue in business.

The directors are responsible for the keeping of adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements and the directors' remuneration report comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors have delegated responsibility to the manager for the maintenance and integrity of the Company's page of the manager's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The work carried out by the auditor does not involve any consideration of these matters and, accordingly, the auditor accepts no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

Each of the directors, whose names and functions are listed on page 35 confirm that, to the best of their knowledge:

- the financial statements, which have been prepared in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), give a true and fair view of the assets, liabilities, financial position and loss of the Company;
- the annual report and financial statements includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that it faces and the directors' report contains those matters required to be disclosed by applicable law; and
- they consider that the annual report and financial statements, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position, performance, business model and strategy.

By order of the board

**Julian Cazalet**
19 February 2019

Julian Cazalet

# INDEPENDENT AUDITOR'S REPORT
## TO THE MEMBERS OF HERALD INVESTMENT TRUST PLC

### OPINION
We have audited the financial statements of Herald Investment Trust plc ("the Company") for the year ended 31 December 2018 which comprise the Income Statement, the Balance Sheet, the Statement of Changes in Equity, the Cash Flow Statement and the related notes 1 to 20, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland" (United Kingdom Generally Accepted Accounting Practice).

In our opinion, the financial statements:
- give a true and fair view of the Company's affairs as at 31 December 2018 and of its loss for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

### BASIS FOR OPINION
We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report below. We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### CONCLUSIONS RELATING TO PRINCIPAL RISKS, GOING CONCERN AND VIABILITY STATEMENT
We have nothing to report in respect of the following information in the annual report, in relation to which the ISAs(UK) require us to report to you whether we have anything material to add or draw attention to:
- the disclosures in the annual report set out on page 33 that describe the principal risks and explain how they are being managed or mitigated;
- the directors' confirmation set out on page 33 in the annual report that they have carried out a robust assessment of the principal risks facing the entity, including those that would threaten its business model, future performance, solvency or liquidity;
- the directors' statement set out on page 40 in the annual report about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, and their identification of any material uncertainties to the entity's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements;
- whether the directors' statement in relation to going concern required under the Listing Rules in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit; or
- the directors' explanation set out on page 33 in the annual report as to how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the entity will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

### OVERVIEW OF OUR AUDIT APPROACH

| | |
|---|---|
| **Key audit matters** | – Incomplete or inaccurate revenue recognition.<br>– Incorrect valuation and defective title of the investment portfolio. |
| **Materiality** | – Overall materiality of £9.0m which represents 1% of net assets. |

### KEY AUDIT MATTERS
Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in our opinion thereon, and we do not provide a separate opinion on these matters.

| Risk | Our response to the risk | Key observations communicated to the Audit Committee |
|---|---|---|
| **Incomplete or inaccurate revenue recognition £11.3m (2017: £10.8m).**<br><br>As described in Accounting policies (page 56); and Note 2 (page 57) to the financial statements. The Company has reported investment income of £11.3m (2017: £10.8m). Special dividend income for the year amounted to £0.2m, of which all was treated as revenue (2017: £0.4m of which £0.3m was treated as revenue and £0.1m was treated as capital).<br><br>Special dividends by their nature require the exercise of judgment as to whether the income received should be classified as 'revenue' or 'capital' for Section 1158 of the Corporation Tax Act, 2010 purposes. For special dividends the Company determines whether amounts should be credited to the revenue or capital columns of the Income Statement based on the underlying substance of the transaction.<br><br>We focus on the recognition of revenue and its presentation in the financial statements as it is a key area for shareholders. There is a risk that an incorrect classification of revenue in the Income Statement could potentially result in the mis-representation of financial information to shareholders and put the Company's investment trust status at risk.<br><br>Specifically, in relation to our procedures over management override, we consider the risk that inappropriate journal entries are applied to the income account resulting in a manipulation of the Company's revenue to support performance targets. | We performed the following procedures:<br>– We obtained an understanding of The Bank of New York Mellon International Limited ("the Administrator") processes and controls for the recognition of investment income by performing walkthrough procedures, reviewing the Administrator's internal control reports and discussing with Herald Investment Management Limited ("the Manager") the governance structure and protocols for oversight of investment income recognition.<br>– For a sample of dividend receipts, we agreed dividends received from the income report to an independent pricing source for occurrence and measurement. We also agreed this sample to the bank statement to test the receipt of the income.<br>– We agreed all accrued dividends at the period end to the Custodian and Depositary statements, an independent pricing source, and post year-end broker statements.<br>– For one special dividend received during the year, we reviewed its recognition basis to ensure it was appropriately allocated between revenue and capital within the Income Statement.<br>– We corroborated the appropriateness of journal entry adjustments made in relation to investment income in the preparation of the financial statements with source documentation. | The results of our procedures to test investment income identified no issues with the occurrence, measurement or completeness of investment income.<br><br>We concurred with the accounting treatment adopted for a sample of special dividends.<br><br>Based on the work performed, we had nothing to communicate. |
| **Valuation and defective title of the investment portfolio.**<br><br>As described in Accounting policies (page 56); and Note 9 (page 60) to the financial statements.<br><br>Investments held at the year-end were valued at £832m (2017: £926m). Quoted investments held at the year-end were £816m (2017: £913m).<br><br>Unquoted investments held at the year-end were £16m (comprising 1.9% of the total investment portfolio) (2017: £13m comprising 1.6% of the total investment portfolio).<br><br>The valuation of the assets held in the investment portfolio is the key driver of the Company's net asset value and investment return. Incorrect asset pricing or a failure to maintain proper legal title of assets by the Company could have a significant impact on portfolio valuation and, therefore, the return generated for shareholders. | We performed the following procedures:<br>– We obtained an understanding of the Administrator's systems and controls in relation to investments by performing a walkthrough, reviewing the Administrator's internal control reports and discussing with the Manager the governance structure and protocols for oversight of the valuation for investments.<br>– We agreed the existence for 100% of the quoted and unquoted investment portfolio to third-party confirmations.<br>– We reviewed the year end reconciliation of the Company's records to those of the Custodian and Depositary and confirmed all reconciling items were appropriate.<br><br>For quoted investments:<br>– We compared the prices of 100% of the quoted investment portfolio to an independent pricing source.<br>– We recalculated the value of quoted investments in foreign currencies to verify the accuracy of the corresponding sterling balances based upon exchange rates from an external source.<br><br>For unquoted investments:<br>– For a sample of 5 positions representing 86% of their balance, we reviewed management's methodology for determining the fair value of the investments is consistent with the International Private Equity and Venture Capital Guidelines, agreed the inputs into the valuation to third party sources (such as financial statements of the issuer, investor reports and the instrument terms) and re-performed calculations to confirm their arithmetical accuracy. | The results of our procedures on existence of investments identified no material errors in the reconciliation.<br><br>The results of our procedures on the valuation of the total investment portfolio identified no material error.<br><br>Based on the work performed, we have no further observations to communicate. |

# INDEPENDENT AUDITOR'S REPORT CONTINUED
## TO THE MEMBERS OF HERALD INVESTMENT TRUST PLC

### AN OVERVIEW OF THE SCOPE OF OUR AUDIT
### TAILORING THE SCOPE

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for the company. This enables us to form an opinion on the financial statements. We take into account size, risk profile, the organisation of the company and effectiveness of controls, including controls and changes in the business environment when assessing the level of work to be performed. All audit work was performed directly by the audit engagement team.

### OUR APPLICATION OF MATERIALITY

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

**Materiality**
*The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.*

We determined materiality for the company to be £9.0million (2017: £9.7million), which is 1% (2017: 1%) of shareholders' funds. We have derived our materiality calculation based on a proportion of shareholders' funds as it is the most important financial metric on which shareholders judge the performance of the Company.

During the course of our audit, we reassessed initial materiality and made no changes to the basis of calculation from our original assessment at the planning stage.

**Performance materiality**
*The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.*

On the basis of our risk assessments, together with our assessment of the company's overall control environment, our judgement was that performance materiality was 75% (2017: 75%) of our planning materiality, namely £6.8m (2017: £7.2m). We have set performance materiality at this percentage due to our past experience of the audit that indicates a lower risk of misstatements, both corrected and uncorrected.

Given the importance of the distinction between revenue and capital for the Company we have also applied a separate testing threshold of £0.5m (2017: £0.5m) for the revenue column of the Income Statement, being the reporting threshold.

**Reporting threshold**
*An amount below which identified misstatements are considered as being clearly trivial.*

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.5m (2017: £0.5m), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

### OTHER INFORMATION

The other information comprises the information included in the Annual Report set out on pages 1 to 45, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

In this context, we also have nothing to report in regard to our responsibility to specifically address the following items in the other information and to report as uncorrected material misstatements of the other information where we conclude that those items meet the following conditions:

- **Fair, balanced and understandable** set out on page 39 – the statement given by the directors that they consider the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or
- **Audit committee reporting** set out on page 39 – the section describing the work of the audit committee does not appropriately address matters communicated by us to the audit committee; or
- **Directors' statement of compliance with the UK Corporate Governance Code** set out on page 38 – the parts of the directors' statement required under the Listing Rules relating to the company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R(2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code.

### OPINIONS ON OTHER MATTERS PRESCRIBED BY THE COMPANIES ACT 2006

In our opinion the part of the directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and directors' reports have been prepared in accordance with applicable legal requirements.

### MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or directors' report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

### RESPONSIBILITIES OF DIRECTORS

As explained more fully in the statement of directors' responsibilities set out on page 45, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

### AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE FINANCIAL STATEMENTS

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

### EXPLANATION AS TO WHAT EXTENT THE AUDIT WAS CONSIDERED CAPABLE OF DETECTING IRREGULARITIES, INCLUDING FRAUD

The objectives of our audit, in respect to fraud, are: to identify and assess the risks of material misstatement of the financial statements due to fraud; to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud, through designing and implementing appropriate responses; and to respond appropriately to fraud or suspected fraud identified during the audit. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management.

Our approach was as follows:

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Company and determined that the most significant are the Companies Act 2006, the Listing Rules, the Disclosure and Transparency Rules, the UK Corporate Governance Code 2016 and section 1158 of the Corporation Tax Act 2010.
- We understood how Herald Investment Trust plc is complying with those frameworks through discussions with the Audit Committee and company secretary, and review of the Company's documented policies and procedures.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved review of the reporting to the Directors with respect to the application of the documented policies and procedures and review of the financial statements to ensure compliance with the reporting requirements of the Company.
- We have reviewed that the Company's control environment is adequate for the size and operating model of such a listed investment company.
- We assessed the susceptibility of the financial statements to material misstatement, including how fraud might occur by considering the key risks impacting the financial statements. We identified a fraud risk with respect to management override in relation to inappropriate revenue journals. We noted no issues in agreeing a sample of revenue journal entries back to the corresponding announcements prepared from the investee companies.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at https://www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

### OTHER MATTERS WE ARE REQUIRED TO ADDRESS

- We were appointed by the company on 16 June 1994 to audit the financial statements for the year ending 31 December 1994 and subsequent financial periods.

  The period of total uninterrupted engagement including previous renewals and reappointments is 25 years, covering the years ending 31 December 1994 to 31 December 2018.
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the company and we remain independent of the company in conducting the audit.
- The audit opinion is consistent with the additional report to the audit committee.

### USE OF OUR REPORT

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Ernst & Young LLP

**Ashley Coups (Senior Statutory auditor)**
**for and on behalf of Ernst & Young LLP, Statutory Auditor**
London
19 February 2019

Notes:
1. The maintenance and integrity of the Herald Investment Trust plc web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.
2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

# Financial Statements

# INCOME STATEMENT

## For the year ended 31 December

| | Notes | 2018 Revenue £'000 | 2018 Capital £'000 | 2018 Total £'000 | 2017 Revenue £'000 | 2017 Capital £'000 | 2017 Total £'000 |
|---|---|---|---|---|---|---|---|
| (Losses)/gains on investments | 9 | – | (50,436) | (50,436) | – | 205,508 | 205,508 |
| Currency gains/(losses) | | – | 2,048 | 2,048 | – | (3,172) | (3,172) |
| Income | 2 | 11,250 | – | 11,250 | 10,799 | – | 10,799 |
| Investment management fee | 3 | (10,050) | – | (10,050) | (8,962) | – | (8,962) |
| Other administrative expenses | 4 | (719) | (7) | (726) | (578) | (5) | (583) |
| **Profit/(loss) before finance costs and taxation** | | 481 | (48,395) | (47,914) | 1,259 | 202,331 | 203,590 |
| Finance costs of borrowings | 5 | (156) | – | (156) | (514) | – | (514) |
| **Profit/(loss) before taxation** | | 325 | (48,395) | (48,070) | 745 | 202,331 | 203,076 |
| Tax | 6 | (267) | – | (267) | (259) | – | (259) |
| **Profit/(loss) after taxation** | | 58 | (48,395) | (48,337) | 486 | 202,331 | 202,817 |
| **Profit/(loss) per ordinary shares (basic and diluted)** | 8 | 0.08p | (69.67p) | (69.59p) | 0.68p | 283.44p | 284.12p |

There is no final dividend proposed (2017 – nil). *More information on dividend distributions can be found in note 7 on page 59.*

The total column of this statement is the profit and loss account of the Company, prepared in accordance with UK Accounting Standards.

The profit after taxation is the total comprehensive income and therefore no additional statement of comprehensive income is presented. The supplementary revenue and capital columns are presented for information purposes in accordance with the Statement of Recommended Practice issued by the Association of Investment Companies. All items in the above statement derive from continuing operations of the Company. No operations were acquired or discontinued in the year.

# BALANCE SHEET
## At 31 December

| | Notes | 2018 £'000 | 2018 £'000 | 2017 £'000 | 2017 £'000 |
|---|---|---|---|---|---|
| **Fixed assets** | | | | | |
| Investments held at fair value through profit or loss | 9 | | **831,680** | | 925,541 |
| **Current assets** | | | | | |
| Cash and cash equivalents | | **68,860** | | 41,870 | |
| Other receivables | 10 | **1,575** | | 1,682 | |
| | | **70,435** | | 43,552 | |
| **Current liabilities** | | | | | |
| Other payables | 11 | **(961)** | | (2,443) | |
| | | **(961)** | | (2,443) | |
| Net current assets | | | **69,474** | | 41,109 |
| **TOTAL NET ASSETS** | | | **901,154** | | 966,650 |
| **Capital and reserves** | | | | | |
| Called up share capital | 13 | | **17,225** | | 17,577 |
| Share premium | 14 | | **73,738** | | 73,738 |
| Capital redemption reserve | 14 | | **4,727** | | 4,375 |
| Capital reserve | 14 | | **804,245** | | 869,799 |
| Revenue reserve | 14 | | **1,219** | | 1,161 |
| **SHAREHOLDERS' FUNDS** | | | **901,154** | | 966,650 |
| **NET ASSET VALUE PER ORDINARY SHARE (including current year revenue)** | 15 | | **1,307.89p** | | 1,374.88p |
| **NET ASSET VALUE PER ORDINARY SHARE (excluding current year revenue)** | | | **1,307.81p** | | 1,374.20p |

The financial statements of Herald Investment Trust plc (company registration number 02879728) were approved by the board of directors and authorised for issue on 19 February 2019 and signed on its behalf by

**Julian Cazalet**
Chairman

Julian Cazalet

# STATEMENT OF CHANGES IN EQUITY

## For the year ended 31 December 2018

| | Notes | Called up share capital £'000 | Share premium £'000 | Capital redemption reserve £'000 | Capital reserve £'000 | Revenue reserve £'000 | Shareholders' funds £'000 |
|---|---|---|---|---|---|---|---|
| Shareholders' funds at 1 January 2018 | | 17,577 | 73,738 | 4,375 | 869,799 | 1,161 | 966,650 |
| (Loss)/profit after taxation | | – | – | – | (48,395) | 58 | (48,337) |
| Shares purchased for cancellation | 13 | (352) | – | 352 | (17,159) | – | (17,159) |
| **Shareholders' funds at 31 December 2018** | | **17,225** | **73,738** | **4,727** | **804,245** | **1,219** | **901,154** |

## For the year ended 31 December 2017

| | Notes | Called up share capital £'000 | Share premium £'000 | Capital redemption reserve £'000 | Capital reserve £'000 | Revenue reserve £'000 | Shareholders' funds £'000 |
|---|---|---|---|---|---|---|---|
| Shareholders' funds at 1 January 2017 | | 18,266 | 73,738 | 3,686 | 695,049 | 675 | 791,414 |
| *Profit after taxation* | | – | – | – | 202,331 | 486 | 202,817 |
| Shares purchased for cancellation | 13 | (689) | – | 689 | (27,581) | – | (27,581) |
| Shareholders' funds at 31 December 2017 | | 17,577 | 73,738 | 4,375 | 869,799 | 1,161 | 966,650 |

# CASH FLOW STATEMENT
## For the year ended 31 December

| | Notes | 2018 £'000 | 2018 £'000 | 2017 £'000 | 2017 £'000 |
|---|---|---|---|---|---|
| **(Loss)/profit before finance costs and taxation** | | **(47,914)** | | 203,590 | |
| Adjustments for losses/(gains) on investments | | **50,436** | | (205,508) | |
| (Increase)/decrease in accrued income | | **(341)** | | 8 | |
| Purchase of investments | | **(153,429)** | | (156,421) | |
| Sale of investments | | **195,948** | | 171,125 | |
| Decrease/(increase) in other receivables | | **4** | | (38) | |
| (Decrease)/increase in other payables | | **(27)** | | 119 | |
| Amortisation of fixed income book cost | | **(127)** | | (22) | |
| Effect of foreign exchange rate changes | | **(2,048)** | | 3,172 | |
| Overseas tax suffered | | **(267)** | | (259) | |
| **Net cash inflow from operating activities** | | | **42,235** | | 15,766 |
| **Finance activities** | | | | | |
| Loan repayment | 11 | **–** | | (25,000) | |
| Interest paid on loan | | **(116)** | | (582) | |
| Shares repurchased | 13 | **(17,177)** | | (27,590) | |
| **Net cash outflow from financing activities** | | | **(17,293)** | | (53,172) |
| **Increase/(decrease) in cash and cash equivalents** | | | **24,942** | | (37,406) |
| Cash and cash equivalents at start of year | | | **41,870** | | 82,448 |
| Effect of foreign exchange rate changes | | | **2,048** | | (3,172) |
| **Cash and cash equivalents at end of year** | | | **68,860** | | 41,870 |
| **Comprised of:** | | | | | |
| Cash and cash equivalents | | | **68,860** | | 41,870 |

Cash flow from operating activities includes interest received of £849,000 (2017 – £518,000) and dividends received of £9,848,000 (2017 – £9,674,000).

# NOTES TO THE FINANCIAL STATEMENTS

## 1. ACCOUNTING POLICIES

The financial statements for the year to 31 December 2018 have been prepared on the basis of the accounting policies set out below. The Company has applied 'FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland' (FRS 102), which forms part of Generally Accepted Accounting Practice ('UK GAAP') issued by the Financial Reporting Council.

### (A) ACCOUNTING CONVENTION

The financial statements are prepared on the assumption that approval as an investment trust will be retained.

The financial statements are presented in sterling, which is the Company's functional and presentational currency and the currency in which the Company's share capital and expenses, as well the majority of its assets and liabilities, are denominated.

The financial statements have been prepared in accordance with The Companies Act 2006, FRS 102 and with the Statement of Recommended Practice 'Financial Statements of Investment Trust Companies and Venture Capital Trusts' issued by the Association of Investment Companies (AIC) in November 2014 as amended in January 2017, updated in February 2018.

In order to better reflect the activities of the Company and in accordance with guidance issued by the AIC, supplementary information which analyses the profit and loss account between items of a revenue and capital nature has been presented in the income statement.

### (B) FINANCIAL INSTRUMENTS

The Company recognises financial assets and financial liabilities when the Company becomes a party to the contractual provisions of the instrument. The Company will offset financial assets and financial liabilities if the Company has a legally enforceable right to set off the recognised amounts and interests and intends to settle on a net basis.

The Company has chosen to apply the provisions of sections 11 and 12 of FRS 102 in full in respect of the financial instruments.

### (C) INVESTMENTS

Purchases and sales of investments are accounted for on a trade date basis.

All investments are at fair value through profit or loss upon initial recognition and are measured at subsequent reporting dates at fair value. The fair value of listed security investments is bid value. Investments on the Alternative Investment Market are included at their bid value. The fair value of unlisted investments uses valuation techniques determined by the directors on the basis of latest information in line with the relevant principles of the International Private Equity and Venture Capital Valuation Guidelines.

Gains and losses arising from changes in the unrealised fair value and on the sale of investments are taken to capital reserve through the income statement.

### (D) CASH AND CASH EQUIVALENTS

Cash and cash equivalents may comprise cash as well as cash equivalents (including short term deposits and money market funds which are readily convertible to a known amount of cash and are subject to an insignificant risk of change in value). Investments are regarded as cash equivalents if they meet all of the following criteria: highly liquid investments held in the Company's base currency that are readily convertible to a known amount of cash, are subject to an insignificant risk of change in value and provide a return no greater than the rate of a three-month high quality government bond.

### (E) INCOME

Dividend income is accounted for when the entitlement to the income is established (normally on the ex-dividend date). Franked income is stated net of tax credits. Foreign dividends that suffer withholding tax at source are shown gross, with the corresponding tax charge in the income statement. Unfranked investment income includes the taxes deducted at source. Interest from fixed interest securities is recognised on an effective yield basis. Underwriting commission and interest receivable on deposits are recognised on an accruals basis.

### (F) EXPENSES

All expenses are accounted for on an accruals basis and are charged through the revenue column of the income statement except where they relate directly to the acquisition or disposal of an investment (transaction costs) and are taken to the income statement as a capital item.

### (G) FINANCE COSTS

Finance costs are accounted for on an effective interest basis and are charged through the revenue column of the income statement.

**(H) DEFERRED TAXATION**
Deferred taxation is provided on all timing differences which have originated but not reversed at the balance sheet date, calculated on an undiscounted basis, and based on enacted tax rates relevant to the benefit or liability. Deferred tax assets are recognised only to the extent that it is more likely than not that there will be taxable profits from which underlying timing differences can be deducted.

**(I) FOREIGN CURRENCY**
Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date. Exchange differences of a revenue or capital nature are taken to the revenue or capital reserves respectively through the income statement.

**(J) USE OF ESTIMATES**
The preparation of financial statements requires the Company to make judgements, estimates and assumptions that affect amounts reported for assets and liabilities as at the balance sheet date and the amounts reported for revenues and expenses during the year. However, the nature of estimation means that the actual outcomes could differ from those estimates, possibly significantly. The judgements relate to the investments where there is no appropriate market price i.e. the unquoted investments.

**(K) SINGLE SEGMENT REPORTING**
The Company has only one material segment, being that of an investment trust company investing primarily in listed companies throughout the world.

## 2. INCOME

| | 2018<br>£'000 | 2017<br>£'000 |
|---|---|---|
| **Income from investments** | | |
| UK dividends from listed investments | **3,086** | 2,893 |
| UK dividends from unlisted investments (inc AIM) | **3,406** | 3,657 |
| Income from unlisted (inc AIM) UK convertible bonds | **263** | 262 |
| Overseas dividend from UK listed companies | **708** | 1,080 |
| Overseas dividend income | **2,913** | 2,358 |
| Overseas interest | **578** | 178 |
| | **10,954** | 10,428 |
| **Other income** | | |
| Other income | **–** | 272 |
| Deposit interest | **266** | 99 |
| Underwriting commission | **30** | – |
| **Total income** | **11,250** | 10,799 |
| Total income comprises: | | |
| Dividends from equity securities at fair value through profit and loss | **10,113** | 9,988 |
| Interest from financial assets at fair value through profit and loss | **841** | 440 |
| Other income | **296** | 371 |
| | **11,250** | 10,799 |

## 3. INVESTMENT MANAGEMENT FEE

| | 2018<br>£'000 | 2017<br>£'000 |
|---|---|---|
| **Investment management fee** | **10,050** | 8,962 |

Herald Investment Management Limited is appointed investment manager under a management agreement which is terminable on twelve months' notice. Their fee is calculated on a monthly rate of 0.08333% of the Company's net asset value (excluding current year net income) based on middle market prices. The management fee is levied on all assets.

# NOTES TO THE FINANCIAL STATEMENTS CONTINUED

## 4. OTHER ADMINISTRATIVE EXPENSES

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Custodian's fees | **71** | 64 |
| Registrars' fees | **38** | 41 |
| Directors' fees | **114** | 99 |
| Auditor's fees – statutory audit | **23** | 24 |
| Depositary's fees | **181** | 159 |
| Miscellaneous expenses | **292** | 191 |
| | **719** | 578 |

## 5. FINANCE COSTS OF BORROWINGS

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Bank loan* and commitment fee | **156** | 514 |
| | **156** | 514 |

* The bank loan of £25 million was repaid on 29 December 2017. The Company retains a £25 million multi-currency revolving credit facility (undrawn).

## 6. TAXATION

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| **Analysis of charge in year** | | |
| Overseas taxation | **267** | 259 |
| **Factors affecting tax charge for year** | | |
| The tax charge for the year is higher than the standard rate of corporation tax in the UK of 19.00% (2017 – 19.25%). The differences are explained below: | | |
| (Loss)/profit before taxation | **(48,070)** | 203,076 |
| (Loss)/profit multiplied by the standard rate of corporation tax in the UK of 19.00% (2017 – 19.25%) | **(9,133)** | 39,092 |
| **Effects of:** | | |
| Capital losses/(gains) not taxable | **9,583** | (39,560) |
| UK dividends not subject to UK tax | **(1,228)** | (1,261) |
| Overseas dividends not subject to UK tax | **(672)** | (662) |
| Capital (gains)/losses on foreign exchange movements not subject to tax | **(390)** | 611 |
| Disallowable expenses | **1** | 1 |
| Overseas withholding tax | **267** | 259 |
| Movement in excess management expenses | **1,839** | 1,779 |
| **Total tax charge for the year** | **267** | 259 |

As an investment trust, the Company's capital gains are not taxable.

There is no UK corporation tax charge at 31 December 2018 or 31 December 2017 as the Company has unrelieved management expenses which are available to be carried forward. The tax charge for 31 December 2018 and 2017 comprises overseas withholding taxes suffered.

At 31 December 2018, the Company had a potential deferred tax asset of £16,017,000 (2017 – £14,370,000) on taxable losses of £94 million (2017 – £85 million) which are available to be carried forward and offset against future taxable profits. A deferred tax asset has not been provided on these losses as it is considered unlikely that the Company will make taxable revenue profits in the future and it is not liable to tax on its capital gains. The potential deferred tax asset has been calculated using a corporation tax rate of 17% (2017 – 17%).

## 7. DIVIDENDS ON ORDINARY SHARES

| | 2018 | 2017 | 2018 £'000 | 2017 £'000 |
|---|---|---|---|---|
| Amounts recognised as distributions in the period: | | | | |
| Previous year's final | **nil** | nil | **nil** | nil |

Set out below are the total dividends payable in respect of the financial year, which is the basis on which the requirements of Section 1158 of the Corporation Tax Act 2010 are considered. The revenue available for distribution by way of dividend for the year ended 31 December 2018 is £58,000 (2017 – £486,000).

| | 2018 | 2017 | 2018 £'000 | 2017 £'000 |
|---|---|---|---|---|
| Amounts paid and proposed in respect of the period: | | | | |
| Proposed final dividend per ordinary share | **nil** | nil | **nil** | nil |

## 8. NET RETURN PER ORDINARY SHARE

| | 2018 Revenue | 2018 Capital | 2018 Total | 2017 Revenue | 2017 Capital | 2017 Total |
|---|---|---|---|---|---|---|
| | **0.08p** | **(69.67p)** | **(69.59p)** | 0.68p | 283.44p | 284.12p |

Revenue, capital and total return per ordinary share is based on each of the returns on ordinary activities after taxation (respectively, revenue profit of £58,000 (2017 – revenue profit of £486,000), capital loss of £48,395,000 (2017 – capital profit of £202,331,000) and total loss of £48,337,000 (2017 – total profit of £202,817,000)) and on 69,460,637 ordinary shares (2017 – 71,385,469) being the weighted average number of ordinary shares in issue during the year.

There are no dilutive or potentially dilutive shares in issue.

## 9. FIXED ASSET INVESTMENTS

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Financial assets designated at fair value through profit or loss on initial recognition | | |
| Listed UK – equity investments – London Stock Exchange | **135,253** | 147,622 |
| – AIM | **317,444** | 422,131 |
| Listed overseas – equity investments | **316,263** | 313,464 |
| Government debt securities | **46,785** | 29,445 |
| Unquoted* | **15,935** | 12,879 |
| Total investments in financial assets at fair value through profit or loss | **831,680** | 925,541 |

* The unquoted balance comprises BE Heard Group at £160,000, Blackline Safety £244,000, Business Control Solutions at £699,000, Celoxica at £217,000, EU Supply at £250,000, Freshwater UK at £113,000, Fusionex International at £1,402,000, Herald Venture II at £2,694,000, HIML at £4,047,000, Intechnology at £213,000, Intercede at £375,000, Zinc Media at £2,565,000 and ZOO Digital at £2,956,000.

# NOTES TO THE FINANCIAL STATEMENTS CONTINUED

## 9. FIXED ASSET INVESTMENTS CONTINUED

| | Listed in UK £'000 | Listed overseas £'000 | AIM £'000 | Unquoted £'000 | 2018 Total £'000 | 2017 Total £'000 |
|---|---|---|---|---|---|---|
| Cost of investments at 1 January | 64,812 | 198,854 | 237,370 | 18,650 | **519,686** | 450,812 |
| Investment holding gains/(losses) 1 January | 82,810 | 144,055 | 184,761 | (5,771) | **405,855** | 262,157 |
| Fair value of investments at 1 January | 147,622 | 342,909 | 422,131 | 12,879 | **925,541** | 712,969 |
| Movements in the year: | | | | | | |
| Purchases at cost | 16,649 | 99,282 | 35,783 | 255 | **151,969** | 156,290 |
| Sales – proceeds | (21,653) | (84,296) | (88,624) | (386) | **(194,959)** | (148,875) |
| – gains/(losses) on investments | 13,718 | 22,924 | 53,497 | (800) | **89,339** | 61,810 |
| Amortisation of fixed income book cost | – | 127 | – | – | **127** | 22 |
| Transferred from listed to AIM | (4,682) | – | 4,682 | – | – | – |
| Transferred from AIM to listed | – | 1,201 | (1,201) | – | – | – |
| Transferred from AIM to unquoted | – | – | (1,690) | 1,690 | – | – |
| Return of capital/capital special dividends | – | (445) | (76) | (41) | **(562)** | (373) |
| *Changes in investment holding (losses)/gains* | (16,401) | (18,654) | (107,058) | 2,338 | **(139,775)** | 143,698 |
| **Fair value of investments at 31 December** | **135,253** | **363,048** | **317,444** | **15,935** | **831,680** | 925,541 |
| Cost of investments at 31 December | 68,844 | 237,647 | 239,741 | 19,368 | **565,600** | 519,686 |
| Investment holding gains/(losses) 31 December | 66,409 | 125,401 | 77,703 | (3,433) | **266,080** | 405,855 |
| **Fair value of investments at 31 December** | **135,253** | **363,048** | **317,444** | **15,935** | **831,680** | 925,541 |

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| **Gains on investments** | | |
| Realised gains on sales | **89,339** | 61,810 |
| Changes in investment holding gains | **(139,775)** | 143,698 |
| | **(50,436)** | 205,508 |

The investments in the equity and fixed interest stocks of unlisted companies that the Company holds are not traded and as such the prices are more uncertain than those of more widely traded securities. The fair value of unlisted investments uses valuation techniques determined by the directors on the basis of latest information in line with the relevant principles of the International Private Equity and Venture Capital Valuation Guidelines. The fair value of unlisted investments at 31 December 2018 was £15,935,000 (2017 – £12,879,000).

At 31 December 2018 the Company was the beneficial owner of 15.4% (2017 – 15.4%) of the ordinary share capital of HIML Holdings Limited. HIML Holdings Limited is incorporated in the United Kingdom and is the parent company of the Company's manager.

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| **Transaction costs** | | |
| Commission costs: | | |
| Purchases | **201** | 339 |
| Sales | **300** | 453 |
| Total commission costs | **501** | 792 |
| Custody transaction costs | **7** | 5 |
| Other transaction costs | **53** | 66 |
| | **561** | 863 |

## 10. OTHER RECEIVABLES

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| **Due within one year:** | | |
| Income accrued and prepayments | **1,412** | 1,071 |
| Sales for subsequent settlement | **–** | 444 |
| Taxation recoverable | **163** | 167 |
| | **1,575** | 1,682 |

The carrying amount of other receivables is a reasonable approximation of fair value.

## 11. OTHER PAYABLES

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| **Amounts falling due within one year:** | | |
| Purchases for subsequent settlement | **–** | 1,477 |
| Other payables | **961** | 966 |
| | **961** | 2,443 |

Included in other payables and accruals is £758,000 (2017 – £812,000) in respect of the investment management fee.

The Company has a £25 million multi-currency revolving credit facility maturing 31 December 2019. At 31 December 2018, there were no outstanding drawings on the multi-currency revolving credit facility (2017 – £nil).

The main covenants relating to the facility are:
Total borrowings shall not exceed 25% of the Company's Total Qualifying Assets adjusted by deducting:
(i) the amount by which the market value of any single investment of the Borrower exceeds 5% of Total Qualifying Assets;
(ii) the amount by which the aggregated value of the ten largest Qualifying Assets exceeds 35% of Total Qualifying Assets; and
(iii)the amount by which the aggregated value of AIM Assets exceeds 45% of Total Qualifying Assets.

All covenants have been complied with during the year (2017 – same).

## 12. DERIVATIVE FINANCIAL INSTRUMENTS

At 31 December 2018, the Company held no open positions in derivative financial instruments (2017 – nil).

## 13. CALLED UP SHARE CAPITAL

| | 2018 Number | 2018 £'000 | 2017 Number | 2017 £'000 |
|---|---|---|---|---|
| Allotted, called up and fully paid: | | | | |
| Ordinary shares of 25p: | **68,901,568** | **17,225** | 70,307,785 | 17,577 |

At the annual general meeting on 19 April 2018, shareholders granted the Company authority to purchase shares in the market up to 10,415,889 ordinary shares (equivalent to 14.99% of its issued share capital at that date). During the year to 31 December 2018, a total of 1,406,217 (2017 – 2,754,016) ordinary shares with a nominal value of £351,554 (2017 – £688,504) were bought back and cancelled at a total cost of £17,159,129 (2017 – £27,580,701). At 31 December 2018 the Company had authority to buy back a further 9,009,672 ordinary shares. Under the provisions of the Company's articles share buy-backs are funded from the capital reserve.

# NOTES TO THE FINANCIAL STATEMENTS CONTINUED

## 14. CAPITAL AND RESERVES

| | Share premium £'000 | Capital redemption reserve £'000 | Capital reserve £'000 | Revenue reserve £'000 |
|---|---|---|---|---|
| At 1 January 2018 | 73,738 | 4,375 | 869,799 | 1,161 |
| Shares purchased for cancellation | – | 352 | (17,159) | – |
| Gains on sales | – | – | 89,339 | – |
| Changes in investment holding gains | – | – | (139,775) | – |
| Other exchange differences | – | – | 2,048 | – |
| Custody transaction costs | – | – | (7) | – |
| Profit after taxation | – | – | – | 58 |
| Balance at 31 December 2018 | 73,738 | 4,727 | 804,245 | 1,219 |

The capital reserve includes investment holding gains of £266,080,000 (2017 – gains of £405,855,000) as disclosed in note 9.

The revenue reserve represents the only reserve from which dividends can be funded.

## 15. NET ASSET VALUE PER ORDINARY SHARE

The net asset value per ordinary share and the net assets attributable to the ordinary shareholders at the year end calculated in accordance with the articles of association were as follows:

| | **2018** | 2017 | **2018 £'000** | 2017 £'000 |
|---|---|---|---|---|
| Total net assets (including current year revenue) | **1,307.89p** | 1,374.88p | **901,154** | 966,650 |
| Net revenue profit after taxation | | | **58** | 486 |
| Total net assets (excluding current year revenue) | **1,307.81p** | 1,374.20p | **901,096** | 966,164 |

Net asset value per ordinary share is based on net assets as shown above and on 68,901,568 (2017 – 70,307,785) ordinary shares, being the number of ordinary shares in issue at each balance sheet date.

## 16. CONTINGENT LIABILITIES, GUARANTEES AND FINANCIAL COMMITMENTS

There were no contingent liabilities, guarantees or financial commitments at 31 December 2018.

## 17. CAPITAL MANAGEMENT

The Company does not have any externally imposed capital requirements. The capital of the Company is the ordinary share capital and reserves as detailed in notes 13 and 14. It is managed in accordance with its investment policy in pursuit of its investment objective, both of which are detailed on page 2, and shares may be repurchased as explained on page 38.

## 18. FINANCIAL INSTRUMENTS

In accordance with the corporate objective of maximising capital appreciation the Company invests in securities on a worldwide basis. The Company makes use of gearing to achieve improved performance in rising markets. The Company's other financial instruments consist of cash and cash equivalents, short term debtors and creditors.

The main risks arising from the Company's financial instruments are:

### A. MARKET RISK

(i) Other price risk, being the risk that the value of investment holdings will fluctuate as a result of changes in market prices caused by factors other than interest rate or currency rate movement;
(ii) Interest rate risk, being the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates; and
(iii) Foreign currency risk, being the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

### B. CREDIT RISK

Being the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

The Company is exposed to counterparty credit risk from the parties with which it trades and will bear the risk of settlement default. Counterparty credit risk to the Company arises from transactions to purchase or sell investments held within the portfolio.

There were no past due nor impaired assets as of 31 December 2018 (31 December 2017 – nil).

The counterparties engaged with the Company are regulated entities and of high credit quality.

**C. LIQUIDITY RISK**
Being the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities.

These risks and the policies for managing them have been applied throughout the year and are summarised below. Further detail is contained in the strategic report on page 33.

**A. MARKET RISK**
**(i) Other Price Risk**
The Company's investment portfolio is exposed to market price fluctuations which are monitored by the manager in pursuance of the corporate objective. Listed securities held by the Company are valued at bid prices, whereas material unlisted investments are valued by the directors on the basis of the latest information in line with the relevant principles of the International Private Equity and Venture Capital Valuation Guidelines (Accounting Policy 1(c)). These valuations also represent the fair value of the investments, see note 9 on pages 59 and 60.

A full list of the Company's investments is given on pages 20 to 26. In addition, a geographical analysis of the portfolio, an analysis of the investment portfolio by broad industrial or commercial sector and a review of the 20 largest equity investments by their aggregate market value, are shown on pages 7, 13 and 16 to 19.

**Other Price Risk Sensitivity**
17.6% of the Company's equity investments at 31 December 2018 (2017 – 16.7%) were listed on the main list of the London Stock Exchange and a further 41.3% (2017 – 47.8%) on AIM. The NASDAQ Stock Exchange accounts for 24.5% (2017 – 20.9%), New York Stock Exchange for 4.1% (2017 – 3.2%) and other stock exchanges or unlisted 12.5% (2017 – 11.4%). A 10% increase in equity investment prices at 31 December 2018 would have increased total net assets and profit & loss after taxation by £78,490,000 (2017 – £89,610,000). A decrease of 10% would have the exact opposite effect. The portfolio does not target any exchange as a comparative index, and the performance of the portfolio has a low correlation to generally used indices.

The shares of Herald Investment Trust plc have an underlying NAV per share. The NAV per share fluctuates on a daily basis. In addition, there is volatility in the discount/premium the share price has to NAV.

**(ii) Interest Rate Risk**
The majority of the Company's assets are equity shares and other investments which neither pay interest nor have a maturity date. However, the Company does hold convertible bonds and Government bonds, the interest rate and maturity dates of which are detailed below. Interest is accrued on cash balances at a rate linked to the UK base rate.

At 31 December 2018, the Company had an undrawn £25 million multi-currency credit facility (2017: multi currency loan: £nil). The aim of the use of gearing is to enhance long term returns to shareholders by investing borrowed funds in equities and other assets. Gearing is actively managed. How and where borrowings are invested is reviewed by the board in consultation with the manager at every board meeting. In light of the decisions made, appropriate adjustments to the gearing position are then made by the manager.

The interest rate risk profile of the financial assets and financial liabilities at 31 December was:

**FINANCIAL ASSETS**

| | 2018 Fair value £'000 | 2018 Weighted average interest rate/ interest rate | 2018 Weighted average period until maturity/ maturity date | 2017 Fair value £'000 | 2017 Weighted average interest rate/interest rate | 2017 Weighted average period until maturity/ maturity date |
|---|---|---|---|---|---|---|
| Fixed rate: | | | | | | |
| US bonds | **46,785** | **1.6%** | **0.7 Years** | 29,445 | 1.0% | 0.8 Years |
| UK convertible bonds | **4,341** | **6.1%** | **2.1 Years** | 3,238 | 9.8% | 3.4 Years |
| Cash: | | | | | | |
| Other overseas currencies | **35,218** | **0.7%** | | 26,363 | 0.2% | |
| Sterling | **33,642** | **0.0%** | | 15,507 | 0.0% | |
| | **68,860** | | | 41,870 | | |

The benchmark rate which determines the interest payments received on cash balances is the Bank of England base rate.

# NOTES TO THE FINANCIAL STATEMENTS CONTINUED



## 18. FINANCIAL INSTRUMENTS CONTINUED

**Interest rate risk sensitivity**

**(a) Cash**

An increase of 100 basis points in interest rates as at 31 December 2018 would have a direct effect on net assets. Based on the position at 31 December 2018, over a full year, an increase of 100 basis points would have increased the profit & loss after taxation by £689,000 (2017 – £419,000) and would have increased the net asset value per share by 1.00p (2017 – 0.60p). The calculations are based on the cash balances as at the respective balance sheet dates and are not representative of the year as a whole.

**(b) Fixed rate bonds**

An increase of 100 basis points in bond yields as at 31 December 2018 would have decreased total net assets and profit & loss after taxation by £308,000 (2017 – £294,000) and would have decreased the net asset value per share by 0.45p (2017 0.42p). A decrease in bond yields would have had an equal and opposite effect. The convertible loan stocks having an element of equity are not included in this analysis as given the nature of the businesses and the risk profile of the balance sheets they are considered to have more equity like characteristics.

**(iii) Foreign Currency Risk**

The Company's reporting currency is sterling, but investments are made in overseas markets as well as the United Kingdom and the asset value can be affected by movements in foreign currency exchange rates.

Furthermore many companies trade internationally both through foreign subsidiaries, and through exports. The greatest foreign currency risk occurs when companies have a divergence in currencies for costs and revenues. A much less risky exposure to currency is straight translation of sales and profits. The list of investments on pages 20 to 26 breaks down the portfolio by geographic listing. However the location of the stock market quote only has a limited correlation to the costs, revenues and even activities of those companies, and so this note should not be regarded as a reliable guide to the sensitivity of the portfolio to currency movements. For example, the holdings in the portfolio that have suffered most from US dollar weakness are UK companies with US dollar revenues and sterling costs.

The Company does not hedge the sterling value of investments that are priced in other currencies. Overseas income is subject to currency fluctuations. The Company does not hedge these currency fluctuations because it is impossible to quantify the effect for the reasons stated above. However, from time to time the manager takes a view by holding financial assets or liabilities in overseas currencies.

*Exposure to currency risk through asset allocation by currency of listing is indicated below:*

**AT 31 DECEMBER 2018**

| | Investments £'000 | Cash and deposits £'000 | Other receivables and payables £'000 | Net exposure £'000 |
|---|---|---|---|---|
| US dollar | 269,358 | 24,077 | 200 | 293,635 |
| Norwegian krone | 6,265 | 4,537 | – | 10,802 |
| Korean won | 8,623 | – | 114 | 8,737 |
| Taiwan dollar | 15,598 | 1,569 | – | 17,167 |
| Euro | 37,293 | 5,033 | 153 | 42,479 |
| Australian dollar | 13,515 | – | – | 13,515 |
| Other overseas currencies | 12,640 | 2 | 2 | 12,644 |
| Exposure to currency risk on translation of valuations of securities listed in overseas currencies | 363,292 | 35,218 | 469 | 398,979 |
| Sterling | 468,388 | 33,642 | 145 | 502,175 |
| | 831,680 | 68,860 | 614 | 901,154 |

AT 31 DECEMBER 2017

| | Investments £'000 | Cash and deposits £'000 | Other receivables and payables £'000 | Net exposure £'000 |
|---|---|---|---|---|
| US dollar | 243,248 | 20,655 | 103 | 264,006 |
| Norwegian krone | 9,264 | 4,510 | – | 13,774 |
| Korean won | 14,505 | – | 110 | 14,615 |
| Taiwan dollar | 17,175 | 1,143 | – | 18,318 |
| Euro | 44,852 | 52 | 611 | 45,515 |
| Other overseas currencies | 14,098 | 3 | 15 | 14,116 |
| *Exposure to currency risk on translation of valuations of securities listed in overseas currencies* | 343,142 | 26,363 | 839 | 370,344 |
| Sterling | 582,399 | 15,507 | (1,600) | 596,306 |
| | 925,541 | 41,870 | (761) | 966,650 |

**Foreign currency risk sensitivity**

At 31 December 2018, had sterling strengthened by 10% (2017 – 10%) in relation to all currencies, with all other variables held constant, total net assets and profit & loss after taxation would have decreased by the amounts shown below based on the balances denominated in foreign currency. A 10% (2017 – 10%) weakening of sterling against all currencies, with all other variables held constant, would have had the exact opposite effect on the financial statement amounts. However, companies whose cost base diverges in currency terms from its sales will in the longer term have a significantly greater effect on valuation than simple translation. In the short term investee companies generally cover their currency exposure to varying degrees. There is insufficient publicly disclosed information to quantify this, but in the long term this effect is expected to dwarf simple translation of foreign listings in terms of both risk and reward, because many investee companies trade globally. Furthermore, the country of listing is not necessarily an indication of the geography of some or even any operational activities for investee companies. The manager does not use financial instruments to protect against currency movements. From time to time financial leverage has been made using debt in overseas currencies.

| | **2018 £'000** | 2017 £'000 |
|---|---|---|
| US dollar | **29,363** | 26,401 |
| Norwegian krone | **1,080** | 1,377 |
| Korean won | **874** | 1,461 |
| Taiwan dollar | **1,717** | 1,832 |
| Euro | **4,248** | 4,551 |
| Australian dollar | **1,352** | – |
| Other overseas currencies | **1,264** | 1,412 |
| | **39,898** | 37,034 |

**B. CREDIT RISK**

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment which it has entered into with the Company. The manager monitors counterparty risk on an ongoing basis.

The Company has investments in convertible loan stocks that have an element of equity. These securities are viewed as having a risk profile similar to the equity holdings. This is because the convertibles held are in nascent technology companies that may be loss making and may have weak balance sheets. For this reason these stocks are categorised as equity holdings and for risk management purposes excluded from the credit risk analysis.

**Credit Risk Exposure**

The maximum exposure to credit risk at 31 December was:

| | **2018 £'000** | 2017 £'000 |
|---|---|---|
| Fixed interest investments | **46,785** | 29,445 |
| Cash and cash equivalents | **68,860** | 41,870 |
| Other receivables | **1,575** | 1,682 |
| | **117,220** | 72,997 |

During the year the maximum exposure in fixed interest investments was £46,785,000 (2017 – £30,825,000) and the minimum £28,000,000 (2017 – £7,520,000). The maximum exposure in cash was £103,191,000 (2017 – £101,245,000) and the minimum £41,543,000 (2017 – £41,870,000).

# NOTES TO THE FINANCIAL STATEMENTS CONTINUED



**18. FINANCIAL INSTRUMENTS** CONTINUED

**C. LIQUIDITY RISK**

The Company's policy with regard to liquidity is to provide a degree of flexibility so that the portfolio can be repositioned when appropriate and that most of the assets can be realised without an excessive discount to the market price.

**Equity Securities**

The Company's unlisted investments are not readily realisable, but these only amount to 1.8% of the Company's total assets at 31 December 2018 (2017 – 1.3%).

In practice, liquidity in investee companies is imperfect, particularly those with a market value of less than £100 million. To reduce this liquidity risk it is the policy to diversify the holdings and generally to restrict the holding in any one company to less than 10% of the share capital of that company. Furthermore the guideline is for no single investment to account for more than 5% of the assets of the Company.

The market valuation of each underlying security gives an indication of value, but the price at which an investment can be made or realised can diverge materially from the bid or offer price depending on market conditions generally and particularly to each investment. 22.0% (£183 million) (2017 – 20.1% (£178 million)) of the portfolio is invested in listed stocks with a market capitalisation below £100 million, where liquidity is expected to be more limited. If these stocks had on average a realisable value 20% below the bid price the value of the total fund would be adversely affected by 4.1% (2017 – 3.7%).

**Liquidity Risk Exposure**

Contractual maturities of the financial liabilities at the year end, based on the earliest date on which payment can be required are as follows:

| | **2018 One year or less £'000** | 2017 One year or less £'000 |
|---|---|---|
| *Other payables* | **961** | 2,443 |
| | **961** | 2,443 |

**Fair Value of Financial Instruments**

The company's investments, as disclosed in the Company's balance sheet, are valued at fair value.

Nearly all of the Company's portfolio of investments are disclosed in the Level 1 category as defined in FRS 102.

Categorisation is based on the lowest level input that is significant to the fair value measure in its entirety.

The three levels set out in FRS 102 follow:

Level 1 – The unadjusted quoted price in an active market for identical assets or liabilities that the entity can access at the measurement date.

Level 2 – Inputs other than quoted prices included within Level 1 that are observable (i.e. developed using market data) for the asset or liability, either directly or indirectly.

Level 3 – Inputs are unobservable (i.e. for which market data is unavailable) for the asset or liability.

The investment manager considers observable data to be that market data that is readily available, regularly distributed or updated, reliable and verifiable, not proprietary, and provided by independent sources that are actively involved in the relevant market.

The analysis of the valuation basis for the financial instruments based on the hierarchy as at 31 December is as follows:

**AT 31 DECEMBER 2018**

| | **Level 1 £'000** | **Level 2 £'000** | **Level 3 £'000** | **Total £'000** |
|---|---|---|---|---|
| **Financial assets** | | | | |
| Equity investments | **768,960** | **–** | **10,302** | **779,262** |
| Government debt securities | **46,785** | **–** | **–** | **46,785** |
| Other debt securities | **–** | **–** | **5,633** | **5,633** |
| **Total investments** | **815,745** | **–** | **15,935** | **831,680** |

AT 31 DECEMBER 2017

| | Level 1 £'000 | Level 2 £'000 | Level 3 £'000 | Total £'000 |
|---|---|---|---|---|
| **Financial assets** | | | | |
| *Equity investments* | 883,217 | – | 8,349 | 891,566 |
| Government debt securities | 29,445 | – | – | 29,445 |
| Other debt securities | – | – | 4,530 | 4,530 |
| **Total investments** | **912,662** | – | **12,879** | **925,541** |

**19. RELATED PARTY DISCLOSURE**
Under UK GAAP, the Company has identified the directors as related parties. The directors' emoluments and interests have been disclosed on page 43 with additional disclosure in note 4. No other related parties have been identified.

*Details of the manager's services and fees are disclosed in the strategic report on page 34 and in notes 3 and 11.*

**20. POST BALANCE SHEET EVENTS**
Any significant events that occurred after the end of the reporting period but before the signing of the statement of financial position will be shown here.

There are no significant events after the end of the reporting period requiring disclosure.

# NOTICE OF ANNUAL GENERAL MEETING



Notice is hereby given that the annual general meeting of Herald Investment Trust plc will be held at 10–11 Charterhouse Square, London EC1M 6EE on 16 April 2019 at 11.30 am for the following purposes:

To consider and, if thought fit, approve resolutions 1 to 10 as ordinary resolutions and resolution 11 as a special resolution.

**ORDINARY RESOLUTIONS**

1. To receive and adopt the directors' report, the strategic report and the financial statements and the auditor's report in respect of the year ended 31 December 2018.
2. To approve the directors' remuneration report for the year ended 31 December 2018.
3. To elect Ian Russell as a director of the Company.
4. To elect Stephanie Eastment as a director of the Company.
5. To re-elect Tom Black as a director of the Company.
6. To re-elect Karl Sternberg as a director of the Company.
7. To re-elect James Will as a director of the Company.
8. To reappoint Ernst & Young LLP as independent auditor of the Company to hold office until the conclusion of the next annual general meeting at which financial statements are laid before the Company.
9. To authorise the audit committee to determine the remuneration of the independent auditor.
10. That, pursuant to article 174 of the Company's articles of association, the Company will continue to operate as an investment trust company until the conclusion of the annual general meeting of the Company to be held in 2022.

**SPECIAL RESOLUTION**

11. That, the Company be generally and subject as hereinafter appears unconditionally authorised in accordance with Section 701 of the Companies Act 2006 (the 'Act') to make market purchases (within the meaning of Section 693(4) of the Act) of its issued shares of 25p each in the capital of the Company in substitution for any existing authority under section 701 of the Act but without prejudice to any exercise of any such authority prior to the date hereof.

**PROVIDED ALWAYS THAT**

(i) the maximum number of shares hereby authorised to be purchased shall be 14.99% of the issued share capital on the date on which this resolution is passed;

(ii) the minimum price which may be paid for a share shall be 25p;

(iii) the maximum price (exclusive of expenses) which may be paid for a share shall not be more than the higher of (a) 5% above the average mid closing price (as derived from the Daily Official List of the London Stock Exchange) for the shares for the five business days immediately preceding the date of purchase and (b) the higher of the last independent trade and the highest current independent bid on the London Stock Exchange;

(iv) any purchase of shares will be made in the market for cash at prices below the prevailing net asset value per share (as determined by the directors);

(v) unless previously varied, revoked or renewed, the authority hereby conferred shall expire at the conclusion of the annual general meeting of the Company to be held in 2020; and

(vi) the Company may make a contract to purchase shares under the authority hereby conferred prior to the expiry of such authority and may make a purchase of shares pursuant to any such contract notwithstanding such expiry.

By order of the Board
**Law Debenture Corporate Services Limited**
**Secretary**

Registered Office:
10–11 Charterhouse Square London EC1M 6EE
19 February 2019

NOTES

1. As a member you are entitled to appoint a proxy or proxies to exercise all or any of your rights to attend, speak and vote at the AGM. A proxy need not be a member of the Company but must attend the AGM to represent you. You may appoint more than one proxy provided each proxy is appointed to exercise rights attached to different shares. You can only appoint a proxy using the procedure set out in these notes. You may not use any electronic address provided either in this notice or any related documents to communicate with the Company for any purpose other than those expressly stated.

2. Shareholders are asked to use the online proxy voting service offered by Link Asset Services at www.signalshares.com to vote or appoint a proxy online. Votes must be received no later than 48 hours (excluding non-working days) before the time of the meeting or any adjourned meeting. To vote online, the unique personal identification Investor code printed on your share certificate will be required. Shareholders who are unwilling or unable to vote digitally can 'opt-in' to receive a paper proxy card by telephoning the shareholder helpline on 0871 664 0300.

3. To be valid any hard copy proxy form or other instrument appointing a proxy, together with any power of attorney or other authority under which it is signed or a certified copy thereof, must be received by post or (during normal business hours only) by hand at the Registrars of the Company at Link Asset Services, 34 Beckenham Road, Beckenham, BR3 4TU no later than 48 hours (excluding nonworking days) before the time of the meeting or any adjourned meeting.

4. CREST members who wish to appoint a proxy or proxies through the CREST electronic proxy appointment service may do so by using the procedures described in the CREST Manual and/or by logging on to the website www.euroclear.com/CREST. CREST personal members or other CREST sponsored members, and those CREST members who have appointed a voting service provider(s), should refer to their CREST sponsor or voting service provider(s), who will be able to take the appropriate action on their behalf.

5. In order for a proxy appointment or instruction made using the CREST service to be valid, the appropriate CREST message (a 'CREST Proxy Instruction') must be properly authenticated in accordance with Euroclear UK & Ireland Limited's specifications, and must contain the information required for such instruction, as described in the CREST Manual. The message, regardless of whether it constitutes the appointment of a proxy or is an amendment to the instruction given to a previously appointed proxy must, in order to be valid, be transmitted so as to be received by the Company's registrar (ID RA10) no later than 48 hours (excluding nonworking days) before the time of the meeting or any adjournment. For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by the CREST Application Host) from which the Company's registrar is able to retrieve the message by enquiry to CREST in the manner prescribed by CREST. After this time any change of instructions to proxies appointed through CREST should be communicated to the appointee through other means.

6. CREST members and, where applicable, their CREST sponsors, or voting service providers should note that Euroclear UK & Ireland Limited does not make available special procedures in CREST for any particular message. Normal system timings and limitations will, therefore, apply in relation to the input of CREST Proxy Instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member is a CREST personal member, or sponsored member, or has appointed a voting service provider(s), to procure that his CREST sponsor or voting service provider(s) take(s)) such action as shall be necessary to ensure that a message is transmitted by means of the CREST system by any particular time. In this connection, CREST members and, where applicable, their CREST sponsors or voting system providers are referred, in particular, to those sections of the CREST Manual concerning practical limitations of the CREST system and timings.

7. The Company may treat as invalid a CREST Proxy Instruction in the circumstances set out in Regulation 35(5)(a) of the Uncertificated Securities Regulations 2001.

8. The submission of a completed proxy form or other instrument of proxy will not prevent you attending the AGM and voting in person if you wish.

9. Pursuant to Regulation 41 of the Uncertificated Securities Regulations 2001 and Section 311 of the Companies Act 2006 the Company specifies that to be entitled to attend and vote at the AGM (and for the purpose of the determination by the Company of the votes they may cast), shareholders must be registered in the Register of Members of the Company no later than 48 hours (excluding non-working days) prior to the commencement of the AGM or any adjourned meeting. Changes to the Register of Members after the relevant deadline shall be disregarded in determining the rights of any person to attend and vote at the meeting.

10. Any person to whom this notice is sent who is a person nominated under Section 146 of the Companies Act 2006 to enjoy information rights (a 'Nominated Person') may, under an agreement between him/her and the shareholder by whom he/she was nominated, have a right to be appointed (or to have someone else appointed) as a proxy for the AGM. If a Nominated Person has no such proxy appointment right or does not wish to exercise it, he/she may, under any such agreement, have a right to give instructions to the shareholder as to the exercise of voting rights.

11. The statement of the rights of shareholders in relation to the appointment of proxies in Notes 1 and 3 above does not apply to Nominated Persons. The rights described in those Notes can only be exercised by shareholders of the Company.

12. The members of the Company may require the Company to publish, on its website, (without payment) a statement (which is also passed to the auditors) setting out any matter relating to the audit of the Company's accounts, including the auditors' report and the conduct of the audit. The Company will be required to do so once it has received such requests from either members representing at least 5% of the total voting rights of the Company or at least 100 members who have a relevant right to vote and hold shares in the Company on which there has been paid up an average sum per member of at least £100. Such requests must be made in writing and must state your full name and address and be sent to the Company at 10–11 Charterhouse Square, London, EC1M 6EE.

13. Information regarding the AGM, including information required by Section 311A of the Companies Act 2006, is available from the Company's page of the manager's website at www.heralduk.com.

14. Members have the right to ask questions at the meeting in accordance with Section 319A of the Companies Act 2006.

15. As at 18 February 2019 (being the last practicable date prior to the publication of this notice) the Company's issued share capital consisted of 68,391,977 ordinary shares, carrying one vote each. Therefore, the total voting rights in the Company as at 18 February 2019 were 68,391,977 votes.

16. Any person holding 3% or more of the total voting rights of the Company who appoints a person other than the Chairman of the meeting as his proxy will need to ensure that both he and his proxy complies with their respective disclosure obligations under the UK Disclosure and Transparency Rules.

17. No director has a contract of service with the Company.

# FURTHER SHAREHOLDER INFORMATION

**HOW TO INVEST**
The Company's shares are traded on the London Stock Exchange. They can be bought by placing an order with a stockbroker or an online share dealing platform or by asking a professional adviser to do so.

**SOURCES OF FURTHER INFORMATION ON THE COMPANY**
The price of shares is quoted daily in the Financial Times, The Daily Telegraph and The Times. The NAV per share is calculated and released daily to the London Stock Exchange and monthly to the Association of Investment Companies.

**KEY DATES**
If a dividend is declared in respect of a financial year, it is normally paid late April/early May. The AGM is normally held in April.

**TAXATION**
The price of the ordinary shares (adjusted for the price of attributable warrants) on 21 February 1994, which was the first day of trading, was 90.9p. The amount attributable to the warrants for the purpose of capital gains tax is 9.1p per share issued (1994 Annual Report). Any shareholder uncertain of his or her position is recommended to seek expert advice.

**ISAS**
The ordinary shares of the Company are qualifying investments for individual saving accounts.

**ELECTRONIC PROXY VOTING**
If you hold stock in your own name you should vote by returning proxies electronically at www.signalshares.com. If you have any questions about this service please contact Link Asset Services on 0871 664 0300 (overseas +44 (0)371 664 0300) (calls cost 12p per minute plus your phone company's access charge; or applicable international rate; lines are open 9.00 am to 5.30 pm Monday-Friday). Shareholders who wish to do so can obtain a hard copy proxy form by calling the above number or writing to the registrar at: Link Asset Services, 34 Beckenham Road, Beckenham, BR3 4TU.

**MAINSTREAM INVESTMENT**
The Company conducts its affairs so that its ordinary shares are capable of being recommended by independent financial advisors to ordinary retail investors in accordance with relevant FCA rules. Our ordinary shares are, we consider, mainstream investment products because they are shares in an investment trust. The Company intends to continue conducting its affairs for the foreseeable future so that the ordinary shares can continue to be categorised as mainstream.

**KEY INFORMATION DOCUMENT ("KID")**
From 1 January 2018 we are required to make a KID available to retail investors in the Company. The KID provides key information about the Company's shares as an investment product. The information is required by law to help potential shareholders understand the nature, risks, costs, potential gains and losses of the Company's shares and to help them compare it with other products. The KID can be viewed at https://www.heralduk.com/the-packaged-retail-and-insurance-based-investment-products-regulation-priips/

The Company is an investment trust. Investment trusts offer investors the following:

- Participation in a diversified portfolio of shares.
- Constant supervision by experienced professional managers.
- The Company is free from capital gains tax on capital profits realised within the portfolio.
- The opportunity to achieve improved performance for shareholders' funds in rising markets by the borrowing of additional money.

**SECRETARY**
Law Debenture
Corporate Services Limited

**REGISTERED OFFICE**
10–11 Charterhouse Square
London
EC1M 6EE

**ADMINISTRATOR**
The Bank of New York Mellon

**COMPANY NUMBER**
**02879728**
(England and Wales)

**ALTERNATIVE INVESTMENT FUND MANAGER AND PORTFOLIO MANAGER**
Herald Investment Management Limited
10–11 Charterhouse Square
London
EC1M 6EE
Tel: 020 7553 6300
Fax: 020 7490 8026
Website: www.heralduk.com
E-mail: info@heralduk.com

**INDEPENDENT AUDITOR**
Ernst & Young LLP
25 Churchill Place
Canary Wharf
London
E14 5EY

**ADVISERS**

**SOLICITORS**
Macfarlanes LLP
20 Cursitor Street
London
EC4A 1LT

**STOCKBROKERS**
N+1 Singer
One Bartholomew Lane
London
EC2N 2AX

Peel Hunt LLP
Moor House
120 London Wall
London
EC2Y 5ET

**BANKERS**
The Bank of New York Mellon
One Piccadilly Gardens
Manchester
M1 1RN

**REGISTRARS**
Link Asset Services
The Registry
34 Beckenham Road
Beckenham
Kent BR3 4TU
Tel: 0871 664 0300
(overseas +44 (0)371 664 0300)

(calls cost 12p per minute plus your phone company's access charge; or applicable international rate; lines are open 9.00 am to 5.30 pm Monday–Friday)

Website: www.signalshares.com
E-mail: enquiries@linkgroup.com

**DEPOSITARY AND CUSTODIAN**
The Bank of New York Mellon (International) Limited
1 Canada Square
London
E14 5AL

# ALTERNATIVE PERFORMANCE MEASURES

Alternative performance measures are numerical measures of the Company's current, historical or future performance, financial position or cash flows, other than financial measures defined or specified in the financial framework that the Company has chosen to apply (FRS 102 and the AIC SORP). The directors use these measures as a means of assessing the Company's performance. The measures are particularly relevant for investment trusts and are widely used across the investment trust sector.

**NET ASSET VALUE ('NAV') PER ORDINARY SHARE**
The value of the Company's assets less any liabilities for which the Company is responsible, divided by the number of shares in issue. See note 15 on page 62. The NAV per ordinary share is published daily.

The change in NAV per share (see total return below) during 2018, as shown on page 1, is calculated by taking 2018 total return and dividing by the opening NAV for the year (that is, the NAV disclosed for 31 December 2017).

**ONGOING CHARGES**
The ongoing charges have been calculated in accordance with AIC guidelines: annualised charges (total expenses), excluding non-recurring expenses and interest, incurred by the Company, divided by the average daily net asset values throughout the year.

The ongoing charges are derived in accordance with the following table:

| | **2018 £'000** | 2017 £'000 |
|---|---|---|
| Investment management fee | **10,050** | 8,962 |
| Other administrative expenses | **726** | 583 |
| Less non-recurring expenses | **(44)** | (3) |
| Ongoing charges | **10,732** | 9,542 |
| Average net assets £'000 | **998,889** | 884,785 |
| Ongoing charges figure | **1.07%** | 1.08% |

**TOTAL RETURN**
The return on the share price or NAV taking into account the movement of share price, NAV and the dividends (if any) paid to shareholders, assuming these are reinvested in the Company at the prevailing NAV/share price.

**Herald Investment Trust plc**
10–11 Charterhouse Square
London EC1M 6EE
020 7553 6300
www.heralduk.com