VCT RESEARCH REPORT

DOWNING ONE VCT

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RICHARD TROUE
HEAD OF INVESTMENT ANALYSIS

Generalist

Generalist VCTs primarily invest in unquoted companies in a wide variety of sectors and stages of development.

This report is not a substitute for reading the prospectus, and any decision to invest must be made purely on the basis of the prospectus.

Risk factors
VCTs are substantially higher risk than mainstream equities. They invest in smaller companies, which can be prone to failure. VCT shares are difficult to buy and sell – the market price may not reflect the value of the underlying investments.

The value of the shares will fluctuate, income is not guaranteed and investors could lose money. Tax and VCT rules can change and tax benefits depend on individual circumstances. If a VCT loses its qualifying status investors may have to repay any tax rebate. The prospectus will give fuller details of the risks.

Their place in a portfolio
VCTs must be held for five years in order to retain the tax relief, but a ten-year view would be better as dividends are the primary source of returns as the VCT portfolio matures.

VCTs are sophisticated, long-term investments only suitable for inclusion in significant portfolios. The general view is that they should account for no more than 10% of an equity portfolio. It is difficult to access the capital invested in the short term, and anyone considering an investment should ensure they are comfortable with this, and all other risks. We assume investors will make their own assessment of their expertise and the suitability of a VCT for their circumstances. Those with any doubts should seek expert advice.

OFFER SUMMARY

Funds	Downing ONE VCT
Amount seeking	£10 million
Minimum investment	£5,000

OUR VIEW

In November 2013 Downing merged six of their evergreen generalist VCTs to create the Downing ONE VCT. It combines Downing's approach of focusing on unquoted businesses with significant tangible

assets (usually freehold property); renewable energy projects; and investing in AIM-listed companies. It is well-diversified across a variety of sectors and types of company, with the aim of providing a stable income and some capital growth.

While the merger has created a larger, more diversified VCT, which should result in lower costs, we would like to see a longer track record of strong performance following the merger before becoming more positive.

WHAT ARE GENERALIST VCTs?

Generalist VCTs are relatively broad-based, usually investing in a range of unquoted companies across a wide variety of sectors. Some target companies which are already established and profitable, while others have a bias towards very small businesses at an early stage of their development. Most aim to provide steady dividends to investors with the potential for higher payments if and when they sell successful investments. They also aim to maintain or steadily grow capital over the long term, although there are no guarantees.

HARGREAVES LANSDOWN

One College Square South,
Anchor Road, Bristol, BS1 5HL
www.hl.co.uk

Regardless of the type of company Downing places an emphasis on finding talented entrepreneurs and management teams with a track record of running successful businesses.

Investors should ensure they are comfortable with an individual VCT's approach and risks before investing. We believe building a portfolio of different VCTs is sensible as the diversification reduces risk. Starting by selecting those focusing on more mature, established companies; and then adding higher risk VCTs targeting early-stage companies to an already diverse portfolio could be wise. While the VCT must be held for five years to benefit from the tax relief, we believe 10 years plus is a more realistic time horizon.

PHILOSOPHY

This VCT is managed using a hybrid approach, aiming to generate a stable income from asset-backed investments and renewable energy projects; and capital growth from investments in AIM-listed companies. Regardless of the type of company Downing places an emphasis on finding talented entrepreneurs and management teams with a track record of running successful businesses.

COMPANY CASE STUDY

Cadbury House Holdings Limited is an example of an unquoted investment. The company owns and operates a health club, restaurant and conference centre at Cadbury House, near Bristol which trades as The DoubleTree by Hilton, Bristol. The restaurant trades as a Marco Pierre White Steakhouse Bar and Grill. During its last accounting period the company made a small profit of £0.1 million on turnover of £7.7 million.

Science in Sport is an example of an AIM-listed investment. It is a leading sports nutrition company that develops, manufactures and markets sports nutrition products for professional athletes and sports enthusiasts. The Company floated on AIM in August 2013 and is not yet profitable, but has turnover of £6.8 million.

PERFORMANCE & DIVIDENDS

There is a dividend target of 4% a year based on the NAV. Dividends are expected to be paid twice each year in February and August. Since the launch of this VCT just over a year ago dividends totalling 4p per share have been paid. The next dividend of 2p per share will be paid on 20 February 2015 to shareholders on the register at 30 January 2015. Over the long term the team also hopes to generate capital growth from the portfolio of AIM-listed investments. There are no guarantees target returns can be met.

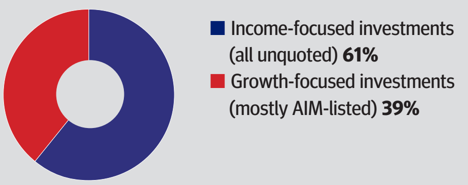
PORTFOLIO CONSTRUCTION

The majority of the portfolio will be invested in income-generating assets, which will account for between 50% and 75% of qualifying investments. This is likely to include asset-backed investments in unquoted companies and renewable energy projects. For the asset-backed deals there will be an emphasis on companies trading from freehold premises, such as pubs, health clubs and children's nurseries. Companies in the leisure, real estate and healthcare sectors lend themselves to this type of VCT as investments can be secured against the property they own.

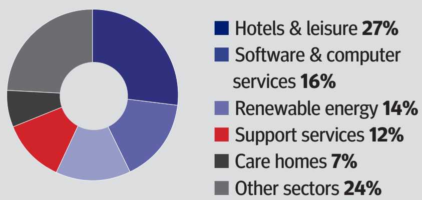
Renewable energy investments currently include solar power, hydroelectricity generation and anaerobic digestion projects. Once operational renewable energy projects generate revenue from government subsidies and from selling power in the open market. Government subsidies (which are often linked to inflation) provide relative stability over the level of returns and help provide the VCT with a steady income. From April 2015 renewable energy companies which benefit from energy generation subsidies will no longer qualify for VCT investment so no new renewable energy projects are likely to be included after this.

Growth-focused investments will tend to account for 25% to 50% of the qualifying portfolio. These will predominantly be AIM-listed companies, but also some unquoted companies where the team believe there are good prospects for capital growth. The charts below show the breakdown of the portfolio by category and sector.

Portfolio breakdown - investment type



Portfolio breakdown - sector split



ABOUT THE MANAGER

Downing has specialised in tax-efficient investments for over 25 years. The primary focus has been on investments in businesses that trade from freehold premises (where in the event of poor trading there will usually be value in the property); AIM-listed companies; and more recently renewable energy businesses benefiting from government subsidies (whose performance can be forecast with a certain level of accuracy).

Downing has a 10-strong team that focuses on unearthing new unquoted investment opportunities, including a dedicated renewable energy specialist. Members of this team are responsible for meeting management and conducting due diligence. A 13-strong portfolio team is responsible for monitoring investments on an on-going basis. A team of three individuals is responsible for analysing and selecting investments for the AIM portfolio. Downing estimates there will typically be between 20 and 25 AIM-listed holdings and upwards of 70 unquoted holdings in the portfolio.

As well as looking for strong management teams and significant assets the team also looks for businesses with stable revenues or cash flows and a scalable business model. In contrast, early stage and start-up companies will be avoided as will more speculative companies where there are no tangible assets or there is no evidence of a business model capable of sustainable growth. They also generally avoid companies with existing bank debt that would rank ahead of the VCT if the company were to fail. Downing often backs successful entrepreneurs more than once and the relationships they have built over the years have contributed to deal flow remaining strong recently.

Hargreaves Lansdown is able to offer a discount of 2.25% off the initial charge.

CHARGES & FEES

The initial charge is 4%. Hargreaves Lansdown is able to offer a discount of 2.25% off the initial charge. In addition, for applications accepted before 6 March 2015 there is a further discount of 1%. The following net initial charges therefore apply (please note discounts are paid in the form of additional shares):-

	Net initial charge
Applications accepted before 06 March	0.75%
Applications accepted after 06 March	1.75%

The annual management charge is 1.8%. There are also other fees and expenses. Unusually for a VCT there is no performance-related fee which we view as a significant positive. Full details of the charges and fees can be found in the prospectus. Investors should ensure they are comfortable with the charging structure and risks before investing.

SHARE BUY BACK POLICY

Downing will aim to maintain a maximum discount to NAV of 5% although share buybacks are at the discretion of the Board and there are no guarantees the target can be met. Please refer to the prospectus for further details. VCT shares must be held for five years to retain the tax relief.

HOW TO APPLY

To apply please read the prospectus for the offer and fill out the application form at the back. The prospectus is available to download from the Hargreaves Lansdown website or by calling **0117 900 9000**.

The signed application and a cheque for the amount to be subscribed should be returned to Hargreaves Lansdown. The cheque should be made payable to the VCT, as indicated in the prospectus, but the application and cheque must be returned to Hargreaves Lansdown in order to benefit from our discount.

We will acknowledge applications and share certificates and tax certificates will be sent once the shares have been allotted. Shares are allotted periodically and allotment could take a number of months following the acceptance of an application. Shares will be issued according to the most recently announced NAV per share of the VCTs, adjusted for the costs of the offer.

Dividends can be paid by cheque or into a bank account. Please see the relevant section of the prospectus and application form for further details.