VCT RESEARCH REPORT

HARGREAVE HALE AIM VCTS

www.hl.co.uk
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HEAD OF INVESTMENT ANALYSIS

AIM

AIM VCTs primarily invest in companies that are listed or are about to list on the Alternative Investment Market.

Exclusive 2% discount via Hargreaves Lansdown - act by 16 January

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 you could get back less than you invest. Tax and VCT rules can change and tax benefits depend on your 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
We feel VCTs should account for no more than 10% of an equity portfolio. They 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 only suitable for sophisticated long-term investors with significant portfolios. They are unlikely to be suitable for investors who may need access to their money in the short term, or for whom loss of the investment will cause hardship. We assume you will make your own assessment of your expertise and the suitability of a VCT for your circumstances. If you have any doubts you should seek expert advice.

OFFER SUMMARY

Funds	Hargreave Hale AIM VCT & Hargreave Hale AIM VCT 2
Amount seeking	£20m
Minimum investment	£2,500 in each VCT and a minimum aggregate investment of £5,000
Split	Investors can choose either or both, subject to the minimums above

OUR VIEW

This is our preferred option for investors seeking exposure to AIM-listed companies in a VCT. A stronger economy over the past year has given many companies the confidence to issue new shares and raise money to fund growth and exciting new projects.

AIM provides a wealth of under-researched opportunities. Giles Hargreave and Oliver Bedford, co-managers of the VCTs, have proved adept at uncovering businesses with excellent potential and they are encouraged by the number of high-quality investment opportunities they are seeing.

We have long held Giles Hargreave and his team in high regard and their experience makes these VCTs stand out from the crowd.

WHO SHOULD CONSIDER AIM VCTs?

London's Alternative Investment Market (AIM) is often where young, growing companies choose to list their shares. Some successful, well-known and large businesses, such as online fashion retailer ASOS, are also listed on AIM. This creates opportunities to invest in established and profitable, as well as new and exciting businesses. It is higher risk as not all will succeed. AIM VCTs could be considered by investors seeking tax-efficient exposure to smaller companies alongside a well-diversified portfolio of mainstream investments and other VCTs.

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PHILOSOPHY

Both VCTs are managed using the same strategy. The team aims to invest the core of the portfolios in established and profitable businesses with the potential for strong earnings growth. There is also exposure to companies at an earlier stage of their development, which is higher risk.

COMPANY CASE STUDY

Cohort: The experience and contacts of the Hargreave Hale team often yield good opportunities. They invested in Cohort, having known the Chairman, Nick Prest, from his time at Alvis, which he led from 1996 through to its sale to BAE in 2004. Cohort is a sizeable niche defence technology company that supports a variety of platforms from the UK's Astute Class submarine to the Tornado and Typhoon fighters:-

- First investment made in 2006 when the company listed on AIM as a small defence consultancy business with revenues of £14m.
- Revenues have increased 400% to £70m and profits before tax have reached £8m.
- Whilst large MOD contracts can be lumpy and difficult to secure, the programmes are often for extended periods of time, one of the reasons why the company has £82m of revenue under contract.
- The company is cash generative and had £16m of net cash as of 30 April 2014.
- Cohort is a good example of a mature company found in the VCTs.

Audioboom: For most people, listening to the radio is a secondary activity, undertaken while walking, driving, or doing chores. Audioboom is seeking to revolutionise the way we listen to digital audio content such as news, sport and entertainment through its smartphone app:-

- It provides content from over 1,000 partners including the BBC, Sky, BMG, talkSPORT and The Guardian.
- Over time the Audioboom app learns a user's preferences and sends customised content to their internet-enabled smartphone, which can be downloaded for offline consumption.
- Growth has been impressive, with 3 million registered users so far, 28 million monthly active users and 260m page impressions reported in August 2014.
- Revenues are low, but expected to build in 2015 with a maiden profit in 2016.
- This is a good example of an earlier stage, higher risk investment.

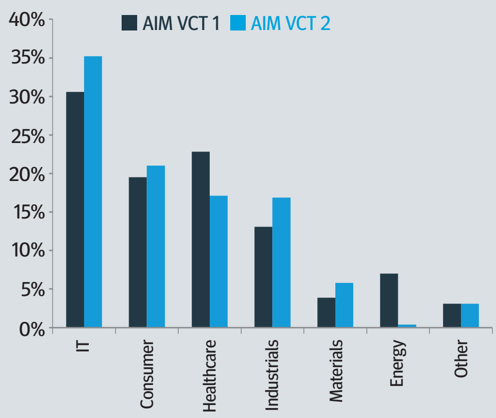
PORTFOLIO CONSTRUCTION

The VCTs hold a diversified selection of businesses across a range of sectors, as shown below. There are currently 61 qualifying investments in AIM VCT 1 and 54 in AIM VCT 2.

Small positions are initially taken in target companies and then increased over time as confidence grows. The maximum investment in a single company is likely to be 7% to 8%, but profits will often be taken before this. Beyond this level the portfolio can become overly reliant on a small number of companies; we therefore like this pragmatic approach.

There are some differences between the two portfolios due to their different ages and the timing of buying and selling certain stocks, but overall there is a high degree of overlap. We believe splitting an investment between the two could be sensible for most investors.

Part of the portfolio is also likely to be invested in the Marlborough Special Situations Fund and/or cash depending on stock market conditions. The aim of this is to enhance returns and reduce volatility, but there are no guarantees this will succeed.



Source: Hargreave Hale
(as at 30/06/2014 for VCT1 and 31/08/2014 for VCT2)

PERFORMANCE & DIVIDENDS

Like traditional smaller company unit trusts and OEICs, AIM VCTs aim to generate capital growth, but the VCT rules allow them to pay out the majority of this capital growth to investors in the form of tax-free dividends. Please remember dividends are not guaranteed. The team also aims to grow the NAV of both VCTs over the long term with less volatility overall than the AIM market.

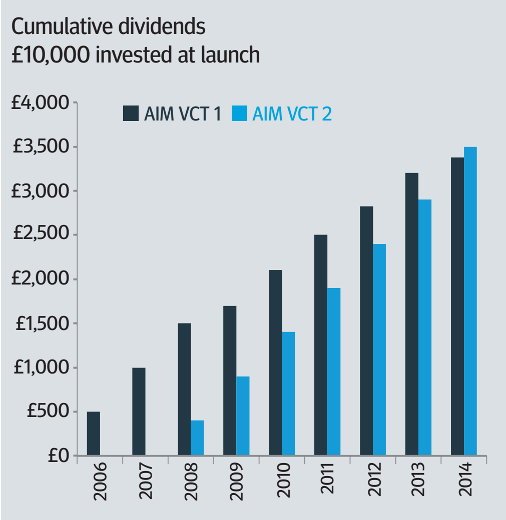
	Hargreave Hale AIM VCT 1	Hargreave Hale AIM VCT 2
Annual dividend target	5% of NAV	5% of NAV
Payment frequency	Semi-annually	Semi-annually
Current yield	4.79%	5.74%

	Hargreave Hale AIM VCT 1		Hargreave Hale AIM VCT 2	
Financial year	Dividend paid (p)	Year end NAV yield	Dividend paid (p)	Year end NAV yield
2006	5p	4.70%	-	-
2007	5p	4.80%	-	-
2008	5p	7.60%	4p	4.10%
2009	2p	3.10%	5p	5.20%
2010	4p	6.40%	5p	4.90%
2011	4p	6.50%	5p	4.60%
2012	3.25p	5.30%	5p	5.20%
2013	3.75p	5.2%	5p	5.20%
2014	1.75p*	-	-	-

Source: Hargreave Hale to 31/08/2014. *Interim dividend only

The AIM VCTs will perform differently from the other smaller company funds advised by Hargreave Hale. Historically the results have been more mixed in the VCTs, partly due to having more concentrated, less frequently traded portfolios and holding more cash. We believe they are adept at finding winning companies and over the long-term the VCTs could achieve attractive results for adventurous investors.

The table and chart below show the annual dividends paid and the cumulative dividends to date, based on a £10,000 investment at launch.



Source: Hargreave Hale to 31/08/2014.

ABOUT THE MANAGER

Hargreave Hale advises approximately £2 billion across a number of smaller company funds. Giles Hargreave and the wider Hargreave Hale team are best known for advising the Marlborough Special Situations, UK Micro Cap Growth, Nano Cap and Multi-Cap Income funds many of which feature on our Wealth 150 list of favourite open-ended funds across the major sectors, but the VCTs are managed using a similar philosophy.

Few can claim to have the strength and depth of the Hargreave Hale team when it comes to researching AIM and smaller company investments. Giles Hargreave and Oliver Bedford are supported by a team of 11, all of whom can contribute ideas to the VCTs. Indeed, companies held in the VCTs can ultimately graduate into other funds advised by Hargreave Hale so it is in the team's best interest to collaborate to identify good opportunities from an early stage.

Most research is done in-house and the team places great emphasis on getting to know companies well from an early stage and assessing the quality of management. They meet target companies regularly and also assess their customers, suppliers and competitors to build knowledge of the company and industry over time. This is a labour intensive process and a large team is an advantage in this respect. Ultimately they are looking for companies in a strong financial position and with the potential to grow earnings strongly.

Hargreaves Lansdown is offering an exclusive 'early bird' discount of 2% off the initial charge

CHARGES & FEES

The initial charge is 3.5%. Hargreaves Lansdown is offering an exclusive 'early bird' discount of 2% off the initial charge for applications accepted before 16 January 2015. This discount is only available through Hargreaves Lansdown. After 16 January 2015 the discount falls to 1%. The following net initial charges therefore apply (please note discounts are applied in the form of additional shares):-

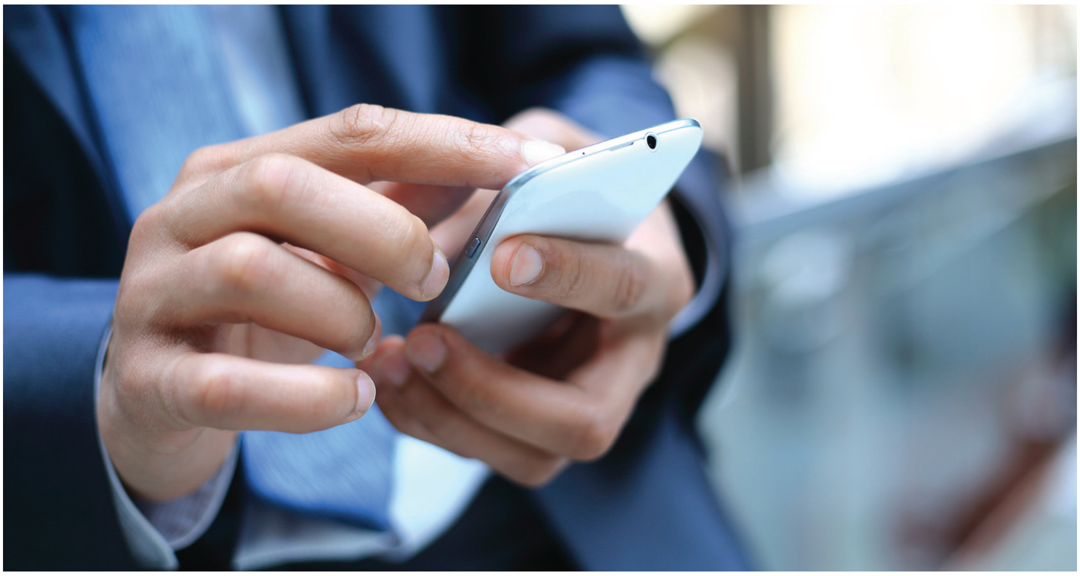
Before 16 January 2015	After 16 January 2015
1.5%	2.5%

The annual management charge is 1.5% for both VCTs, which is low in comparison with other AIM VCTs. There are also other expenses and a performance fee. Full details can be found in the prospectus and investors should ensure they are comfortable with the charging structure before investing.

SHARE BUY BACK POLICY

An impressive feature of the Hargreave Hale VCTs has been the narrow discounts to NAV that have been maintained at around 5% to 10%. This has been down to a continual share buyback policy, and to date investors wishing to exit have done so on good terms. Share buy backs are subject to on-going board approval.

HOW TO APPLY



To apply please read the enclosed prospectus for the offer and fill out the enclosed application form. You may photocopy the form if additional copies are required, or download one from **www.hl.co.uk/VCT**.

The signed application and a cheque for the amount you wish to subscribe 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 for you to benefit from our discount.

We will acknowledge your application and your share certificate and tax certificate will be sent once the shares have been allotted. Shares are allotted periodically and allotment could take up to two months following the acceptance of your application.

Shares will be issued according to the NAV of the VCTs adjusted for the cost of the offer. The NAVs at the time of writing are 80.49p for Hargreave Hale AIM VCT and 110.96p for Hargreave Hale AIM VCT 2.

Dividends will be paid by cheque, but you can elect for them to be paid into your bank account. Please see the relevant section of the prospectus and application form for further details.