Downing Strategic Micro-Cap Investment Trust PLC

Report and accounts

For the period 17 February 2017
to 28 February 2018

Company number: 10626295

Downing

Strategy

We are value investors who seek to grow net asset value (NAV) at 15% per annum over the long term through making investments in listed micro-cap companies. We believe that this universe offers attractive investment opportunities and is highly inefficient, which will aid the realisation of the return target. Additionally, the Manager seeks 'strategic' involvement in their investee companies – a process through which they have proved to be effective at delivering returns in the past.

Universe

- The Manager considers the micro-cap universe to be sub £150 million market cap companies, at the time of investment.
- By definition, this comprises over 70% of UK listed companies.
- On average, there are less than two analysts covering any of these companies leading to pricing inefficiencies.
- The Manager expects these inefficiencies to become greater due to regulatory change in the financial sector.

Portfolio

- The Company's portfolio of investments is expected to comprise between 12 and 18 holdings when fully invested.
- The Company will typically seek to hold between 3% and 25% of the equity of these investee companies, notwithstanding the ability to use debt instruments alongside equity.
- Typically investments will be appraised over a three to seven-year investment horizon.

Process

- The Manager's investment process is bottom up and value driven. This means that they focus on company fundamentals rather than macro-economic drivers, and that they aim to invest in line with value principles.
- The Manager focuses on cash generation and return on capital metrics.

Strategic involvement

- The Manager seeks to invest in companies which are materially undervalued and where there is scope for strategic involvement going forward.
- Strategic mechanisms typically include, but are not limited to: providing funding for organic and inorganic growth; providing capital for restructuring operations; implementing incentive plans to align management over the long term; and rectifying sub-optimal corporate governance practices.

Discount control

- The Company has a buyback procedure which is expected, in normal markets, to manage the discount of the Company's share price to the underlying NAV per share.

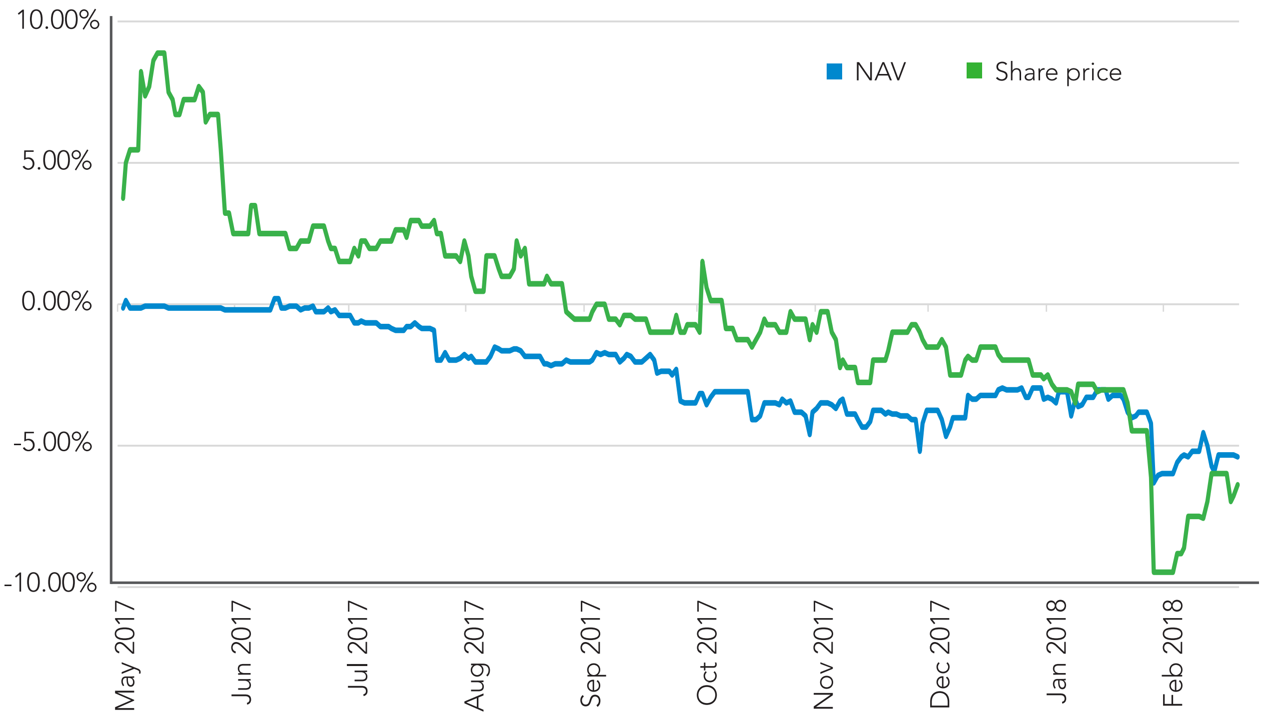
Contents

Strategic report

Financial performance summary

Performance	28 February 2018
Net assets (£'000)	51,744
Net asset value (NAV) per Ordinary Share	93.06p
Mid market price per Ordinary Share	93.60p
Premium	0.58%
Revenue return per Ordinary Share	(0.03p)
Capital return per Ordinary Share	(6.22p)
Total return per Ordinary Share	(6.25p)
	%
Decrease in NAV since admission (9 May 2017)	(6.94)
Decrease in share price since admission (9 May 2017)	(6.40)

Performance from launch* to 28 February 2018



*The Company commenced trading on the main market of the London Stock Exchange on 9 May 2017.
Source: Downing LLP.

Operational highlights

The Company raised £54.5 million (net) in May 2017 and over the course of the period to 28 February 2018 these monies have been invested in the equity and debt instruments of the following businesses:

AdEPT Telecom PLC (AdEPT)	Real Good Food PLC (RGD)
Braemar Shipping Services PLC (Braemar)	Redhall Group PLC (Redhall)
Gama Aviation PLC (Gama)	Science in Sport PLC (SiS)
Hargreavs Services PLC (Hargreaves)	Sprue Aegis PLC (Sprue)
Ramsdens Holdings PLC (Ramsdens)	Synectics PLC (Synectics)

- The Company had retained £20.7 million in cash for making new and follow-on investments as at 28 February 2018.
- The investment rate is encouraging.
- The underlying operational performance of all portfolio holdings is in line with our expectations, except RGD, which continues to consume a significant amount of our time. We are confident that we should realise a positive outcome for our investors and initial feedback from the new management team has been positive.
- Investments are spread between sectors and in companies that we believe are each at a transformation stage.

Chairman's statement

Your Company made ten investments in the ten months to 28 February 2018. Along with other Downing funds, that makes a portfolio of strategic holdings where stakes of between 22.80% and 5.22% of the underlying companies are held. The Company's holdings are set out on page 12.

Nine of those investments we would make again today. All have seen positive developments in intrinsic value through organic growth or decisive, strategic, management action, which we have supported or are on a path to supporting. As value investments these holdings are attractive and the Manager calculates that the discount to intrinsic value has increased by approximately 10% since investment was made, reflecting the progress of the portfolio.

One holding has been disappointing, to put it politely, but the structure of our investment has allowed us to drive change throughout that business. Board members and top management have been replaced, the business has been refocused, and we believe that it should generate a gain for our shareholders in the medium term.

Returning to the nine holdings, in our view these businesses represent even better value today than when we initially invested. Although wider recognition of that may call for patience, the scope is greater with strategic holdings in well managed micro-caps. We hold significant positions in companies that we believe have competent management, growing markets, sound and often transformational strategies, good margins, healthy operating cash flows and who appreciate our support and influence. Where key qualities are lacking, we encourage the necessary strategic action or improvement in performance. That gives us confidence that over the longer term intrinsic value will become evident and our investments will either be revalued or the companies acquired.

As to our 'disappointment', we took a board seat suspecting that governance could be improved. What we did not expect to find was both bad governance and false accounting. A disproportionate amount of time has been taken up on this investment in unearthing wrongdoing and a lack of internal controls, replacing the CEO, the Audit Committee Chairman, the Finance Director and some senior management, replacing the auditors, resetting strategy and refinancing the company. I comment later on the importance of competent, thoughtful, engaged directors, and on the need for better oversight of companies.

That instance apart, the continuing principles of the Manager's stock selection (set out in more detail in the Manager's Report) have evidently worked well in identifying investment opportunities that prove to be worthwhile. The Board continues to be impressed with the management team, led with vigour by Judith MacKenzie, and there is a good, constructive relationship between Board and Manager on both potential investments and the portfolio's performance.

In October 2017, in our interim report, I set out the importance that we place on governance in our investments. Our expectations draw heavily on the General Duties of Directors, set out in the Companies Act and company law, on the UK Corporate Governance Code and on the Quoted Companies Alliance Code. We repeat those expectations in this Annual Report on page 18, and may well do in our future reports. Correct governance of companies is critical to their corporate health and investors' confidence. The core of good governance is directors actively 'directing', striving for the success of the companies of which they are fortunate enough to be directors, overseen by nominated advisers (Nomads) who should be doing more than going through the motions, and by an FCA and LSE AIM team that should monitor with determination. As investors we should not have to be as concerned as we are about that.

Share price and NAV

The net result for the first ten months has been a decline in our NAV from 98p to 93p. While disappointing, strategic investments do tend to have some element of drawdown in their early stages. As the Manager demonstrates, the intrinsic value of the portfolio has actually increased across a number of holdings but shareholders will only see that come through in the NAV if either the true value of investee companies is recognised by the market, or they are acquired. One or other of those outcomes is likely in every case and, crucially, we invest as a catalyst to facilitate that. The Company's share price has kept close to the NAV. I have said before that we wish to keep any discount to a minimum and, bar market crises, we will seek to do so.

Shareholders

I have already started meeting larger shareholders and as soon as these reports and accounts are despatched in May I will be seeking to meet more later in that month and into June. Your Board is committed to shareholder engagement. We now produce an extensive quarterly newsletter (see our website) and monthly factsheets will start being issued in June. To receive regular email news and updates please visit www.downingstrategic.co.uk and register.

May I also encourage shareholders to come to our investor event and AGM on **27 June 2018 at 2:30pm** at the **Andaz Hotel, 40 Liverpool Street, London, EC2M 7QN**. Details are given in the notice of the Annual General Meeting on page 78.

Board

On 4 April 2018 Diana Hunter resigned from the Board. We are seeking to find as strong and spirited a replacement.

Hugh Aldous
Director

23 May 2018

Investment Manager's report

Investment strategy

We invest in publicly quoted businesses typically below £150 million market cap at the time of investment. Rather than passively investing, we aim to take large equity stakes which allows us to implement strategic initiatives in order to grow the value of our investment over time. We are not 'activists', rather we prefer to foster a constructive relationship with our management teams and other stakeholders.

We are long term value investors meaning that we seek to hold companies for many years, supporting management teams as they deliver on their strategy. We also try to acquire our shareholding at a significant discount to intrinsic value which, in turn, we hope will steadily grow over time. Before investing, we undertake an extensive due diligence process which typically involves desk work, as well as site visits and meeting the company's executive and non-executive directors of the business.

When valuing businesses we typically look for sustainable and growing free cash flows. Part of this requirement is that we should be able to forecast cash flow and capital expenditure. We tend to avoid highly speculative businesses in sectors such as mining, oil and gas, and biotech for this reason. All of our investment decisions are based around the margin of safety in our intrinsic valuation versus our entry price. In addition to this process, which values the operations of the business, we also overlay a scenario analysis which looks at various outcomes including downside and upside, rerating, and trade exits. Given the inefficient nature of the smaller companies market, we typically seek to invest in businesses where we deem some potential for a trade exit as we cannot always be sure that our intrinsic value will be realised.

We believe that smaller companies are capable of delivering the highest risk adjusted returns for our strategy. These companies are typically under researched which can lead to large pricing inefficiencies. Our portfolio is concentrated and seeks to hold between 12-18 holdings when fully invested. We believe that this concentration will allow us greater time to engage constructively with management teams and help reduce the overall risk of our long-term holdings.

Portfolio review

The Company is still deploying capital and was 63.5% invested as at 28 February 2018. With commitments made to impending transactions we were close to being fully invested at the time of the first anniversary (which we deem to be approximately 80-85% invested). Since the interim report dated 31 August 2017, we have made a number of new and follow on investments. The investment rationale and descriptions of these investments can be found of page 13. Specifically, we invested £3.4 million in Synectics and £2.6 million in Ramsdens. We took part in fundraisings for SiS, contributing £1.5 million, and undertook a follow-on investment with Gama for £1.8 million. Both of these investments were to provide growth capital. We also invested £3.7 million in Hargreaves. We have deployed an additional £843,044 in Real Good Foods (RGD) through additional secured and unsecured loan notes, and deployed a further £1.9 million increasing our holdings in AdEPT, Braemar, Gama, and Redhall where share prices have been weak.

Performance review

The Company's NAV performance has declined 6.94% over the period to 28 February 2018 due to: 1) expected or unexpected share price declines where a company in the portfolio is in a highly strategic turnaround situation; 2) unexpected share price declines where the company has missed short-term expectations; 3) unexpected share price declines where there is negative sentiment; and 4) share price appreciation, which is outweighed by the combination of the other points above.

Real Good Food (RGD) is a strategic turnaround situation. Redhall (RHL), despite large new orders, has failed to meet short term expectations on project delivery and is also suffering from negative sentiment. Gama (GMAA) and Ramsdens (RFX) have both performed well, delivering unrealised gains to date. This includes the Gama placing shares which we subscribed for in the fundraise in early 2018, but which had not yet been issued at the date of the statement of financial position. We believe that the other companies fall under the negative sentiment category, and in some cases this sentiment has been materially negative, such as with AdEPT (ADT), which is performing well, and Braemar (BMS).

Real Good Food continues to take up the Managers time as we seek to drive a favourable outcome for our investors and for the company. Since we initially invested, we have taken a board seat and have helped provide new management and sought to improve corporate governance practises. Two of its divisions - Renshaw, the decorations business, and Brighter Foods, a contract supplier to Slimming World - continue to trade in line with the Manager's expectations. Haydens, the bakery business, where there has been significant investment in new plant and equipment to service contracted demand is likely to be facing headwinds from commodity prices. However, the investment made should allow management to capitalise on previous operational inefficiencies. Overall the management are seeking to implement a number of self-help measures that include the disposal of non-core businesses (Garretts Ingredients has already been sold). We believe that we will drive a favourable outcome from our investment which is likely to be achieved through a trade exit.

Post period end, a funding of up to £8.7 million has been announced by Real Good Food. This will satisfy outstanding liabilities and fund the business over the long term. The Company has supported this funding; the terms are attractive and should maximise both the security held through loan notes and the equity position due to the conversion terms proposed.

Redhall is at an interesting juncture as its order book and pipeline continue to grow, although this has yet to be adequately reflected in the share price. Admittedly, investors are likely becoming fatigued at the recent delays and some investors are easily shaken out by these short-term disappointments. Unfortunately, delays are not uncommon in businesses with exposure to high-value, critical infrastructure projects. We believe that this remains an attractive company operating in niche end markets which aim to deliver impressive returns over the long term. This is supported by the most recent contract wins with Cavendish Nuclear Limited and Hinkley Point C. Post period end, Redhall announced that its orderbook had grown to £35 million, excluding the Cavendish teaming agreement valued at £18 million over three years. Over the long term we expect that the market will realise the potential in Redhall's quality order book and the shares will subsequently re-rate or that it will be acquired. In the meantime, we will take advantage of what we believe is a pricing anomaly.

Gama is delivering exactly on our investment case. In February 2018, it raised £48 million to deliver a number of organic growth initiatives in Asia, the Middle East, and the US, as well as further inorganic growth initiatives. As part of this, the company also gained a material strategic investor in Hutchison Capital Holdings Limited who now own 21% of the equity. The Board was also strengthened in the period. We believe that these growth initiatives could be transformational for the business in the mid to long term. Post period end, the business posted a positive set of full year results. The focus has been on free cash flow generation and, pleasingly, Gama generated US$14 million in 2017. Operating margins continue to improve across the segments in line with management's long-term targets of 5% in the Air division and 20% in the Ground division.

Ramsdens delivered a strong set of interim results in November 2017 indicating an 18% increase in revenue and 63% increase in profit before tax. In subsequent conversations with management we have been impressed by the continued growth across the business segments. Our investment case is on track with regard to a number of store openings and we note that their flagship Braehead, Glasgow store opened post period end. Elsewhere in the sector, we believe that there may be opportune estate expansion at attractive prices given the challenging high street retail environment.

Since the period end, Sprue Aegis has been challenged by litigation from its US ex-distribution partner which disrupted trading and led to a profit warning. The litigation has been settled and Sprue is hopeful of significant new tender wins in the second quarter of 2018. This trip-up is unfortunate for a company that has a dominant market position, improving margins and regulatory drivers in its key markets.

> *"We are not 'activists', rather we prefer to foster a constructive relationship with our management teams and other stakeholders."*

Outlook

We follow a strict value investing mandate, seeking to invest in businesses which are trading, or where we can engineer an entry, at a discount to our determination of intrinsic value.

Our determination of risk revolves around permanent erosion of capital, rather than volatility. Therefore, we attempt to avoid investing in anything highly speculative where intrinsic value cannot be determined through forecastable cash flows. We also look favourably upon strong balance sheets, particularly those with net cash positions or where we can find valuation support through net asset value alone, ideally tangible net assets.

With this in mind, we believe that our portfolio is well positioned on valuation grounds to protect and grow our shareholder's capital in the long term. We also believe that by leveraging various strategic initiatives, these businesses should be able to deliver compound growth rates that meet or exceed our 15% p.a. return target over the long term.

Given the heightened volatility which has typified the market since the beginning of 2018, we believe that our value strategy will perform well as we opportunistically add to our positions in what we believe are already undervalued shares.

Judith MacKenzie
Partner and Head of Public Equity, Downing LLP

23 May 2018

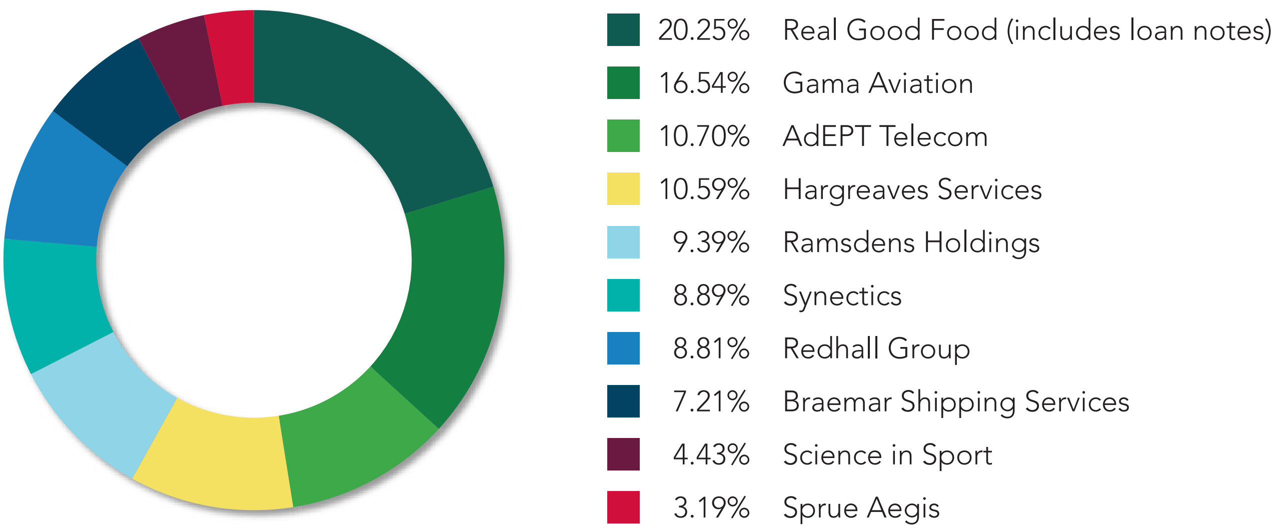
Portfolio information

As at 28 February 2018

Holding in Ordinary Shares unless otherwise stated	Market value (£'000)	% of investments*
Gama Aviation	5,436	16.54
Real Good Food 6.5% loan note (28/06/2020)**	4,906	14.93
AdEPT Telecom	3,518	10.70
Hargreaves Services	3,478	10.59
Ramsdens Holdings	3,086	9.39
Synectics	2,922	8.89
Redhall Group	2,896	8.81
Braemar Shipping Services***	2,370	7.21
Science in Sport	1,457	4.43
Sprue Aegis	1,047	3.19
Real Good Food	902	2.75
Real Good Food 10% loan note (30/09/2019)**	673	2.05
Real Good Food 10% loan note (30/06/2018)**	170	0.52
Total investments	**32,861**	**100.00**

All investments are quoted on the AIM unless indicated. The total number of holdings as at 28 February 2018 was 10. Details of the equity interest comprising more than 3% of any company's share capital are given in note 17 on page 73.

*Excludes cash
**Unquoted
***Quoted on the Main Market



Background on the investments

AdEPT Telecom PLC (AdEPT)

AdEPT is one of the UK's leading independent providers of managed services for IT, unified communications, and connectivity and voice solutions. It is a business that Judith MacKenzie has known over a decade, so our long-standing relationship has given us a high level of conviction over the ability and integrity of the management team.

Investment case

- **Higher quality earnings:** AdEPT has migrated from being a provider of just fixed line solutions to a provider of higher margin managed service solutions across converged telecom and IT activities, introducing higher quality revenue streams to the group at a better margin. The company has an EBITDA margin of approximately 21% and low capital expenditure requirements, which makes the operating structure highly cash generative.
- **M&A:** management has made a number of acquisitions since IPO. We have been impressed with management's ability to acquire businesses at attractive prices and how the management of these target businesses are brought into the culture of AdEPT.
- **Engagement:** Ian Fishwick, CEO, and John Swaite, FD, are well known to the Downing Public Equity team. Judith first met Ian in 2006 at the IPO of the business, and over this period a strong relationship and level of understanding has been reached. Our relationship with the business is highlighted by our invitation to the Annual Group Sales Conference.

Braemar Shipping Services PLC (Braemar)

Braemar is a leading international provider of broking, financial, consultancy, technical and other services to shipping and marine related industries. We know the business and management team well from Downing client funds' investment spanning over six years.

Investment case

- **Improving margins:** we expect global gross domestic product (GDP) growth to be positive year on year, which we believe should drive a steadily increasing demand for shipping and freight volume over the long term. We also expect shipping rates to improve, aided by a shortage of shipping supply (although this can be volatile and we do not attempt to explicitly forecast global supply).
- **Restructuring:** operationally, we believe that a restructuring could help to improve Braemar's margins through cost savings. At the time of investment, we expected that the Marine Services restructure would result in a £6 million per annum cost saving from 2018.
- **M&A:** we also believe that it could dispose of lower margin businesses and build or acquire higher margin businesses which will be accretive to group margins. This could also be supported by a move to the Alternative Investment Market (AIM) through which the company would enjoy materially lower transaction costs.

Gama Aviation PLC (Gama)

Gama is a global business aviation service provider, headquartered at Farnborough airport. It focuses on air operations (business aircraft management, special missions and charter of business aircraft) and ground operations (engineering, design, software, maintenance, repair and overhaul (MRO), passenger handling and consultancy).

Investment case

- **Organic growth:** we expect natural growth to be aided by the increasing cost of compliance which naturally favours players with scale, crowding out the smaller, localised operators that characterise the business aviation market. We also expect margin growth through operational efficiencies and new higher margin activities.
- **Consolidation:** Gama is one of the top three global players in the sector. Owing to the crowding out mentioned above, the fragmented market, and Gama's public listing, we believe that the company has the potential to be the consolidator of the market.
- **Re-rating:** underlying the operational and market opportunity, we believe that the business is misunderstood and undervalued by the market. Key to a rerating will be Gama's ability to closely control working capital and consistently generate free cash flow. These are aspects which we believe are improving with every successive reporting period.

Hargreaves Services PLC (Hargreaves)

Hargreaves is a conglomerate of infrastructure and commodities businesses which has historically been held in the Downing UK Micro-Cap Growth Fund.

Investment case

- **Value creation:** we believe that there is £35 to £50 million of value creation potential over and above the current book value in the next five years – the first plot sale at Blindwells should act as validation. The spin-off of the wind energy assets into Brockwell Energy could also generate a material upwards revaluation as they are developed.
- **Value realisation:** the business targets a 40% pay-out ratio but in a capital asset intensive business, returns to shareholders have been reduced through high recurring capital expenditure. In 2017, cash realisations were £25.5 million from legacy assets, but post reinvestment this sum is materially reduced. We expect that the winding down of the legacy capital intensive activities will increase distributable cash.
- **Reducing risk:** the winding down of the legacy coal business and associated reduction in inventory reduces the risk to our NAV play and frees up additional cash for developing NAV accretive projects with higher returns, or distribution to shareholders.

Ramsdens Holdings PLC (Ramsdens)

Ramsdens is a growing and diversified financial services provider and retailer, operating in four core business segments of foreign currency exchange, pawnbroking loans, precious metals buying and selling, and retailing of second hand and new jewellery. The group operates from over 120 stores in the UK. We believe that market forecasts are too light and that the business has the potential to grow earnings and dividends around 10-15% per annum.

Investment case

- **Organic growth:** the foreign exchange (FX), Retailing and Pawnbroking divisions have grown at annualised rates of 37%, 25% and 7% respectively. We have made prudent assumptions around these verticals but still arrive at numbers materially ahead of the market.
- **Estate growth:** management has grown the estate by approximately 12 new stores each year since 2002. Based on management's strategy, and the historic rollout pattern, it would be fair to assume that the company targets a similar level of openings per year over the next 10 years, however the market has assumed far fewer.
- **Operating model:** we believe that Ramsdens has an attractive operating model with strong cash generation, a net cash balance sheet, barriers to entry provided by the regulatory environment, and a strong and prudent management team.

Real Good Food PLC (RGD)

RGD groups its operation into two main divisions: Cake Decoration and Premium Bakery; and one smaller segment: Food Ingredients. The Cake Decoration business manufacturers sugar pastes and decorations. Hayden's, the brand under which Premium Bakery operates, is a manufacturer and distributor of premium bakery products, with clients including Waitrose and Marks & Spencer.

Investment case

- **Growth:** our investment was to provide a large amount of capital expenditure, which we believe is capable of generating enhanced return on capital and, ultimately, improved earnings in the long term.
- **Governance:** the business was in need of appropriate financial controls, accountability and corporate governance which we believe has now largely been implemented.
- **Valuation:** we believe that there is a material disconnect between intrinsic value and enterprise value. We expect that the delivery of growth and governance will reduce this valuation spread.

Redhall Group PLC (Redhall)

Redhall is an engineering business offering design, manufacture, installation, maintenance and decommissioning services to a variety of sectors. We were attracted to the business on the basis of increasing UK infrastructure projects and Redhall's strength in its niches.

Investment case

- **Order book:** we think that Redhall's growing order book is undervalued in terms of its potential to grow, the visibility provided, and in terms of the quality of the underlying projects.
- **Critical infrastructure:** Redhall brings material exposure to high value UK public sector contracts, specifically in nuclear projects. We know these to be very long duration – for example, Hinkley Point is expected to be constructed over eight to ten years.
- **Improving margin:** as the business continues to deliver on new contracts, we expect operational gearing and continuous process improvement to lift margins. This is on the back of the completion of the Strategic Turnaround Plan which was executed by outgoing CEO Phil Brierley, and focused on exiting capital intensive, low margin contracting activities.

Science in Sport PLC (SiS)

SiS is a leading sports nutrition company that develops, manufactures and markets sports nutrition products for professional athletes and sports enthusiasts. Downing managed funds initially invested in the company in 2013 and were impressed by the strength of the brand and the management team.

Investment case

- **Gross margin:** the business has sector-leading gross margins and we believe that this will continue. We believe revenue growth will further improve utilisation of the current facility and the company's growing e-commerce business will provide additional margin support.
- **Growth:** in November 2017, SiS returned to the market for working capital and growth investment for further expansion in the US and Italy, and into a new target market – football. The Company participated in this placing.
- **Return on capital:** valuation approach in this case is centred around incremental return on invested capital on our monies. It assumes an exit at a multiple at least as great as the sector average, which we believe to be around 2.5x enterprise value (EV)/sales. On this basis, we believe that the company can deliver more than a 15% internal rate of return (IRR) over our investment horizon.

Sprue Aegis PLC (Sprue)

Sprue is a major designer and distributor of smoke and carbon monoxide detectors and other safety-related devices, in Europe. Those incorporating Sprue's own technology/IP are sold under several brands including FireAngel,the UK's number one retail brand of detectors.

Investment case

- **Legislative drivers:** the company benefits from country legislation which is driving the adoption of fire protection products. Guidance is for the purchase of smoke alarms with a 10-year lifespan and we are already beginning to see a replacement cycle in mature markets where there is high penetration.
- **Improving margins:** gross margins on Sprue's products differ to those of typical white goods – earning around 30%, and over 45% on IP-enabled products. When combined with an improved operational structure, conversion to profits and cash flow are expected to improve. The move to Flex in Poland for manufacturing and supply of smoke detectors is progressing to plan and we believe this will enable closer control of production costs. Finally, the termination of a distribution agreement with BRK Brands will save £2.9 million in annual distribution fees.
- **Market growth:** Sprue has robust technology and IP around device interactivity, owing to its long tenure in the sector. While there are new upstarts in the Internet of Things (IoT) sector, who are investing heavily to gain market share, we believe that Sprue's technology is superior. Exploitation of the IoT market potential could offer material upside.

Synectics PLC (Synectics)

Synectics is a leader in the design, integration, control and management of advanced surveillance technology and networked security systems. It operates mainly in heavily regulated industries, including gaming, transport and critical infrastructure, high security and public space applications and oil and gas.

Investment case

- **Order book:** our investment case is predicated on the strong order book. We see great potential in the gaming market where Synectics has an existing client base of global casino owners and operators.
- **Improving quality earnings:** having recently restructured we believe that the business is more operationally geared and could double its return on capital employed in the mid-term. We also value Synectics' focus on managed services which contribute approximately 25% of higher quality recurring revenues.
- **Strategic opportunity:** we see the opportunity on two levels - the first is an improvement in operating performance and the second is consolidation potential in what is a fragmented sector with exposure to highly regulated markets.

Our expectations of the investee companies

When we invest in companies we expect, in return, rigorous and effective corporate governance; directors who understand their duties and who are familiar with The General Duties section of the Companies Act 2006 and The UK Corporate Governance Code from the Financial Reporting Council in 2016.

- **Directors' responsibilities:** in our view directors' responsibilities are demanding. They stand accountable for the culture, foresight and success of the company, to which they should apply the best of their knowledge and ability to enquire and act in the interests of the company as a whole for its current and future shareholders. A company's success depends on investment in its long-term, sustainable advantage as well as its financial strength and profitability. A company's return on investment underpins its shareholders' returns.
- **Constructive challenge:** we look for alert, questioning, competent boards that constructively challenge management, help develop strategy and long-term objectives, monitor performance, ensure the build-up of necessary assets, skills and capable management and lead in setting a culture of integrity. We will take action if we do not find that level of competence.

  In particular we would expect to find:
- **Leadership:** every investee company should be headed by an independent Chairman leading an effective, questioning, challenging board that sees itself as collectively responsible for the long-term success of the company. We will encourage that if it is missing. We will say so publicly if we do not think the Chairman is up to the job.
- **Effectiveness:** the board and its committees should be engaged with the business and have the skills, experience, independence and knowledge to enable them to challenge constructively, and fully undertake their duties. It should be clear to investors why each director is on the board, what skills and contribution that director is there to provide and all directors and senior management should regularly update and refresh their skills and knowledge. There should be a rigorous process for the appointment of new directors.
- **The Chairman;** should lead the board, create the conditions for overall board and individual director effectiveness, ensure that the board gets information in a form and of a quality sufficient to discharge its duties and should undertake a formal annual evaluation of the board and each director's performance.
- **Accountability:** We expect all directors to appreciate that accountability for culture, integrity, the 'tone from the top', the creation of value, of corporate and shareholder value, and the company's success lies with them.

It is with those expectations of the boards of directors that we invest.

Business model

The Company invests in accordance with the investment objective. The Board is collectively responsible to shareholders for the long-term success of the Company. There is a clear division of responsibility between the Board and the Manager. Matters reserved for the Board include setting the Company's strategy, implementing the investment objective and policy, capital structure, governance and appointing and monitoring of the performance of service providers, including the Manager.

As the Company's business model follows that of an externally managed investment company, it does not have any employees and outsources its activities to third party service providers including the Manager who is the principal service provider.

Status of the Company

The Company is a public limited company incorporated on 17 February 2017 in England and Wales under registered number 10626295. It commenced trading on the main market of the London Stock Exchange and was admitted to the premium segment of the Official List of the UK Listing Authority on 9 May 2017. It is an investment company as defined in section 833 of the Companies Act 2006.

The Company's principal activity is to carry on business as an investment trust. It has been approved by HM Revenue & Customs as an investment trust under the Investment Trusts (Approved Company) (Tax) Regulations 2011 and, as a result, is not liable for taxes on capital gains. The Directors are of the opinion that the Company has conducted its affairs for the period ended 28 February 2018 so as to be able to continue to qualify as an investment trust. The Company is not a close company for taxation purposes.

As an investment company managed and marketed in the United Kingdom the Company is an Alternative Investment Fund (AIF) under the provisions of the Alternative Investment Fund Manager's Directive (AIFMD). The Company was registered by the FCA as a Small Registered UK Alternative Investment Fund Manager (AIFM) with effect from 16 March 2017.

The Company currently conducts its affairs so that the shares issued by the Company can be recommended by Independent Financial Advisers to ordinary retail investors in accordance with the FCA's rules in relation to non-mainstream investment products and intends to continue to do so for the foreseeable future.

> ***The investment objective** of the Company is to generate capital growth for Shareholders over the long term, from a focused portfolio of UK micro-cap companies (those whose market capitalisations are under £150 million at the time of investment) targeting a compound return of 15 per cent. per annum over the long term.*

Investment policy

The Company intends to invest in UK publicly quoted companies that are defined by the Investment Manager as micro-cap, reflecting a market capitalisation of under £150 million of the investee company at the time of investment.

The Investment Manager will select a concentrated portfolio of between 12 and 18 investments (once fully invested). The Company will seek to hold between 3% - 25% of the equity of these investee companies, although it may hold larger or smaller stakes when it deems appropriate (including up to a maximum of 29% of the equity of any one company at the time of investment), but only where the Company holds an additional right of conversion (e.g. option rights or convertible loan notes) that would, on exercise, result in the Company holding above 25% of the equity). It is likely that the majority of the investments held in the Company's portfolio will be quoted on AIM and will typically be drawn from the Numis Smaller Companies Index plus AIM (Excluding Investment Companies).

The Investment Manager will:

- deploy a private-equity style diligence approach to investing, focusing on the future value of free cash flows, sustainability of margins and strength of the management team;
- take advantage of the inefficiencies within the microcap market which include lack of analyst coverage;
- have the ability to invest up to 10% of the Gross Assets at the time of investment in unquoted or traded companies, or in any one unquoted or untraded company;
- procure that the Company invests where analysis indicates an ability to create shareholder value of 15% compound growth per annum over a 3-7-year investment horizon;
- favour a proactive style of engagement with management, aiming to maximise shareholder value over the long term particularly where diligence highlights a strength of management, an entry value that is a discount to the Investment Manager's calculation of intrinsic value, and where active engagement is likely to mitigate some of the inefficiencies presented by the micro-cap market.

The Investment Manager believes that this is best achieved by the Company taking strategic shareholdings between 3% - 25% of the equity of the investee company, although the Company may hold larger or smaller stakes where it deems appropriate (including up to a maximum of 29% of the equity of any one company at the time of investment, but only where the Company holds an additional right of conversion (e.g. option rights or convertible loan notes) that would, on exercise, result in the Company holding above 25% of the equity). No single investment will represent materially more than 15% of the Gross Assets at the time of investment. The Company's portfolio is expected to be diversified by industry and market but stock selection will be determined by the results of extensive due diligence rather than a weighting in any particular index. However, the Investment Manager will not invest on behalf of the Company in early stage technology, mining and extraction companies and early-stage biotech (unless the Company can see a defined route to profitability) and does not intend to invest in initial public offerings, unless in exceptional circumstances where it has a historic relationship with and an in-depth knowledge of the investee company.

The Company may use derivative instruments including index-linked notes, contracts for difference, covered options and other equity-related derivative instruments for efficient portfolio management, gearing and investment purposes. Any use of derivative instruments for investment purposes will be made on the basis of the same principles of risk spreading and diversification that apply to the Company's direct investments, as described above, although the Company would not hold more than 5% of Net Assets in a derivative of any single investee company. The Company will not enter into uncovered short positions.

If companies in the portfolio achieve organic growth or grow through corporate activity such as acquisitions, and consequently have a market capitalisation that would place them outside the investable universe (described above), the Investment Manager will not be obliged to sell those holdings, but the proportion of the portfolio in such companies will be carefully monitored by the Investment Manager and the Board so that the overall investment policy to invest in the smallest quoted or traded companies is not materially altered.

No material change will be made to the investment policy without the approval of Shareholders by ordinary resolution.

Performance

Details of the Company's performance are set out in the Highlights and the Chairman's Statement on pages 4 to 7.

A review of developments during the year as well as information on investment activity within the Company's portfolio and the factors likely to affect the future performance of the Company are included in the Investment Manager's Report on pages 8 to 18 and the Chairman's Statement on pages 6 and 7.

Results and dividend

The results of the Company are set out in the statement of comprehensive income on page 60.

The total net loss for the year, after taxation was £2.8 million, of which the revenue return amounted to (0.03p) per share, and the capital return amounted to (6.22p) per share.

The Directors are not recommending the payment of a final dividend.

Dividend policy

The Company will only pay dividends on the Ordinary Shares to the extent that it has sufficient financial resources available for the purpose in accordance with the Companies Act 2006. The Company has no stated dividend target.

Key Performance Indicators (KPIs)

A number of performance indicators are used to monitor and assess the Company's success in achieving its objectives and to measure its progress and performance.

The principal KPIs are described below:

- Performance against the Company's peers - while the principal objective is to achieve capital growth, the Board also monitors the performance relative to a broad range of competitor funds. The Company does not have a benchmark.
- Share price discount to NAV per share - the Board monitors the level of the Company's premium or discount to NAV closely. During the period 9 May 2017 to 28 February 2018, the shares traded between a premium of 10.96% and discount of 2.01% at an average premium of 4.01%.
- Share price movements - the Company's Ordinary Share price decreased by 6.4% over the period under review.
- Ongoing charges - the ongoing charges represent the Company's management fee and all other operating expenses excluding any finance costs, expressed as a percentage of the average daily net assets during the year. The ongoing charges for the period ended 28 February 2018 were 1.48%.

Principal Risks

The Company is exposed to a variety of risks and uncertainties. The Directors confirm that they have carried out a robust assessment of the principal risks facing the Company, including those that would threaten its investment objective, business model, future performance, solvency or liquidity.

The Company maintains a risk matrix which sets out the risks facing the Company, the likelihood and potential impact of each risk and the controls established for mitigation. The risk matrix is reviewed by the Audit Committee on a regular basis.

The principal risks identified and the actions taken to mitigate those risks are set out below.

Risk	Mitigation
Investment performance	
The investment objective of the Company may not be achieved as returns are reliant primarily upon the performance of the portfolio.	The Company is reliant on the Investment Manager's investment process. The Board has set investment restrictions and guidelines which the Investment Manager monitors and regularly reports on. The Board monitors the implementation and results of the investment process with the Investment Manager. The Investment Manager attends all Board meetings and provides the Board with information including performance data, an explanation of stock selection decisions, portfolio exposure and the rationale for the portfolio composition.
The Company will invest primarily in the smallest UK quoted or traded companies, by market capitalisation. Smaller companies can be expected, in comparison to larger companies, to have less mature businesses, a more restricted depth of management and a higher risk profile.	The Investment Manager has significant experience in small cap investing and deploys an approach that is designed to maximise the potential for the investment objective to be achieved over the longer-term.
Operational	
The Company relies on external service providers. In the event that they are unable, or unwilling to perform in accordance with its terms of appointment the Company may impact the Company's performance. Disruption to the accounting, payment systems or custody records could prevent the accurate reporting and monitoring of the Company's financial position.	Due diligence is undertaken before contracts are executed with potential service providers. The Board monitors the performance of service providers together with the associated costs. The Board also reviews reports on the effective operation of the internal controls of service providers.

The security of the Company's assets, dealing procedures, accounting records and adherence to regulatory and legal requirements depend on the effective operation of the control systems of the service providers.	The Company's assets are subject to a strict liability regime and in the event of a loss of financial assets held in custody assets of an identical type or the corresponding amount must be returned unless the loss was beyond the reasonable control of the custodian. The Board also considers the business continuity arrangements of the Company's key service providers. The Board may terminate all key contracts on normal market terms.
Financial	
The Company's investment activities expose it to a variety of financial risks that include interest rate, currency and liquidity risk.	Further details of these risks are disclosed in Note 14 to the financial statements together with a summary of the policies for managing these risks
Legal and compliance	
The Company has been accepted by HM Revenue & Customs as an investment trust, subject to continuing to meet the relevant conditions.	The Investment Manager monitors investment movements and the amount of proposed dividends, if any, to ensure that the relevant provisions of the Corporation Tax Act 2010 are not breached. A report is provided to the Board at each meeting.
The Company is subject to the Companies Act 2006, the Alternative Investment Fund Manager's Directive, the UK Listing Rules and Disclosure & Transparency Rules and the Market abuse Regulations	The Company Secretary and the Company's professional advisers provide reports to the Board in respect of compliance with all applicable rules and regulations and will ensure that the Board is made aware of any changes to these rules and regulations. Compliance with the accounting rules affecting investment trusts is also monitored.

Exercise of voting rights in investee companies

The exercise of voting rights attached to the Company's portfolio has been delegated to the Investment Manager, whose voting policy states:

- we intend to vote at all shareholder meetings of companies in which our clients are invested. In cases where there are significant obstacles to voting such as share-blocking or requirements for a power of attorney, we will review the resolutions to assess the extent of the restrictions on voting against the potential benefits;
- we will vote in favour of proposals which we expect to enhance shareholder value, and on routine issues where we are supportive of a company's management;
- we will vote against proposals which we believe may damage shareholders' rights or economic interests; and
- we will abstain on proposals where we wish to indicate to the Company issues over which we have some concerns.

In all situations the economic interests of our clients will be paramount.

Further details of the Investment Manager's Proxy Voting and Engagement Principles may be found at **www.downingstrategic.co.uk**.

During the period 9 May 2017 to 28 February 2018, the Investment Manager voted at five general meetings on behalf of the Company. At these meetings the Investment Manager voted in favour of all resolutions.

Share capital

Discount, share buy backs and the return of capital

The Company has the authority to repurchase shares in the market for cancellation or to be held in treasury and to issue new shares for cash. No Ordinary Shares were repurchased or new Ordinary Shares issued during the period under review or following the period end.

Ordinary Shares held in treasury may be subsequently cancelled or sold for cash. The Directors do not intend to sell any Ordinary Shares held in treasury at a discount to the prevailing NAV (cum income) per Ordinary Share. Ordinary Shares held in treasury will not be entitled to receive any dividends declared by the Company or the Board.

Resolutions for authority to issue new shares or to reissue shares from treasury and to repurchase shares for cancellation or to be held in treasury will be put to shareholders at the forthcoming annual general meeting.

The current share capital is set out in note 12 on page 69.

Viability statement

The Company is an investment trust with an objective of achieving long-term capital growth. Taking account of the Company's current position, the principal risks that it faces and their potential impact on its future development and prospects, the Directors have assessed the prospects of the Company, to the extent that they are able to do so, over the next five years. They have made that assessment by considering:

- the long-term nature of the Company's investment objectives and strategy;
- the Company's principal risks and uncertainty's that are not expected to change materially, as set out on pages 23 and 24;
- the Company's business model which should remain attractive for longer than the period to 28 February 2023;
- the relative stability of the Company's expenses and liabilities; and
- the outlook for the value of the Company's investment portfolio.

In determining the appropriate period of assessment the Directors had regard to their view that, given the Company's objective of achieving capital growth, shareholders should consider the Company as a long term investment proposition. This is consistent with the general view of financial advisers that investors should consider investing in equities for a minimum of five years. Accordingly, the Directors consider five years to be an appropriate time horizon over which to assess the Company's viability.

The Directors confirm that they have a reasonable expectation, on the assumption that the principal risks identified on pages 23 and 24, are managed or mitigated effectively, that the Company will be able to continue in operation and meet its liabilities as they fall due over the five-year period of assessment.

Future prospects

The Board's main focus is the achievement of capital growth and an attractive compound return over the long term. The future of the Company is dependent upon the success of the Company's investment strategy. The outlook for the Company is discussed in both the Chairman's Statement on pages 6 and 7 and the Investment Manager's report on pages 8 to 18.

Modern Slavery Act 2015 (the MSA)

As an investment vehicle, the Company does not have any employees or provide goods and services in the normal course of business. Accordingly, the Directors consider that the Company is not required to make a slavery and human trafficking statement under the MSA.

Employees social community human rights and environmental matters

The principal activity of the Company is to invest in accordance with the Investment Policy set out on pages 20 and 21. The Company has no employees and accordingly it has no direct social, human rights or environmental impact from its operations. In carrying out its investment activities and relationships with suppliers the Company aims to conduct itself responsibly, ethically and fairly.

Directors, employees and gender representation

During the period under review to 28 February 2018 the Company had one female and three male directors. The Company now has three male directors and is undertaking a search for an additonal director. The Board will take its policy on diversity, including gender, into account during the recruitment and appointment process. The Company does not have any employees, therefore there are no disclosures to be made in respect of employees.

The Chairman's statement on pages 6 and 7 together with the Investment Manager's Report and portfolio information on page 12 form part of the strategic report.

The strategic report was approved by the Board at its meeting on 18 May 2018.

For and on behalf of the Board

Hugh Aldous
Chairman

23 May 2018

Investment team and committee

Judith MacKenzie

Partner and Head of Downing Public Equity

Judith joined Downing in October 2009 and established Downing's Public Equity division. Judith was previously a partner at Acuity Capital, a buy-out from Electra Partners Group, where she managed small company assets with an activist strategy. Prior to Acuity, Judith spent seven years with Aberdeen Asset Management Growth Capital as co-Fund Manager of the five Aberdeen VCTs, focusing on technology and media investments in both the public and private arenas. Judith has held a number of directorships, and advisory roles to companies and Government. She has 20 years of industry experience which she has leveraged in her building out of Downing's Public Equity division and Investment Team. Judith was named Fund Manager of the Year in the 2013 and 2015 Small Cap Awards. Judith has passed the examinations of the Securities Institute and holds a BA in Economics and Finance.

Nicholas Hawthorn

Investment Manager

Nicholas joined Downing in September 2015 as an Equity Analyst working on the micro-cap strategies. Prior to joining Downing, he worked as a Financial Analyst for the Private Equity team at BP Investment Management Ltd and as a Financial Analyst in Group Finance at Aberdeen Asset Management PLC. He is currently studying towards Level III of the Chartered Financial Analyst (CFA) exams and holds the Investment Management Certificate. He holds an MSc degree in Finance and Investments and an MA degree in Accounting and Economics.

Alyx Wood

Fund Manager

Alyx joined Downing in February 2014 as an Investment Manager working alongside Judith on the micro-cap strategies. He is also co-fund manager of the MI Downing Diversified Global Managers Fund. Prior to joining Downing, Alyx worked at Deutsche Bank AG for two years as a Business and Fund Finance Manager. Alyx also trained as a Management consultant at KPMG LLP in its Advisory practice between 2007 and 2012. He specialised in Investment Management and his main clients included BlackRock, Goldman Sachs AM and HM Treasury. He also completed secondments to Corporate Finance and Tax during his employment with KPMG. Alyx is a Chartered Accountant (ICAS), holds a BA in Accounting and Economics and the Investment Management Certificate.

James Lynch

Fund Manager

James joined Downing in February 2012 as Investment Executive within the private equity division. He gained transaction experience in the SME space across a range of industries before transferring to Downing Public Equity in 2013. James has specific responsibility for a number of strategic investments held by the MI Downing Micro Cap Growth Fund. He is also Fund Manager for the Downing Monthly Income Fund. Prior to joining Downing, James worked within the asset management division of Ernst & Young after specialising in smaller companies at HW Fisher & Company. James is a CFA Charterholder, Chartered Accountant (ACA) and holds the Investment Management Certificate.

Cheryl Vickers

Portfolio Manager

Cheryl joined Downing in 2010 from Rathbones where she gained over 12 years' experience working on VCT, EIS and IHT portfolio services. Cheryl provides portfolio support and oversight to all of the Downing Public Equity funds. Cheryl graduated from Keele University and is a Chartered Fellow of the Securities Institute.

Director's biographies

Hugh Aldous

Chairman, Chairman of the Management Engagement Committee

Hugh is a director of three public companies, two listed in the UK and one in the US, where he chairs respectively audit and corporate governance committees. He is also Chairman of the board of a Guernsey investment company. Previously, Hugh has been Executive Chairman of an AIM listed company sold to a FTSE 100 company, director and chairman of London listed investment companies, chairman of a funds administrator and chairman of four companies backed by private equity. Hugh's current quoted company directorships include a London listed fund management company managing three listed investment companies and some 19 open-ended funds, a US speciality chemicals company quoted on NASDAQ and a Venture Capital Trust. Hugh's career included 35 years as director of a wide selection of companies from nationalised industries to private equity across a range of sectors, 10 years as managing partner, and latterly head of Financial Services, of Robson Rhodes (now Grant Thornton), 16 years of appointments as a DTI Companies Act Inspector responsible for several reports, including two major published reports, and membership of the UK Monopolies & Mergers and Competition Commissions.

Andrew Griffiths

Andrew founded Green Star Media Ltd after a career in print journalism including five years as business correspondent of The Daily Telegraph. Andrew has been responsible for the creation and launch of eleven specialist magazines and newsletters, including the AIM Newsletter. Andrew has been a non-executive director of several venture capital trusts and was previously a Non-Executive Director of Downing ONE VCT plc.

Stephen Yapp

Chairman of the Audit Committee

Stephen has almost 25 years' experience as director of public and private companies over the course of his career. Presently, Stephen is Non-Executive Chairman at Pittards Plc and Chairman of MNH Grp Limited. Stephen was Non-Executive Director of Journey Group Limited (formerly Journey Group plc), Executive Chairman of Altitude Group Plc from September 2013 to April 2015 and of Redstone plc (now Castleton Technology plc) from September 2009 to September 2010, and Non- Executive Director of Imagesound plc (now Imagesound Limited) from January 2007 to December 2008. Prior to this, Stephen was Chief Executive of DCS Group plc between 2001 and 2006 and held the position of Finance Director at SBG between 1997 and 2000. Stephen is also a Fellow Chartered Management Accountant and holds an MBA.

All Directors were appointed on 17 February 2017 and are considered independent of the Manager. All Directors are members of the Management Engagement Committee and the Audit Committee.

Director's report

The Directors present their report together with the audited financial statements of the Company for the period ended 28 February 2018.

Directors

The Directors of the Company in office at the date of this report and their biographies are set out on page 30. Details of their interests in the Ordinary Shares of the Company are provided on page 50. All of the Directors, and Diana Hunter who resigned on 4 April 2018, held office throughout the period under review.

In accordance with the provisions of the Company's Articles of Association:

- each Director shall retire at the annual general meeting held in the third calendar year following the year in which he was elected or last re-elected by the Company;
- each Director shall retire at each annual general meeting following the ninth anniversary of the date on which he was first elected (as opposed to re-elected) by the Company; and
- a Director who retires at any annual general meeting shall be eligible for re-election unless the Directors otherwise determine.

In accordance with the Articles, each of the Directors having been appointed on incorporation of the Company on 17 February 2017 holds office only until the first annual general meeting. Each Director in office at the date of this report will offer himself for election by shareholders at that meeting. Accordingly, Mr Aldous, Mr Griffiths, and Mr Yapp will offer themselves for re-election for a further three years.

The Board considers that each of the current Directors bring to the Board extensive knowledge and commercial experience and individually have the knowledge, skills and experience required to provide effective and independent challenge, leadership and direction to the Company.

The Board accordingly recommends the election of each of the Directors.

There were no contracts in existence during or at the end of the year in which a Director of the Company is or was materially interested and which is or was significant in relation to the Company's business.

The powers of the Directors are set out in the corporate governance statement on pages 38 to 43.

Conflicts of interest

The Company's Articles of Association permit the Board to consider and, if appropriate, to authorise situations where a Director has an interest that conflicts, or might possibly conflict, with the Company. The Board has a formal system in place for the Directors to declare situations for authorisation by those Directors not interested in the situation. Any situations considered and any authorisations subsequently given are appropriately recorded.

The Board believes that the system it has in place for reporting, considering and recording situations where a Director has an interest that conflicts, or might possibly conflict, with the Company operates effectively and operated effectively during the period under review.

Directors' remuneration report and policy

The Directors' remuneration report is set out on pages 47 to 50. An advisory ordinary resolution to approve this report will be put to shareholders at the Company's AGM. The Company is also required to put the Director's remuneration policy to a binding shareholder vote. Accordingly, an ordinary resolution to approve the Company's remuneration policy will also be put to shareholders at the forthcoming AGM.

Directors' responsibilities

The Directors' responsibilities in preparing these financial statements are noted on page 51.

Investment management and administration

Management

The Company's investment manager is Downing LLP (the Investment Manager). The Investment Manager is responsible for providing management services to the Company in accordance with the Company's investment policy and the terms of the management agreement dated 23 March 2017. Further details of the terms of the Investment Management Agreement in respect of the calculation of the investment management fee are provided in note 4 on page 67.

The Investment Management Agreement is for a minimum term of three years and is terminable by the Company, or the Investment Manager, providing not less than six months' written notice, such notice not to expire prior to the expiry of the three-year minimum term.

Company secretarial and administration

Maitland Administration Services Limited has been appointed as Company Secretary and Administrator pursuant to the Administration Agreement. The Administrator provides general fund valuation, accounting and investment operation services to the Company, AIFM support services and company secretarial services.

The Administration Agreement is for an initial period of one year from the commencement date.

Either the Company or the Administrator may terminate the Administration Agreement by giving not less than three months' prior written notice, such notice not to expire earlier than the expiry of the initial period.

Custodian

The Northern Trust Company has been appointed as Custodian pursuant to the Custody Agreement. The Custody Agreement may be terminated by either party giving 30 days' written notice.

The Custodian receives a safe-keeping fee and transaction fees which vary by market, subject to a minimum fee of £7,500 per annum.

Registrar

Computershare Investor Services PLC has been appointed as registrar to the Company under the Registry Services Agreement. The Registrar is entitled to a fee calculated on the basis of the number of shareholders and the number of transfers processed. The Registry Services Agreement may be terminated on not less than six months' notice, such notice not to expire prior to the end of the third anniversary of the commencement date of the Registry Services Agreement.

The Registrar is also entitled to reimbursement of all disbursements and out of pocket expenses.

Appointment of the Investment Manager

The Board, through the Management Engagement Committee, considers arrangements for the provision of investment management and other services to the Company on an ongoing basis and a formal review is conducted annually. As part of this review the Board considers the quality and continuity of individuals responsible for the Company's affairs, the investment process and the performance achieved. The specialist nature of the Company's investment remit is, in the Board's view, best served by Downing LLP, who have a proven track record in small cap investing.

The principal contents of the agreement with the Investment Manager are set out in note 4. Having considered the terms of the agreement the Board considers that these represent an appropriate balance between cost and incentivisation of the Investment Manager.

It is the opinion of the Directors that the continuing appointment of the Investment Manager is in the interests of shareholders as a whole. The Board believes that the Investment Manager has executed the investment strategy in accordance with the Prospectus.

Change of Control

There are no agreements to which the Company is a party that might be affected by a change in control of the Company.

Going Concern

The financial statements of the Company have been prepared on a going concern basis. After reviewing the Company's budget, including the current financial resources and projected expenses for the next 12 months together with its medium-term plans, the Directors believe this to be an appropriate basis. The Directors consider that the Company is financially sound and has adequate resources to continue in operational existence for the foreseeable future, being a period of at least 12 months from the date on which these Financial Statements are approved. In reaching this conclusion, the Directors had particular regard to the Company's ability to meet its obligations as they fall due and the liquidity of the portfolio. The Company is also able to meet all of its liabilities from its assets and the ongoing charges are approximately 1.5% of the net assets.

The Company's longer term viability is considered in the Viability Statement on page 26.

Substantial Share Interests

As at 28 February 2018 the Company had received notification in accordance with the FCA's Disclosure and Transparency Rule 5.1.2R of the following interests in 3% or more of the voting rights attaching to the Company's issued share capital.

	Number of Ordinary Shares	% of issued share capital
The Central Finance Board of the Methodist Church UK Equity Fund and Epworth Investment Management Limited Affirmative Equity Fund	3,600,000	6.47
EQ Investors Limited	7,296,972	13.12
Downing One VCT PLC	5,000,000	8.99
Downing Four VCT PLC	4,600,000	8.27

EQ Investors Limited notified the Company that with effect from 14 May 2018 their holding of Ordinary Shares had increased to 7,857,654, 14.13% of the Company's issued share capital. There were no further changes notified in the period to 17 May 2018.

Share Capital

On incorporation, the issued share capital of the Company was £50,000.002 represented by 2 Ordinary Shares of a nominal value of £0.001 and 50,000 Management Shares of a nominal value of £1.00 each. To enable the Company to obtain a certificate of entitlement to conduct business and to borrow under Section 761 of the Companies Act 2006, on 17 February 2017, the 50,000 Management Shares were allotted fully paid to Downing Corporate Finance Limited, a member of the Investment Manager's group. The Management Shares were redeemed following Admission of the Ordinary Shares on 9 May 2017 out of the proceeds of the issue.

On 9 May 2017 as part of the initial public offering the Company issued 55.6 million Ordinary Shares of £0.001 each at a price of £1.00 per share in a placing, offer for subscription and intermediaries offer that raised £54.5 million after expenses.

Full details of the Company's issued share capital are given in note 12 on page 69. Details of the voting rights in the Company's shares as at the date of this report are also given in note XII to the Notice of Annual General Meeting on page 78. The Ordinary Shares carry the right to receive dividends and have one voting right per Ordinary Share. There are no restrictions on the voting rights of the Ordinary Shares. There are no shares which carry specific rights with regard to the control of the Company.

Discount management

The Directors recognise the importance to investors of ensuring that any discount of the Company's share price to the underlying NAV per Ordinary Share is as small as possible. The Directors will monitor any discount closely.

Share issues and repurchases

The Directors will consider repurchasing Ordinary Shares in the market if they believe it to be in shareholders' interests and as a means of correcting any imbalance between the supply and demand for Ordinary Shares.

Purchases of Ordinary Shares will be made at the discretion of the Board within guidelines established from time to time and regularly reviewed by the Board. Any such purchases will be made out of the available cash resources of the Company at prices below the relevant prevailing NAV (cum-income) per Ordinary Share. Ordinary Shares purchased by the Company may be held in treasury or cancelled.

On 15 March 2017 the Directors were granted authority to:

- make market purchases of up to 14.99% of the Ordinary Shares in issue on Admission to be held in treasury or cancelled;
- to allot such number of Ordinary Shares and/or C Shares in aggregate as shall equal 100 million Ordinary Shares and/or C Shares less the aggregate number of Ordinary Shares issued pursuant to the First Issue in the period immediately following First Admission.

The Directors considered that it was unnecessary to buy back any of the Ordinary Shares during the period as there was demand for them in the market.

During the period, the Company did not issue any new Ordinary or C Shares or purchase any shares for cancellation.

The current authorities expire at the conclusion of the first AGM of the Company and the Directors are proposing that the authorities be renewed at the forthcoming AGM.

Redemption facility

The Directors of the Company have discretion to implement a redemption facility through which shareholders will be entitled to request the redemption of all or part of their holding of Ordinary Shares with reference to a redemption pool or process set out by the Directors in any redemption year. Subject to the Board exercising its discretion to operate the redemption facility, the first redemption year will be 2020 and every second year following the first redemption year.

Treasury Shares

The Company may hold Ordinary Shares acquired by way of market purchases in treasury. The Company may hold up to 10% of the issued Ordinary Shares at any time in this way.

Ordinary Shares held in treasury may subsequently be cancelled or sold for cash. No Ordinary Shares will be sold at a price less than the (cum income) NAV per existing Ordinary Share at the time of their sale.

There were no shares held in treasury on 28 February 2018 and at the date of this report.

Cancellation of share premium

Pursuant to a special resolution approved by the Company on 15 March 2017, the Company applied for cancellation of its share premium account so that the amount standing to the credit of that account immediately following the issue of Ordinary Shares pursuant to the offer, be cancelled.

Court approval was received on 12 July 2017 and £54.5 million was transferred from the share premium account to distributable reserves.

Articles of Association

Any amendments to the Company's Articles must be made by special resolution.

Global greenhouse gas emissions

The Company has no greenhouse gas emissions to report from its operations, nor does it have responsibility for other emission producing sources under the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013.

Annual General Meeting

Note: this section is important and requires your immediate attention.

If you are in any doubt as to the action you should take, you should seek your own personal financial advice from your stockbroker, bank manager, solicitor or other financial advisor authorised under the Financial Services and Markets Act 2000.

Resolutions relating to the following items of special business will be proposed at the forthcoming AGM:

- **Resolution 9 Authority to allot shares:** the Directors may only allot shares for cash if authorised to do so by shareholders in a general meeting. This resolution seeks to renew the authority of the Directors to allot ordinary shares for cash up to an aggregate nominal amount of £2,830 (or such other amount as shall be equivalent to 5% of the Company's issued Ordinary share capital (excluding treasury shares) as at the date of passing the Resolution. The Directors will use this authority when it is in the best interests of the Company to issue ordinary shares for cash. This authority will expire at the conclusion of the AGM to be held in 2019 unless renewed prior to that date.
- **Resolution 10 Authority to disapply pre-exemption rights:** by law, Directors require specific authority from shareholders before allotting new shares or selling shares out of treasury for cash without first offering them to existing shareholders in proportion to their holdings. Resolution 10 empowers the Directors to allot new ordinary shares for cash or to sell shares held by the Company in treasury, otherwise than to existing shareholders on a pro rata basis, up to an aggregate nominal amount of £2,830 (or such other amount as shall be equivalent to 5% of the Company's issued Ordinary share capital (excluding treasury shares) as at the date of passing the Resolution. This authority will expire at the conclusion of the AGM to be held in 2019 unless renewed prior to that date.

- **Resolution 11 Authority to buy back shares:** the resolution to be proposed will seek to renew the authority granted to Directors enabling the Company to purchase its own shares. The Directors will only consider repurchasing shares in the market if they believe it to be in shareholders' interests and as a means of correcting any imbalance between supply and demand for the Company's shares. The Directors are seeking authority to purchase up to 8,340,000 (being the equivalent of 14.99% of the issued ordinary share capital (excluding treasury shares) or such other amount as shall be equivalent to 14.99% of the Company's issued Ordinary share capital (excluding treasury shares) as at the date of passing the Resolution. This authority will expire at the conclusion of the AGM to be held in 2019 unless renewed prior to that date. Any ordinary shares purchased pursuant to resolution 11 shall be cancelled immediately upon completion of the purchase or held, sold, transferred or otherwise dealt with as treasury shares in accordance with the provisions of the Companies Act 2006.

Recommendation

Your Board considers that each of the resolutions to be proposed at the Annual General Meeting is likely to promote the success of the Company for the benefit of its members as a whole and are in the best interests of the Company and its shareholders as a whole. The Directors unanimously recommend that shareholders vote in favour of the resolutions, as they intend to do in respect of their own beneficial holdings.

Corporate Governance

Full details are given in the Corporate Governance Statement on pages 38 to 43. The Corporate Governance Statement forms part of this Directors' Report.

Audit Information

As required by Section 418 of the Companies Act 2006 each of the Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are aware, there is no relevant audit information of which the Company's Auditor is unaware and each Director has taken all the steps that they ought to have taken as a Director to make themselves aware of any relevant audit information and to establish that the Company's Auditor is aware of that information.

Auditor

The Auditor, Grant Thornton UK LLP, is willing to continue in office. Resolutions proposing the reappointment of Grant Thornton UK LLP and authorising the Audit Committee to determine the Auditor's remuneration for the ensuing year will be proposed at the AGM.

Listing Rule 9.8.4

Listing Rule 9.8.4 requires the Company to include certain information in a single identifiable section of the annual Report or a cross reference table indicating where the information is set out. The Directors confirm that there are no disclosures to be made in this regard.

By order of the Board

Maitland Administration Services Limited
Secretary

23 May 2018

Corporate Governance Statement

As a UK-listed investment trust company our principal reporting obligation is driven by the UK Corporate Governance Code (the UK Code) issued by the Financial Reporting Council (FRC). However, listed investment trusts differ in many ways from other listed companies and the Association of Investment Companies (AIC) has prepared the AIC Code of Corporate Governance (AIC Code), which has been approved by the FRC, to provide boards with a framework of best practice for the governance of investment companies and to satisfy their requirements in relation to the UK Code.

The UK Code is available from the FRC website at frc.org.uk. The AIC Code is available from the AIC at the aic.co.uk.

Statement of compliance

The Board has made the appropriate disclosures in this report to ensure that the Company meets its continuing obligations. It should be noted that, as an investment trust, most of the Company's day-to-day responsibilities are delegated to third parties, the Company has no employees and the Directors are non-executive. Therefore, not all of the provisions of the UK Code are directly applicable to the Company.

The Board considers that the Company has complied with the recommendations of the AIC Code and the provisions contained within the UK Code that are relevant to the Company throughout this financial period, except for the provisions relating to:

- the role of the chief executive;
- executive directors' remuneration;
- the need for an internal audit function; and
- the appointment of a senior independent director.

For reasons set out in the AIC Guide and as explained in the UK Code, the Board considers that these provisions are not relevant to the Company being an investment company with no executive employees. Information on how the Company has applied the principles of the AIC and UK codes is set out below.

The Board

The Board is collectively responsible for the success of the Company. It is accountable to shareholders for the direction and control of all aspects of the Company's affairs and is ultimately responsible for framing and executing the Company's strategy and closely monitoring risks.

The Board aims to run the Company in a manner that is responsible and to engage with investors. The Directors are committed to maintaining high standards of financial reporting, transparency and business integrity.

The Board currently consists of three non-executive Directors, all of whom are independent of the Investment Manager. The Directors' biographies including details of other significant commitments, are provided on page 30. The biographical details demonstrate that the Directors possess a breadth of investment, commercial and professional experience and a wide range of business and financial expertise relevant to the leadership of the Company.

The provision of the UK Code which relates to the combination of the roles of the chairman and chief executive does not apply as the Company has no executive directors.

Delegation of responsibilities

The Investment Management Agreement between the Company and Downing LLP sets out the matters delegated to the Investment Manager, which include the management of the Company's assets and the exercise of voting rights attached to the securities held in the portfolio. Further details of the terms of the Agreement are set out on page 32. The review of the Investment Manager's performance is an ongoing duty and responsibility of the Board which is carried out at every Board meeting. In addition, a formal review is undertaken annually, details of which are set out in the section on the Company's Management Engagement Committee below.

The provision of accounting, company secretarial and administration services has been delegated to Maitland Administration Services Limited under the terms of the Administration Agreement. The terms of the agreement are summarised on page 32.

The assets of the Company have been entrusted to the custodian for safekeeping. The Custodian is The Northern Trust Company. The address at which the business is conducted is given on page 83.

A formal schedule of matters reserved to the Board for decision has been approved. This includes monitoring of the Company's investment objectives and policy and its future strategic direction, gearing policy, management of the capital structure, appointment and removal of third party service providers, review of key investment and financial data and the Company's corporate governance and risk control arrangements.

Internal control

The Board has established an ongoing process for identifying, evaluating and managing the significant risks faced by the Company. The process conforms to the recommendations of the FRC's Guidance on Risk Management, Internal Control and Related Financial and Business Reporting and is subject to regular review by the Board. The Board is responsible for the Company's system of internal controls and for reviewing its effectiveness. However, such a system can only be designed to manage rather than eliminate the risk of failure to achieve business objectives and therefore can only provide reasonable, but not absolute, assurance against fraud, material misstatement or loss.

The Board maintains a risk matrix, which provides a detailed risk and internal control assessment and is the basis for the Audit Committee and the Board to regularly monitor the effective operation of the controls. The risk matrix is updated when new risks are identified. The risk matrix covers all material financial, operational, compliance controls and risk management systems.

Investment management, custody of assets and all administrative services are provided to the Company by the Investment Manager, Custodian and Administrator respectively. As a consequence, the Company monitors the services provided by these service providers and the operating controls established by them.

The Board, through the Audit Committee, has reviewed the effectiveness of the Company's system of internal controls for the period under review and to the date of this report. During the course of the review no failings or weaknesses determined as significant were identified.

As the Company's investment management, administration and custodial activities are carried out by third party services providers, the Board does not consider it necessary to have an internal audit function or whistleblowing procedures. The Audit Committee reviews annually the whistleblowing procedures of the Investment Manager and the Administrator.

Financial reporting

The statement of Directors' responsibilities in respect of the annual report and financial statements is set out on page 51, the report of the Independent Auditor on pages 52 to 59 and the statement of going concern on page 33.

Board structure and management

The Board meets on a quarterly basis to review investment performance, financial reports and other reports of a strategic nature. Board or Board committee meetings are also held on an ad hoc basis to consider matters as they arise. Key representatives of the Investment Manager and the Company Secretary attend each Board meeting. The Investment Manager, Company Secretary and the Board have a constructive and co-operative relationship. Communication between meetings is maintained between the Board, Investment Manager, Company Secretary and other service providers.

The attendance record for each scheduled meeting held during the period under review is set out below.

Director	Scheduled meetings					
	Board		Audit		Management engagement	
	Number held	Number attended	Number held	Number attended	Number held	Number attended
Hugh Aldous	3	3	1	1	1	1
Andrew Griffiths	3	3	1	1	1	1
Diana Hunter*	3	3	1	1	1	1
Stephen Yapp	3	3	1	1	1	1

* ceased to be a director on 4 April 2018.

Role of the Chairman

With the support of the Company Secretary the Chairman sets the agenda for meetings, manages the meeting timetable and facilitates open and constructive dialogue both during and between the meetings.

Directors' appointment, retirement and succession

Details on the appointment, retirement and rotation of Directors are set out in the Directors' report on page 31.

The Board's individual independence, including that of the Chairman, has been considered, and this independence allows all of the Directors to sit on the Company's various committees.

The Board's view on tenure is that length of service is not necessarily an impediment to independence or good judgement and does not therefore have a formal policy requiring Directors to stand down after a fixed period. It considers that a long association with the Company and experience of a number investment cycles is valuable and does not compromise a Directors' independence.

Appointments will be reviewed as part of the regular board performance evaluations. Directors must be able to demonstrate their commitment, including in terms of time to the Company. The Board will seek to ensure that it is well balanced and refreshed regularly by the appointment of new Directors with relevant skills and experience.

The Board has not appointed a Senior Independent Director in accordance with the provisions of the UK Code. The Board, which is small and entirely comprised of independent non-executive directors, does not consider the appointment of a Senior independent Director is necessary.

Directors' induction training and development

When a Director is appointed he or she will be offered an induction programme organised by the Investment Manager and will be provided with key information on the Company's policies, regulatory and statutory requirements, internal controls and the responsibilities of a director.

Directors are encouraged to keep up to date with industry developments and attend training courses on matters directly relevant to their involvement with the Company. The Directors receive regular briefings from the Company Secretary regarding any proposed developments or changes in laws or regulations that could affect the Company.

Diversity

The Board's policy on diversity, including gender, is to take this into account during the recruitment and appointment process. However, the Board is committed to appointing the most appropriate candidate, regardless of gender or other forms of diversity and therefore no targets have been set against which to report.

Provision of information and support

There is an agreed procedure for Directors, in the furtherance of their duties, to take independent professional advice, if necessary, at the Company's expense. All Directors have access to the Company Secretary, who is responsible for ensuring compliance with appropriate statutes and regulations.

The Chairman, with the assistance of the Company Secretary, ensures that the Directors receive accurate, timely and clear information. All Directors receive appropriate documentation in advance of each Board and committee meeting including detailed briefings on all matters in order to discharge their duties effectively in considering a matter and reaching a decision on it.

The appointment and removal of the Company Secretary is a matter for the whole Board.

Performance evaluation

The Board undertook a self-evaluation of its performance, that of its committees and individual Directors, including the Chairman, in February 2018. The reviews were led by the Chairman, in the case of the Board, and the relevant Chairman for each committee. Each Chairman, assisted by the Company Secretary, determined the scope and format for the review, which due to the Directors having been in-post for only a year was predominantly by way of focused discussions. There were no significant actions arising from the evaluation process and it was agreed that the composition of the Board, at that time, reflected a suitable mix of skills and experience, and that the Board as a whole, the individual Directors and its committees were functioning effectively.

Directors' liability insurance

During the year the Company has maintained appropriate insurance cover in respect of legal action against the Directors.

Board committees

The Board has delegated authority to the committees detailed below and has put in place terms of reference for each committee which are available on the Company's website and from the registered office.

Remuneration Committee

The Company's policy on Directors' remuneration, together with details of the remuneration of each Director, is detailed in the Directors' Remuneration Report on pages 47 to 50. As stated in the Directors' Remuneration Report, the full Board determines the level of Directors' fees and accordingly there is no separate Remuneration Committee.

Nomination Committee

As the Board is small and all of the Directors are non-executive, a separate nomination committee has not been established. The full Board will review its structure and composition. Appointments of new Directors will be made on a formalised basis, with the Board agreeing the selection criteria and the method of selection, recruitment and appointment. Board diversity, including gender, will be taken into account in establishing the criteria. The Board has already instigated a search for a director to replace Diana Hunter following her resignation.

Audit Committee

The Audit Committee which is chaired by Stephen Yapp consists of all the Directors of the Company. Further details are provided in the Report of the Audit Committee on pages 44 to 46.

Management Engagement Committee

The Company's Management Engagement Committee comprises all Directors and is Chaired by Hugh Aldous. The Committee considers the performance, terms, fees and other remuneration payable to the Investment Manager, the Administrator and other service providers. Annually, it reviews the appropriateness of the Investment Manager's continued appointment, together with the terms and conditions of the Investment Management Agreement.

Shareholder relations

The Board is committed to ensuring that there is open and effective communication with the Company's shareholders. The Investment Manager and the Company's broker maintain regular dialogue with major shareholders and provide the Board with reports and feedback.

All shareholders are encouraged to attend and vote at the Company's Annual General Meeting. The Board and the Investment Manager will be available at the Annual General Meeting to discuss issues affecting the Company and to answer any questions. The Notice of Annual General Meeting is set out on pages 78 to 80 and details the business of the meeting. Any item not of an entirely routine nature is explained in the Directors' Report on pages 36 and 37. The Notice of Annual General Meeting and any related papers are sent to shareholders at least 20 business days before the meeting.

Shareholders may contact the Board through the Investment Manager or the office of the Company Secretary. The contact details are given on page 83.

Bribery Prevention Policy

The Company has zero tolerance towards bribery and is committed to carrying out business fairly, honestly and openly. The Board takes its responsibility to prevent bribery seriously and its service providers are contacted in respect of their anti-bribery policies.

Criminal Finances Act 2017

The Board has a zero-tolerance approach to the facilitation of tax evasion.

For and on behalf of the Board

Hugh Aldous
Chairman

23 May 2018

Report of the Audit Committee

The Company has established a separately chaired Audit Committee that will meet at least twice a year and operates within written terms of reference detailing its scope and duties.

Composition

Given that the Board is small it is considered appropriate for all of the Directors to sit on the Audit Committee, including the Chairman of the Company. The members of the Audit committee consider that they have the requisite skills and experience to fulfil the responsibilities of the Committee. The Chairman of the Audit Committee, Stephen Yapp and Hugh Aldous both have recent and relevant financial experience, and the Audit Committee as a whole has competence relevant to the sector.

Role of the Audit Committee

The role of the Audit Committee is to assist the Board in applying financial reporting and internal control principles and to maintain an appropriate relationship with the Auditors. The Audit Committee formally reports to the Board.

Responsibilities

During the period the principal activities of the Audit Committee included:

- considering and recommending to the Board for approval the contents of the half yearly and Annual Report and Financial Statements and reviewing the Independent Auditor's Report thereon;
- reviewing the appropriateness of the Company's accounting policies;
- following the completion of the audit, the committee will review the effectiveness of the external audit process, the quality of the audit engagement partner, the audit team and based on the review will make a recommendation to the Board on the re-appointment of the auditor;
- considering the quality of the formal audit report to shareholders;
- reviewing and approving the external auditor's plan for the financial period, with a focus on areas of audit risk and the consideration of the appropriateness of the level of audit materiality;
- considering the audit and non-audit services fees payable to the external Auditor and the terms of their engagement; and
- reviewing the adequacy of the internal control systems and evaluating the need for an internal audit function as set out in the Corporate Governance Statement on page 38.

The fees paid to the external Auditor are set out in note 5 on page 67.

Non-audit services

During the period under review, Grant Thornton provided non-audit corporate advisory services to the Company in relation to the listing of the Company on the Main Market of the London Stock Exchange. These included the provision of comfort letters and consents in relation to the documents produced for the IPO. For these services the Company paid Grant Thornton £17,500. The ratio of the fee for non-audit services compared to the audit fee was 70%.

All requests for services to be provided by the external Auditor will be submitted to the Committee in order to ensure that the scope and nature of the proposed work does not affect the Auditor's independence or objectivity and will be determined on a case-by-case basis.

Auditor appointment and tenure

The Committee reviews the scope and results of the external audit, its effectiveness and cost effectiveness and the independence and objectivity of the external Auditor. In the Directors' opinion the Auditor is independent of the Company. The Committee also has primary responsibility for making recommendations to the Board on the re-appointment and removal of the external Auditor.

Representatives of the Company's Auditor attend the Audit Committee meeting at which the draft Annual Report and Financial Statements are considered and also engage with the Directors as and when required. Having reviewed the performance of the external Auditor, including assessing the quality of work, timing of communications and work with the Investment Manager, the Committee considered it appropriate to recommend the Auditors reappointment. The Board supported this recommendation and a resolution will be put to shareholders at the forthcoming AGM.

Grant Thornton UK LLP has been Auditor to the Company since launch in May 2017. The Company is required to re-tender, at the latest, by 2027. Due to the short period since the appointment of the Auditor it is not considered appropriate to review the Auditor's succession at this juncture.

The period under review is the Audit Partner, Marcus Swales' first of a five-year maximum term.

Significant issues considered regarding the Annual Report and Financial Statements

During the year, the Audit Committee considered a number of significant issues and areas of key audit risk in respect of the annual report and financial statements. The Audit Committee reviewed the external audit plan at an early stage and concluded that the appropriate areas of audit risk relevant to the Company had been identified and that suitable audit procedures had been put in place to obtain reasonable assurance that the financial statements as a whole would be free of material misstatements. The table overleaf sets out the key areas of risk identified and also explains how these were addressed.

Significant issue	How the issue was addressed
Valuation, existence and ownership of investments	The valuation of investments is undertaken in accordance with the accounting policies, disclosed in Note 2 on pages 64 to 67. Controls are in place to ensure that valuations are appropriate and existence is verified through custodian reconciliations. The custodian remains responsible for the oversight of the custody of the Company's assets.
Recognition of investment income	The Board relies on the Administrator and the Investment Manager to use correct prices and seeks comfort in the testing of this process through the internal control statements. The Board reviews income forecasts and receives explanations from the Investment Manager for any variations or significant movements from previous forecasts. Subjective elements of income such as special dividends will be reviewed by the Board to agree the accounting treatment.
Maintenance of investment trust status	The Investment Manager and Administrator have reported to the Audit Committee to confirm continuing compliance with the requirements for maintaining investment trust status. The position is also discussed with the Auditor as part of the audit process.

Conclusions in respect of the annual report and financial statements

Having taken all available information into consideration and having discussed the content of the annual report and financial statements with the Investment Manager, Company Secretary and other third-party service providers, the Audit Committee has concluded that the annual report and financial statements as a whole are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position, performance, business model and strategy, and has reported these findings to the Board. The Board's conclusions in this respect are set out in the statement of directors' responsibilities on page 51.

Stephen Yapp
Chairman of the Audit Committee

23 May 2018

Directors' remuneration report

The Board presents the Directors' remuneration report for the period 17 February 2017 to 28 February 2018, which has been prepared in accordance with the requirements of Sections 420-422 of the Companies Act 2006 (the Act) and Schedule 8 of The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008, as amended (the Regulations). An ordinary resolution for the approval of the Directors' remuneration report will be put to shareholders at the forthcoming AGM.

By law, the Company's Auditors are required to audit certain of the disclosures provided. Where disclosures have been audited it is indicated as such. The Auditor's opinion is included in the Independent Auditor's report on pages 52 to 59.

As the Company has no employees and all of the Directors are non-executive, the Board has not established a separate Remuneration Committee. Directors' remuneration is determined by the Board as a whole, at is discretion within an aggregate ceiling of £150,000 per annum. Each Director abstains from voting on their own individual remuneration.

Statement from the Chairman

This Report sets out the Company's remuneration policy which shareholders will also be asked to approve at the 2018 AGM. A separate resolution to adopt the remuneration report is advisory only and not binding on the Company.

Subject to shareholder approval the remuneration policy, set out in the following policy table below, will be binding and effective from the date of the 2018 AGM. It is intended to apply for three years.

Policy Table

Fixed fee element	Remuneration consists of a fixed fee each year and the Directors of the Company are entitled to such rates of annual fees as the Board at its discretion determines.
Discretionary element	In accordance with the Company's Articles of Association, if a Director is requested to perform extra or special services, they will be entitled to receive such additional remuneration as the Board considers appropriate.
Taxable benefits	In accordance with the Company's Articles of Association the Directors are also entitled to be reimbursed for out-of-pocket expenses and any other reasonable expenses incurred in the proper performance of their duties. Such expenses are treated as a benefit in kind and are subject to tax and national insurance.
Purpose and link to strategy	Directors' fees are set to: ▸ be sufficient to attract and retain individuals of a high calibre with suitable knowledge and experience to promote the long-term success of the Company; ▸ reflect the time spent by the directors on the Company's affairs; ▸ reflect the responsibilities borne by the directors; ▸ recognise the more onerous roles of the Chairman of the Board and the Chairman of the Audit Committee through the payment of higher fees.
Operation	Fees payable to the Directors will be reviewed annually. A number of factors will be considered to ensure that the fees are set at an appropriate level. These will include the average rate of inflation during the period since the last fee increase, the level of Directors' remuneration for other investment trusts of a similar size and complexity of the Directors' responsibilities.
Maximum	Total remuneration paid to the non- executive Directors is subject to an annual aggregate limit of £150,000 in accordance with the Company's Articles of Association. Any changes to this limit will require Shareholder approval by ordinary resolution.

There are no performance related elements to the Directors' fees.

Directors do not receive bonus payments or pension contributions from the Company or any option to acquire shares. There is no entitlement to exit payments or compensation on loss of office. None of the Directors has a service contract with the Company and their terms of appointment are set out in a letter provided when they join the Board. These letters are available for inspection at the Company's registered office.

Consideration of Shareholders' Views

In accordance with the requirements of the Companies Act 2006 shareholder approval for the remuneration report will be sought at the 2018 AGM. Shareholders will have the opportunity to express their views and raise any queries on the policy at this meeting.

Remuneration Policy Implementation Report (Audited)

Single Total Figure of Remuneration

The single total remuneration figure for each Director who served during the period 17 February 2017 is set out below.

	Period ended 28 February 2018	
Director	Fees £	Expenses £
Hugh Aldous	29,167	-
Andrew Griffiths	20,833	-
Diana Hunter*	20,833	-
Stephen Yapp	25,000	-
Total	95,833	-

* ceased to be a director on 4 April 2018.

It is not proposed to increase the remuneration for the financial year ending 28 February 2019.

No discretionary payments were made during the period 17 February 2017 to 28 February 2018.

There were no changes to Directors' remuneration during the period to 28 February 2018. The Directors were remunerated for their services from the date of launch, 9 May 2017, and were therefore paid on a pro rata basis. The fees paid to Directors on an annual basis during the period to 28 February 2018 were;

- Chairman - £35,000
- Chairman of the Audit Committee - £30,000; and
- all other Directors - £25,000.

As the Company has no employees the table above sets out the total remuneration costs and benefits paid by the Company.

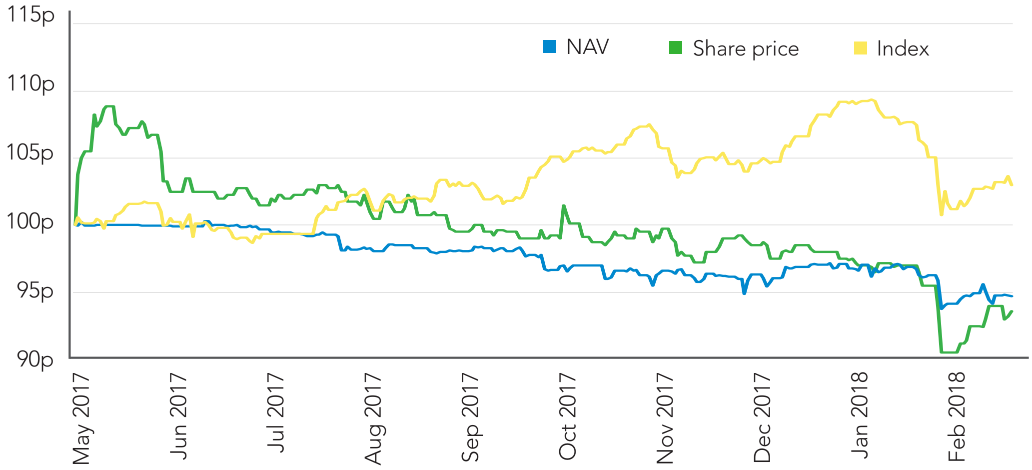
Relative importance of spend on remuneration

The following table shows the proportion of the Company's income spent on remuneration during the period 17 February 2017 to 28 February 2018.

	Period ended February 2018
Management fees paid in the period	447,998
Total remuneration paid to the directors	95,833
Loss on ordinary activities after tax	(2,818)

Performance

The Company does not have a specific benchmark against which performance is measured. The graph below compares the Company's NAV and share price on a total return basis with the total return on an equivalent investment in the Numis Smaller Companies Index plus AIM (excluding investment companies), where the majority of the investments held in the Company's portfolio are drawn from and which is therefore considered the closest broad index against which to measure the Company's performance.



*The Company commenced trading on the main market of the London Stock Exchange on 9 May 2017. Source: Downing LLP. Index: Numis Smaller Companies Index Plus AIM Ex. Investment Companies.

Directors' interests in shares (Audited)

There are no requirements for the Directors to own shares in the Company.

The Directors interests and those of their connected persons in the Ordinary Shares of the Company are set out in the table below. All of the holdings are beneficial and all of the Directors held office during the period under review.

Director	17 May 2018	28 February 2018	9 May 2017[2]
	Ordinary Shares of 0.1 pence per share		
Hugh Aldous	145,091[3]	145,091[3]	120,091[3]
Andrew Griffiths	15,075	15,075	15,075
Diana Hunter[1]	N/A	23,667	23,667
Stephen Yapp	100,500	100,500	100,500

[1] ceased to be a director on 4 April 2018.
[2] date of admission to trading.
[3] includes 19,791 shares held by Mrs Aldous.

No other changes to these holdings had been notified up to the date of this report. The Directors' Remuneration Report was approved by the Board on 18 May 2018.

For and on behalf of the Board

Hugh Aldous
Chairman
23 May 2018

Statement of Directors' responsibilities in respect of the annual report and financial statements

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the Company's financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. 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 and loss 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 estimates that are reasonable and prudent;
- state whether IFRS as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping 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 to enable them to ensure that the financial statements 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 are also responsible for preparing the strategic report, directors' report, Directors' remuneration report, the corporate governance statement and the report of the Audit Committee in accordance with the Companies Act 2006 and applicable regulations, including the requirements of the listing Rules and the Disclosure and Transparency Rules.

The Directors consider that the annual report, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

Each of the Directors, who are listed on page 30, confirms that, to the best of his knowledge:

- the financial statements, which have been prepared in accordance with IFRS as adopted by the European Union on a going concern basis, give a true and fair view of the assets, liabilities, financial position and profits of the Company; and
- the Strategic 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.

For and on behalf of the Board

Hugh Aldous
Chairman

23 May 2018

Independent Auditor's Report to the members of Downing Strategic Micro-Cap Investment Trust PLC

Opinion

Our opinion on the financial statements is unmodified.

We have audited the financial statements of Downing Strategic Micro-Cap Investment Trust PLC (the 'Company') for the period ended 28 February 2018 which comprise the statement of comprehensive income, the statement of changes in equity, the statement of financial position, the statement of cash flow and notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

In our opinion, the financial statements:

- give a true and fair view of the state of the Company's affairs as at 28 February 2018 and of its loss for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; 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. 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.

Who we are reporting to

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.

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 pages 23 and 24 that describe the principal risks and explain how they are being managed or mitigated;
- the directors' confirmation, set out on page 26 of the annual report, that they have carried out a robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity;
- the directors' statement, set out on page 64 of the financial statements, about whether the directors considered it appropriate to adopt the going concern basis of accounting in preparing the financial statements and the directors' identification of any material uncertainties to the Company'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 relating 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 of the annual report, as to how they have assessed the prospects of the Company, 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 Company 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

- Overall materiality £517,000 which represents 1% of the Company's net assets.
- Key audit matters were identified as valuation of investments, existence and ownership of investments and completeness and occurrence of gains and losses on investments held at fair value through profit or loss and investment income.
- Our audit approach was a risk based substantive audit focused on investments at the period end and investment income recognised during the period.

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 that 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 forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key issue	How the matter was addressed in the audit
Valuation of investments The company's investment objective is to generate long-term shareholders returns, mainly in the form of capital growth. This objective is pursued through a focused portfolio of UK micro-cap investments comprising of quoted and unquoted holdings. As at the period end, the company holds a significant holding in one unquoted investment and a number of quoted investments. The investment portfolio at £32.9 million is a significant material balance in the statement of financial position at period -end and the main driver of the Company's performance. Of total investment portfolio, £27.1 million of investments were quoted on recognised stock exchanges, and £5.7 million were held in the form of unquoted loan notes. As different valuation approaches are applied to the different types of investments, there are risks that the investment valuation recorded in the Statement of Financial Position may be misstated. In addition, as unquoted investments are not traded in an active market, management are required to apply judgement in determining the value of these investments. There is a risk that fair value measurements priced using inputs not based on observable market data (using models or similar techniques) may not be correct. We therefore identified valuation of investments as a significant risk which was one of the most significant assessed risks of material misstatement.	**Quoted investments** Our audit work included, but was not restricted to: ▸ obtaining understanding of management's process to value quoted investments through discussions with the management and examination of control reports on third party administrators; ▸ assessing whether the Company's accounting policy for the valuation of investments is in accordance with IFRSs as adopted by the European Union and the Statement of Recommended Practice 'Financial Statements of Investment Trust Companies and Venture Capital Trust' (SORP) and testing whether management have accounted for valuation in accordance with that policy; ▸ independently pricing 100% of the quoted equity portfolio by obtaining the bid prices from the independent market sources and calculating the total valuation based on the Company's investment holdings; and ▸ extracting a report of trading volumes on monthly basis from an independent market source for the equity investments held to test that investments are actively traded. **Unquoted investments** Our audit work included, but was not restricted to: ▸ obtaining an understanding of matters that may affect the fair value of the unquoted investments through discussions with the Investment Manager and independent research into the investee company; ▸ assessing the qualifications, expertise and valuation approach of the expert used by management so we were able to place reliance on for accuracy of these valuations of investee company (we obtained the expert's valuation reports and had discussions with management to challenge the assumptions and estimates supporting the valuations); and ▸ using our valuation experts to confirm our challenge of the investment manager on the valuation methodology used and whether this was in accordance with IFRSs as adopted by the European Union and the SORP. Specifically focussing on the appropriateness of the valuation basis selected, ability of the underlying investment company to repay at the time of maturity of the investment and the underlying assumptions such as discount rate used. The Company's accounting policy on valuation of investments is shown in note 2 and related disclosures are included in note 9 and 15 to the financial statements. The Audit Committee identified valuation of investments as a significant issue in its report on page 44, where the Committee has also described the action that it has taken to address this issue. **Key observations** Our audit work did not identify any material misstatements concerning the valuation of investments.

Key issue	How the matter was addressed in the audit
Existence and ownership of investments There is a risk that the beneficial rights of the Company over the investments may not exist. An error in the holdings could material impact the Company's net asset. We therefore identified existence and ownership of investments as a significant risk which was one of the most significant assessed risks of material misstatement.	Our audit work included, but was not restricted to: ▸ understanding of process in place that ensures all investments transcations are recorded through discussion with management and examination of control reports on third party custodian and administrator; ▸ substantively testing a sample of additions of investments made during the period by agreeing such transactions to bank statements and support documentation such as subscription agreements (no disposals were noted during the period); and ▸ confirming the existence and ownership by comparing the holdings listed in the investment portfolio to an independent confirmation by the Company's custodian. Existence and ownership of unquoted investments was confirmed by loan note subscription agreements and also checked to abridged interim financial statements of the investee company. **Key observations** Our audit work did not identify any material misstatements concerning existence and ownership of investments.
Completeness and occurrence of gains and losses on investments held at fair value through profit or loss and investment income During the period, the Company has recognised losses on investments held at fair value through profit or loss of £2.4 million in capital and investment income of £417,000 revenue. Income from investments is a significant, material item in the statement of comprehensive income. Under International Standard on Auditing (UK) 240 'The auditor's responsibilities relating to fraud in an audit of financial statements', there is a presumed risk of fraud in revenue recognition. We therefore identified completeness and occurrence of gains and losses on investment held at fair value through profit or loss and investment income as a significant risk, which was one of the most significant assessed risks of material misstatement.	Our audit work included, but was not restricted to: ▸ assessing the design and implementation of controls in relation to revenue recognition; ▸ assessment and testing of revenue recognition policies to obtain comfort on compliance with IFRSs and the Statement of Recommended Practice issues by the SORP; ▸ recalculating the unrealised gains and losses arising on investments held at fair value through profit and loss; and ▸ substantively testing income transactions. For investments held during the period, obtaining the ex-dividend dates and rates for dividends declared during the period from an independent source and agreeing the expected dividend entitlements to those recognised in the statement of comprehensive income and agreeing dividend income recognised by the Company to an independent source. to gain comfort over occurrence of income in the period.For unquoted loan notes, this was achieved by recalculating interest income in accordance with underlying agreements. The Company's accounting policy on revenue recognition is shown in note 2 to the financial statements and related disclosures are included in note 3 and note 9. **Key observations** Our audit work did not identify any material misstatements concerning the occurrence and completeness of investment income.

Our application of materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality in determining the nature, timing and extent of our work and in evaluating the results of that work.

We determined materiality for the audit of the financial statements as a whole to be £517,000, which is 1% of the Company's net assets. This benchmark is considered the most appropriate because net assets, which primarily comprise the company's investment portfolio, are considered to be the key driver of the company's total return performance and form a part of the net asset value calculation.

We use a different level of materiality, performance materiality, to drive the extent of our testing and this was set at 75% of financial statement materiality.

We also determine a lower level of specific materiality for certain areas such as investment income being main driver of the Company's performance and related party transactions, being the management fee and directors' remuneration.

We determined the threshold at which we will communicate misstatements to the audit committee to be £35,000. In addition we will communicate misstatements below that threshold that, in our view, warrant reporting on qualitative grounds.

An overview of the scope of our audit

Our audit approach was a risk-based approach founded on a thorough understanding of the Company's business, its environment and risk profile and in particular included:

- obtaining an understanding of relevant internal controls at both the Company and third-party service providers. This included obtaining and reading internal controls reports prepared by the third-party service providers on the description, design, and operating effectiveness of the internal controls at the custodian and administrator; and
- performing substantive audit procedures on specific transactions, which included journal entries and individual material balances and disclosures, the extent of which was based on various factors such as our overall assessment of the control environment and our evaluation of the design and implementation of controls that address significant audit risk.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report set out on pages 4 to 51, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our 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 this 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 51 – 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 pages 44 to 46 – 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 pages 38 to 43 – 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.

Our opinions on other matters prescribed by the Companies Act 2006 are unmodified

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

Matter on which we are required to report under the Companies Act 2006

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 the directors' report.

Matters on which we are required to report by exception

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 for the financial statements

As explained more fully in the directors' responsibilities statement set out on page 51, 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.

We are responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. Owing to the inherent limitations of an audit, there is an unavoidable risk that material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the ISAs (UK).
Our audit approach is a risk-based approach and is explained more fully in the 'An overview of the scope of our audit' section of our audit report.

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

Other matters which we are required to address

We were appointed as auditors by the directors under an engagement letter dated 16 March 2017.

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 our audit.

Our audit opinion is consistent with the additional report to the audit committee.

Marcus Swales
Senior Statutory Auditor

for and on behalf of Grant Thornton UK LLP

Statutory Auditor, Chartered Accountants

London

23 May 2018

GrantThornton

Company accounts

Statement of comprehensive income

For the period 17 February 2017 (date of incorporation) to 28 February 2018

	Revenue (£'000)	Capital (£'000)	Total (£'000)
Losses on investments at fair value through profit or loss (note 9)	-	(2,447)	(2,447)
Investment income (note 3)	417	-	417
	417	(2,447)	(2,030)
Investment management fee (note 4)	(90)	(358)	(448)
Other expenses (note 5)	(339)	(1)	(340)
	(429)	(359)	(788)
Loss before taxation	(12)	(2,806)	(2,818)
Taxation (note 7)	-	-	-
Loss for the period	(12)	(2,806)	(2,818)

	Revenue (p)	Capital (p)	Total (p)
Loss per Ordinary Share (note 6)	**(0.03)**	**(6.22)**	**(6.25)**

The total column of this statement represents the statement of comprehensive income of the Company prepared in accordance with International Financial Reporting Standards ('IFRS') as adopted by the European Union.

The supplementary revenue and capital return columns are prepared under guidance published by the Association of Investment Companies (AIC).

The loss for the period disclosed above represents the Company's total comprehensive income. The Company does not have any other comprehensive income.

All items in the above statement are those of a single entity and derive from continuing operations. No operations were acquired or discontinued during the period.

There are no comparative figures for the prior year as the Company was incorporated on 17 February 2017. These are therefore the first financial statements produced by the Company.

The notes on pages 64 to 73 form an integral part of these financial statements.

Statement of changes in equity

For the period ended 28 February 2018

	Share capital £'000	Share premium account £'000	Special reserve £'000	Capital reserve £'000	Revenue reserve £'000	Total £'000
At 17 February 2017	-	-	-	-	-	-
Loss for the period	-	-	-	(2,806)	(12)	(2,818)
Issue of Management Shares	50	-	-	-	-	50
Redemption of Management Shares	(50)	-	-	-	-	(50)
Issue of Ordinary Shares	56	55,544	-	-	-	55,600
Expenses of share issue	-	(1,038)	-	-	-	(1,038)
Cancellation of share premium account	-	(54,506)	54,506	-	-	-
Dividends paid (note 8)	-	-	-	-	-	-
At 28 February 2018	56		54,506	(2,806)	(12)	51,744

There are no comparative figures for the prior year as the Company was incorporated on 17 February 2017. These are therefore the first financial statements produced by the Company.

The notes on pages 64 to 73 form an integral part of these financial statements.

Statement of financial position

As at 28 February 2018

	2018 £'000
Non-current assets	
Investments held at fair value through profit or loss (note 9)	32,861
	32,861
Current assets	
Trade and other receivables (note 10)	114
Cash and cash equivalents	20,704
	20,818
Total assets	53,679
Current liabilities	
Trade and other payables (note 11)	(1,935)
	(1,935)
Total assets less current liabilities	51,744
Net assets	51,744
Represented by:	
Share capital (note 13)	56
Special reserve	54,506
Capital reserve	(2,806)
Revenue reserves	(12)
Equity shareholders' funds	51,744
Net asset value per Ordinary Share (note 13)	93.06p

There are no comparative figures for the prior year as the Company was incorporated on 17 February 2017. These are therefore the first financial statements produced by the Company.

The financial statements were approved by the Board on 23 May 2018 and were signed on its behalf by:

Hugh Aldous, Chairman
Downing Strategic Micro-Cap Investment Trust PLC
Registered in England and Wales, no. 10626295.

The notes on pages 64 to 73 form an integral part of these financial statements.

Statement of cash flow

For the period 17 February 2017 (date of incorporation) to 28 February 2018

	(£'000)
Operating activities	
Loss before tax	(2,818)
Losses on investments at fair value through profit or loss	2,447
Increase in other receivables	(114)
Increase in other payables	119
Purchases of investments	(33,492)
Sales of investments	-
Net cash outflow from operating activities	(33,858)

Financing activities	
Issues of Ordinary Shares	55,600
Expenses of Ordinary Share issue	(1,038)
Issue of Management Shares	50
Cancellation of Management Shares	(50)
Dividends paid	-
Net cash inflow from financing activities	54,562

Change in cash and cash equivalents	20,704
Cash and cash equivalents at start of period	-
Cash and cash equivalents at end of period	20,704

Comprises	
Cash and cash equivalents	20,704

There are no comparative figures for the prior year as the Company was incorporated on 17 February 2017. These are therefore the first financial statements produced by the Company.

The notes on pages 64 to 73 form an integral part of these financial statements.

Notes to the financial statements

1. General information

Downing Strategic Micro-Cap Investment Trust PLC (the Company) was incorporated in England and Wales on 17 February 2017 with registered number 10626295, as a closed-end investment company.

The Company commenced its operations on 9 May 2017. The Company intends to carry on business as an investment trust within the meaning of Chapter 4 of Part 24 of the Corporation Tax Act 2010.

The Company's shares were admitted to the Official List of the UK Listing Authority with a premium listing on the 9 May 2017. On the same day, trading of the Ordinary Shares commenced on the London Stock Exchange.

2. Accounting policies

The principal accounting policies followed by the company are set out below:

Basis of accounting

The annual financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. These comprise standards and interpretations approved by the International Accounting Standards Board (IASB), together with interpretations of the International Accounting Standards' and Standing Interpretations Committee (IASC) that remain in effect, and to the extent that they have been adopted by the European Union.

These financial statements are presented in Sterling (£) rounded to the nearest thousand. Where presentational guidance set out in the statement of recommended practice 'Financial Statements of Investment Trust Companies and Venture Capital Trusts' (SORP), issued by the Association of Investment Companies (as updated in January 2017), is consistent with the requirements of IFRS, the Directors have sought to prepare the financial statements on a consistent basis compliant with the recommendations of the SORP.

There are no comparative figures for the prior year as the Company was incorporated on 17 February 2017. These are therefore the first financial statements produced by the Company.

Going concern

The financial statements have been prepared on a going concern basis and on the basis that approval as an investment trust company will continue to be met.

The Directors have made an assessment of the Company's ability to continue as a going concern and are satisfied that the Company has the resources to continue in business for the foreseeable future, being a period of 12 months from the date these financial statements were approved. Furthermore, the Directors' are not aware of any material uncertainties that may cast significant doubt upon the Company's ability to continue as a going concern, having taken into account the liquidity of the Company's investment portfolio and the Company's financial position in respect of its cash flows and investment commitments. Therefore, the financial statements have been prepared on the going concern basis.

Presentation of statement of comprehensive income

In order to better reflect the activities of an investment trust and in accordance with guidance issued by the AIC, supplementary information which analyses the income statement between items of revenue and capital nature has been presented alongside the income statement. The net revenue is the measure the Directors believe is appropriate in assessing the Company's compliance with certain requirements set out in the Investment Trust (Approved Company) (Tax) Regulations 2011.

Accounting developments

The following amendments to standards effective this year, being relevant and applicable to the Company, have been adopted, although they have no impact on the financial statements:

- Amendments to IAS 7 - Disclosure initiative - statement of cash flows
- Amendments to IAS 12 - Recognition of deferred tax assets for unrealised losses

The following accounting standards and their amendments were in issue at the period end but will not be in effect until after this financial year end. The Directors are considering the impact these accounting standards will have on the financial statements.

International Financial Reporting Standards

- IFRS 7 Financial Instruments: disclosures for initial application of IFRS 9 - effective 1 January 2016 or when IFRS 9 is first applied
- IFRS 9 Financial Instruments - effective 1 January 2018
- IFRS 15 Revenue from Contracts with Customers - effective 1 January 2018
- IFRS 16 Leases - effective 1 January 2019

The revised IFRS 9 Financial Instruments replaces IAS 39 and applies to the classification and measurement and impairment of financial assets and liabilities, and hedge accounting. The adoption of IFRS 9 will have an effect on the classification but not the measurement of the Company's financial assets, but will potentially have no impact on the classification and measurement of financial liabilities. It will also introduce a new expected loss impairment model requiring more timely recognition of expected credit losses and a reformed model for hedge accounting with enhanced disclosure of risk management activity. The Standard is effective for annual period beginning on or after 1 January 2018.

Critical accounting judgements and uses of estimation

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of policies and the amounts reported in the balance sheet and the income statement. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. There were no significant accounting estimates or significant judgements in the current period, except the loan notes of Real Good Food as explained in note 14.

Investments held at fair value

All investments held by the Company are designated at 'fair value through profit or loss'. Investments are initially recognised at cost, being the fair value of the consideration given. After initial recognition, investments are measured at fair value, with unrealised gains and losses on investments recognised in the statement of comprehensive income and allocated to capital. Realised gains and losses on investments sold are calculated as the difference between sales proceeds and cost.

For investments actively traded in organised financial markets, fair value is generally determined by reference to quoted market bid prices at the close of business on the balance sheet date, without adjustment for transaction costs necessary to realise the asset.

When a purchase or sale is made under a contract, the terms of which require delivery within the time frame of the relevant market, the investments concerned are recognised or derecognised on the trade date.

Unquoted investments are valued by the Directors at the balance sheet date based on recognised valuation methodologies, in accordance with International Private Equity and Venture Capital (IPEVC) Valuation Guidelines such as dealing prices or third-party valuations where available, net asset values and other information as appropriate.

All investments for which fair value is measured or disclosed in the financial statements will be categorised within the fair value hierarchy in the notes of the financial statements, described as follows, based on the lowest significant applicable input:

- Level 1 reflects financial instruments quoted in an active market.
- Level 2 reflects financial instruments whose fair value is evidenced by comparison with other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets.

- Level 3 reflects financial instruments whose fair value is determined in whole or in part using a valuation technique based on assumptions that are not supported by prices from observable market transactions in the same instrument and not based on available observable market data. For investments that are recognised in the financial statements on a recurring basis, the Company determines whether transfers have occurred between levels in the hierarchy by re-assessing the categorisation (based on the lowest significant applicable input) at the date of the event that caused the transfer.

Income

Dividends receivable on quoted equity shares are taken into account on the ex-dividend date. Where no ex-dividend date is quoted, they are brought into account when the Company's right to receive payment is established.

Special dividends will be taken to revenue or capital account depending on their nature. In deciding whether a dividend should be regarded as a capital or revenue receipt, the Company will review all relevant information as to the reasons for the sources of the dividend on a case by case basis.

When the Company elects to receive scrip dividends in the form of additional shares rather than in cash, the amount of the cash dividend forgone is recognised as income. Any excess in the value of the cash dividend will be recognised in the capital column.

Interest on debt securities is recognised on an accruals basis.

Other investment income and interest receivable are included in the financial statements on an effective interest rate basis.

Expenses

All expenses are accounted for on an effective interest rate basis. All expenses are charged through the revenue account in the statement of comprehensive income except as follows:

- expenses which are incidental to the acquisition of an investment are included within the costs of the investment; and
- expenses which are incidental to the disposal of an investment are deducted from the disposal proceeds of the investment.

All other expenses are allocated to revenue with the exception of 80% of the Investment Manager's fee which is allocated to capital. This is in line with the Board's expected long-term split of returns from the investment portfolio in the form of income and capital gains respectively.

Taxation

The charge for taxation is based on net revenue for the year. Deferred taxation is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date. Investment Trusts which have approval under section 1158 of the Corporation Tax Act 2010 are not liable for taxation on capital gains. Any tax relief obtained in respect of investment management fees and other capital expenses charged or allocated to the capital column of the statement of comprehensive income is reflected in the capital reserve and a corresponding amount is charged against the revenue column of the statement of comprehensive income. The tax relief is the amount by which corporation tax payable is reduced as a result of these capital expenses.

Cash and cash equivalents

Cash and cash equivalents are defined as cash in hand, demand deposits and short-term, highly liquid investments readily convertible to known amounts of cash and subject to insignificant risk of changes in value.

Share issue costs

Share issue costs relating to Ordinary Share issues by the Company are charged to the share premium account.

Segmental reporting

The Directors are of the opinion that the Company is engaged in a single segment of business, being investment business. The Company only invests in companies quoted in the UK.

Capital reserve

Capital reserve includes:

- gains and losses on the disposal of investments;
- exchange difference of a capital nature;
- expenses, together with the related taxation effect, allocated to this reserve in accordance with the above policies; and
- increase and decrease in the valuation of investments held at period end.

This reserve is distributable.

Revenue reserve

This reserve includes net revenue recognised in the revenue column of the statement of comprehensive income. This reserve is distributable.

Special reserve

The Company cancelled its share premium account following a court order issued on 12 July 2017. As a result, a distributable special reserve was created. This reserve is distributable.

Dividends payable to shareholders

Dividends to shareholders are recognised as a liability in the period in which they are paid or approved in general meetings and are taken to the statement of changes in equity. Dividends declared and approved by the Company after the balance sheet date have not been recognised as a liability of the Company at the balance sheet date.

3. Income

For the period 17 February 2017 to 28 February 2018

	£'000
Income from investments	
UK dividend income	173
UK fixed interest income	244
Total	**417**

4. Investment management fee

In respect of its services provided under the Management Agreement, the Investment Manager is entitled to receive a management fee payable monthly in arrears calculated at the rate of one twelfth of 1% of the market capitalisation as at the relevant calculation date.

The Investment Manager has agreed that, for so long as it remains the Company's Investment Manager, it will rebate such part of any management fee payable to it so as to help the Company maintain an ongoing charges ratio of 2% or lower.

At 28 February 2018, an amount of £43,368 was outstanding and due to Downing LLP in respect of Management fees.

For the period 17 February 2017 to 28 February 2018

	Revenue £'000	Capital £'000	Total £'000
Investment management fee	90	358	448

5. Other expenses

For the period 17 February 2017 to 28 February 2018

	£'000
Administration and secretarial fees	66
Audit services - Auditor's remuneration[1,2]	30
Directors' fees	96
Safe custody fees	22
Legal fees	30
Sundry fees	90
Taxation services	5
Revenue expenses	339
Capital expenses	1
Total expenses	**340**

[1]During the period, the Company paid £17,500 to the Auditors for non-audit services which included the provisions of comfort letters and consents in relation to the document produced for the IPO. The amount paid has been included in expenses of share issue taken to special reserves shown under note 14. The ratio of the fee for non-audit services compared to the audit fee was 70%.
[2]Inclusive of VAT at 20%.

6. Loss per Ordinary Share

For the period 17 February 2017 to 28 February 2018

	Net return £'000	Per share pence
Revenue return	(12)	(0.03)
Capital return	(2,806)	(6.22)
Total return	(2,818)	(6.25)
Weighted average number of Ordinary Shares		45,089,319

No shares have been issued since launch.

7. Taxation

For the period 17 February 2017 to 28 February 2018

	Revenue £'000	Capital £'000	Total £'000
UK corporation tax at 19.22%	-	-	-

The current taxation charge for the period differs from the standard rate of corporation tax in the UK of 19.22%. The differences are explained below:

	Revenue £'000	Capital £'000	Total £'000
Loss before taxation	(12)	(2,806)	(2,818)
Theoretical tax at UK corporation tax rate of 19.22%	(2)	(539)	(541)
Effects of:			
UK dividends not taxable	(33)	-	(33)
Capital items not taxable	-	470	470
Excess expenses in the period	35	69	104
Actual current tax charge	-	-	-

Factors that may affect future tax charges:

The Company has unrealised expenses of £543,000. It is unlikely that the Company will generate sufficient taxable profits in the future to utilise these expenses, therefore no provision for any deferred tax asset has been made in the current year. The Company has not provided for deferred tax on capital gains or losses arising on the revaluation or disposal of investments as it is exempt from tax on these items because of its status as an investment trust.

8. Dividends

The Board has decided that no final dividend will be paid.

9. Investments

For the period 17 February 2017 to 28 February 2018

	£'000
Opening book cost	-
Opening investment holding gains	-
Opening valuation	-
Movements in the period	
Purchases at cost	35,308
Disposals:	
Proceeds	-
Net realised losses on disposals	-
Movement in investment holding losses	(2,447)
Closing valuation	**32,861**
Closing book cost	35,308
Closing investment holding losses	(2,447)
	32,861
Realised gains on disposals	-
Movement in investment holding losses	(2,447)
	(2,447)

Transaction costs

During the period the Company incurred transaction costs of £44,330 and nil on purchases and sales respectively. These amounts are included in losses on investments, as disclosed in the statement of comprehensive income.

10. Trade and other receivables

At 28 February 2018

	£'000
Dividends receivable	109
Prepayment and other debtors	5
	114

11. Trade and other payables

At 28 February 2018

	£'000
Amount due to brokers	1,816
Other creditors	119
	1,935

12. Called-up share capital

At 28 February 2018

	£'000
At beginning of period	-
Issue of ordinary shares	56
At end of period	**56**

The Company was incorporated on 17 February 2017 with an issued share capital of £50,002 represented by 50,000 Management shares of £1.00 each and 2 Ordinary shares of £0.001. These Management shares were redeemed immediately following admission of the Ordinary shares on the 9 May 2017 out of the proceeds of this issue.

On 9 May 2017, the Company issued 55,600,000 Ordinary £0.001 shares at £1 per share in a placing, offer for subscription and intermediaries offer, raising £54.5 million after expenses.

As at 28 February 2018 there were 55,600,002 Ordinary shares in issue.

13. Net asset value per Ordinary Share

At 28 February 2018

	NAV per share pence	NAV attributable £'000
Ordinary Shares: Basic and diluted	93.06	51,744

NAV per Ordinary Share is based on net assets at the period end and 55,600,002 Ordinary Shares, being the number of Ordinary Shares in issue at the period end.

14. Analysis of financial assets and liabilities

Investment Objective and Policy

The Company's Investment Objective and Investment Policy are detailed on pages 19 to 21. The Company's investing activities in pursuit of its Investment Objective involve certain inherent risks. The Company's financial instruments can comprise:

- shares and debt securities held in accordance with the Company's Investment Objective and investment policies;
- derivative instruments for efficient portfolio management, gearing and investment purposes; and
- cash, liquid resources and short-term receivables and payables that arise from its operations.

The risks identified arising from the Company's financial instruments are market risk (which comprises market price risk, interest rate risk and foreign currency exposure risk), liquidity risk and credit and counterparty risk. The Company may enter into derivative contracts to manage risk. The Board reviews and agrees policies for managing each of these risks, which are summarised below.

Market risk

Market risk arises from uncertainty about future prices of financial instruments used in the Company's business. It represents the potential loss the Company might suffer through holding market positions by way of price movements, interest rate movements and exchange rate movements. The Investment Manager assesses the exposure to market risk when making each investment decision and these risks are monitored by the Investment Manager on a regular basis and the Board at quarterly meetings with the Investment Manager.

Market price risk

Market price risk (i.e changes in market prices other than those arising from currency risk or interest rate risk) may affect the value of investments.

The Board manages the risks inherent to the investment portfolio by ensuring full and timely reporting of relevant information from the Investment Manager.

Investment performance and exposure are reviewed at each Board meeting.

The Company's exposure to changes in market prices as at 28 February 2018 on its equity investments held at fair value through profit or loss was £32,861,000.

A 10% increase in the fair value of its investments at 28 February 2018 would have increased net assets attributable to shareholders by £3,286,000. An equal change in the opposite direction would have decreased the net assets and net profit available to shareholders by an equal and opposite amount. The analysis is based on closing balances only and is not representative of the period as a whole.

Fair value of loan notes of Real Good Food was calculated by discounting the expected future cash flows using the original effective interest ebing 6.5% and 10%. If these rates were increased by 2%, the fair value would have reduced by £206,502. As a result, net assets attributable to shareholders would decline by the same amount. An equal change in opposite direction would have increased the net assets attributable to shareholders by an equal and opposite amount.

Interest rate risk

Interest rate movements may affect the level of income receivable on cash deposits. The Company does not currently receive interest on its cash deposits.

The Company's financial assets may include investment in fixed interest securities, such as UK Corporate debt stock, whose fair value may be affected by movements in interest rates. The majority of the Company's financial assets and liabilities, however, are non-interest bearing. As a result, the Company's financial assets and liabilities are not subject to significant amounts of risk due to fluctuations in the prevailing levels of market interest rates. There was no exposure to interest bearing liabilities during the period ended 28 February 2018.

The possible effects on the fair value and cash flows that could arise as a result of changes in interest rates are taken into account when making investment decisions. The Board imposes borrowing limits to ensure gearing levels are appropriate to market conditions.

The interest rate profile of the Company was as follows:

At 28 February 2018

	£'000
Cash and cash equivalents	20,704
Real Good Food loan notes	5,749

The exposure, at 28 February 2018, of financial assets and liabilities to interest rate risk is shown by reference to:

- floating interest rates – when the rate is due to re-set; and
- fixed interest rates – when the financial instrument is due for repayment.

	2018 in one year £'000	2018 greater than or less £'000	2018 total one year £'000
Exposure to fixed interest rates:			
Unquoted loan notes	170	5,579	5,749
Cash and cash equivalents	20,704	-	20,704
Total	20,874	5,579	26,453

Foreign currency risk

All the Company's assets are denominated in Sterling and accordingly the only currency exposure the Company has is through the trading activities of its investee companies.

Liquidity risk

Liquidity risk is not significant as the Company is a closed-end investment trust and the majority of the Company's assets are investments in quoted equities and other quoted securities that are readily realisable.

Credit and counterparty risk

Credit risk is the risk of financial loss to the Company if the contractual party to a financial instrument fails to meet its contractual obligations.

Credit risk arises from two main sources. Firstly, the possibility that the issuer of a security will be unable to pay interest and principal in a timely manner. Secondly, there is the possibility of default of the issuer. Adhering to investment guidelines and avoiding excessive exposure to one particular issuer or scheme can limit credit risk.

The maximum exposure to credit risk as at 28 February 2018 was £26,562,000. The calculation is based on the Company's credit risk exposure as at 28 February 2018 and this may not be representative for the whole period.

The maximum exposure to credit at 28 February comprises:

	2018 £'000
Dividends	109
Cash and cash equivalents	20,704
Unquoted loan notes	5,749
Total	26,562

The Company's quoted investments are held on its behalf by The Northern Trust Company, acting as the Company's custodian. Bankruptcy or insolvency of the custodian may cause the Company's rights with respect to securities held by the custodian to be delayed. The Board monitors the Company's risk by reviewing the custodian's internal controls report.

Investment transactions are carried out with a number of brokers whose creditworthiness is reviewed by the Investment Manager. Transactions are ordinarily undertaken on a delivery versus payment basis whereby the Company's custodian bank ensures that the counterparty to any transaction entered into by the Company has delivered on its obligations before any transfer of cash or securities away from the Company is completed.

Cash is only held at banks that have been identified by the Board as reputable and of high credit quality.

None of the Company's assets are past due or impaired.

15. Fair value hierarchy

Financial assets and financial liabilities of the Company are carried in the statement of financial position at their fair value. The fair value is the amount at which the asset could be sold or the liability transferred in a current transaction between market participants, other than a forced or liquidation sale. For investments actively traded in organised financial markets, fair value is generally determined by reference to Stock Exchange quoted market bid prices and Stock Exchange Electronic Trading Services (SETS) at last trade price at the balance sheet date, without adjustment for transaction costs necessary to realise the asset.

The Company measures fair values using the following hierarchy that reflects the significance of the inputs used in making the measurements. Categorisation within the hierarchy has been determined on the basis of the lowest level input that is significant to the fair value measurement of the relevant assets as follows:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities.

An active market is a market in which transactions for the asset or liability occur with sufficient frequency and volume on an ongoing basis such that quoted prices reflect prices at which an orderly transaction would take place between market participants at the measurement date. Quoted prices provided by external pricing services, brokers and vendors are included in Level 1, if they reflect actual and regularly occurring market transactions on an arm's length basis.

Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices).

Level 2 inputs include the following:

- quoted prices for similar (i.e. not identical) assets in active markets;
- quoted prices for identical or similar assets or liabilities in markets that are not active. Characteristics of an inactive market include a significant decline in the volume and level of trading activity, the available prices vary significantly over time or among market participants or the prices are not current;
- inputs other than quoted prices that are observable for the asset (for example, interest rates and yield curves observable at commonly quoted intervals); and
- inputs that are derived principally from, or corroborated by, observable market data by correlation or other means (market-corroborated inputs).

Level 3 – Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The level in the fair value hierarchy within which the fair value measurement is categorised in its entirety is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. If a fair value measurement uses observable inputs that require significant adjustment based on unobservable inputs, that measurement is a Level 3 measurement. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgement, considering factors specific to the asset or liability.

At 28 February 2018

	Level 1 £'000	**Level 2 £'000**	**Level 3 £'000**	**Total £'000**
Quoted on Main Market	2,370	-	-	2,370
Quoted on AIM	24,742	-	-	24,742
Unquoted loan notes	-	-	5,749	5,749
	27,112	**-**	**5,749**	**32,861**

There were no transfers between level 1 and levels 2 during the period. A recognition of fair value measurements in level 3 is set out in the following table.

At 28 February 2018

	£'000
Opening balance	-
Purchases	5,749
Sales	-
Total gains or losses included in losses on investments in the statement of comprehensive income	
on assets sold	-
on assets held at period end	-
Closing balance	5,749

16. Capital management

The Company's capital is as disclosed in the statement of financial position and is managed on a basis consistent with its investment objective and policies, as discussed in the strategic report on pages 4 to 27. The principal risks and their management are disclosed in the strategic report.

17. Significant interests

As at 28 February 2018 the Company held interests amounting to 3% or more of the equity the following investee companies.

	Valuation £'000	Cost £'000	%
Redhall	2,896	4,126	12.43
Synectics	2,922	3,414	9.12
RGD	902	1,857	6.76
Ramsdens	3,086	1,857	5.13
AdEPT	3,518	3,629	4.79
Gama	5,303	4,928	4.70
Hargreaves	3,478	3,653	3.27
SiS	1,457	1,500	3.21
Braemar	2,370	2,735	3.20

18. Related parties and Investment Manager

Investment Manager

Downing LLP have been appointed as the Investment Manager to the Company. The relationship is governed by an agreement dated 23 March 2017.

The total investment management fee charged by Downing LLP for the period ended 28 February 2018 was £447,993. The amount outstanding at 28 February 2018 was £43,368.

Directors

Disclosure of the Directors' interests in the Ordinary Shares of the Company and fees and expenses payable to the Directors are set out in the Directors' Remuneration Report on pages 47 to 50. At 28 February 2018, there were no outstanding Directors' fees.

19. Contingent liabilities

There were no contingent liabilities at 28 February 2018.

Shareholder information

Financial calendar

Company year end: 28 February

Annual results announced: May

Annual general meeting: 27 June 2018

Company half-year end: 31 August

Half-yearly results announced: November

Share price and NAV

The Company's Ordinary Shares are listed on the main market of the London Stock Exchange. The market price of these shares can be found in the London Stock Exchange Daily Official List and in the Financial Times. The Company's NAV is published daily and released through the London Stock Exchange's Regulatory News Service and is available through the AIC.

Registrar enquiries

The register for the Ordinary Shares is maintained by Computershare Investor Services PLC. In the event of queries regarding your holding, please contact the registrar on 0370 707 1358.

Changes of name and/or address must be notified in writing to the registrar, whose address is:

Computershare Investor Services PLC, The Pavilions, Bridgwater Road, Bristol BS99 6ZZ.

Common Reporting Standard

Under the Common Reporting Standard financial institutions, including investment trust companies, are required to provide personal information to HMRC on investors who meet certain criteria set out in the legislation.

On an annual basis the Company will provide information to the local tax authority on the tax residencies of non-UK based certificated shareholders and corporate entities. The local tax authority may exchange this information with the tax authorities of another country or countries in which the shareholder may be a tax resident, where those countries, or the tax authorities in those countries, have entered into agreements to exchange financial account information.

New shareholders, excluding those whose shares are held in CREST, entered onto the Company's share register, will be sent a certification form for the purposes of collecting this information.

Share dealing

Investors wishing to purchase more shares in the Company or sell all or part of their existing holding may do so through their financial adviser, stockbroker or one of the platforms listed on the Company's website: downing.co.uk/strategic.

Nominee Code

Where shares are held in a nominee company name, the Company undertakes:

- to provide the nominee company with multiple copies of shareholder communications, so long as an indication of quantities has been provided in advance;
- to allow investors holding shares through a nominee company to attend general meetings, provided the correct authority from the nominee company is available; and
- Nominee companies are encouraged to provide the necessary authority to underlying shareholders to attend the Company's general meetings.

Website

Your Board is committed to shareholder engagement. To receive regular email news and updates about your trust please visit: **www.downingstrategic.co.uk**.

Useful information on the Company, such as investor updates and half year and annual reports can be found on the Company's website.

Company information

Downing Strategic Micro-Cap Investment Trust PLC is an investment company as defined under section 833 of the Companies Act 2006.

Country of incorporation: England.
Company Number: 10626295.
Registered office: Springfield Lodge, Colchester Road, Chelmsford, Essex, CM2 5PW.

AIC

The Company is a member of the Association of Investment Companies.

Glossary

C Shares

C ('Conversion') shares help an investment company grow in a way that protects the interests of existing ordinary shareholders. When an investment company wants to grow, it may issue C shares. These shares and the proceeds are held in a separate pool and invested in a portfolio of assets. After a certain period, or when the pool of new money is fully invested, the two portfolios are merged and the C shares are exchanged for ordinary shares.

Discount and premium

If the share price of an investment trust is lower than the net asset value (NAV) per share, the shares are trading at a discount to NAV. In this circumstance the price that an investor pays or receives for a share would be less than the value attributable to it by reference to the underlying assets. The discount is the difference between the share price (based on mid-market share prices) and the NAV, expressed as a percentage of the NAV.

A premium occurs when the share price is above the NAV. Investors would therefore be paying more than the value attributable to the shares by reference to the underlying assets.

Discounts and premia are generally the consequence of supply and demand for the shares on the stock market.

Gearing

Gearing is the process whereby the Company can borrow to purchase additional investments with the expectation that the return on the investments purchased will exceed the interest cost of the borrowings.

Gearing is calculated by dividing total assets less cash or cash equivalents by shareholders' funds expressed as a percentage.

Intrinsic value

The actual value of a company or an asset based on an underlying perception of its true value including all aspects of the business in terms of both tangible and intangible factors. This value may or may not be the same as the current market value.

Intrinsic value is a core concept to value investors that seek to uncover hidden investment opportunities.

Margin of safety (safety margin)

The difference between the intrinsic value of a stock and its market price.

Net asset value per Share (NAV) per Ordinary Share

The NAV is shareholders' funds expressed as an amount per individual share. Equity shareholders' funds are the total value of all of the company's assets, at current market value, having deducted all current and long-term liabilities and any provision for liabilities and charges.

The NAV is published daily.

Ongoing charges

Ongoing charges are expenses of a type that are likely to recur in the foreseeable future, whether charged to capital or revenue, and which relate to the operation of the investment company as a collective fund, excluding the costs of acquisition or disposal of investments, financing costs and gains or losses arising on investments. Ongoing charges are based on costs incurred in the year as being the best estimate of future costs and include the annual management charge. The calculation methodology is set out by the Association of Investment Companies.

Revenue return per Share

The revenue return per share is the revenue return profit for the year divided by the weighted average number of ordinary shares in issue during the year.

Total return performance

This is the return on the share price or NAV taking into account both the rise and fall of share prices and the dividends and interest paid to shareholders. Any dividends received by a shareholder are assumed to have been reinvested in either additional shares (for share price total return) or the Company's assets (for NAV total return).

Notice of Annual General Meeting

Notice is hereby given that the first Annual General Meeting of Downing Strategic Micro-Cap investment Trust PLC will be held at the **Andaz Hotel, 40 Liverpool Street, London, EC2M 7QN**, at **2:30pm on 27 June 2018** for the following purposes:

Ordinary business

1. To receive the Directors' Report and the financial statements for the period 17 February 2017 to 28 February 2018 with the report of the Auditor thereon.

2. To approve the Directors' Remuneration Report for the period 17 February 2017 to 28 February 2018.

3. To elect Hugh Aldous as a Director.

4. To elect Andrew Griffiths as a Director.

5. To elect Stephen Yapp as a Director.

6. To re-appoint Grant Thornton UK LLP as auditor to the Company to hold office from the conclusion of the first annual general meeting of the Company until the conclusion of the next general meeting at which financial statements are laid before the Company.

7. To authorise the Audit Committee to determine the Auditor's remuneration.

8. To approve the Directors' Remuneration Policy

Special business

Ordinary resolution

9. THAT the Directors of the Company be and they are hereby generally and unconditionally authorised, (in substitution of any authorities previously granted), in accordance with Section 551 of the Companies Act 2006 (the Act) to exercise all the powers of the Company to allot relevant securities (within the meaning of Section 551 of the Act) up to an aggregate nominal amount of £2,830, or such other amount as shall be equivalent to 5% of the Company's issued Ordinary Share capital (excluding treasury shares) as at the date of passing the Resolution provided that this authority shall expire at the conclusion of the next Annual General Meeting of the Company to be held in 2019 unless renewed at a general meeting prior to such time, save that the Company may before such expiry make offers, agreements or arrangements which would or might require relevant securities to be allotted after such expiry and so that the Directors of the Company may allot relevant securities in pursuance of such offers, agreements or arrangements as if the authority conferred hereby had not expired.

Special resolutions

10. THAT subject to the passing of Resolution 9 above, the Directors of the Company be and are hereby empowered pursuant to Sections 570 and 573 of the Companies Act 2006 (the Act) to allot and make offers of agreement to allot equity securities (within the meaning of Section 560 of the Act) and to sell equity securities held by the Company as treasury shares (as defined in section 724 of the Act) for cash pursuant to the authority conferred by Resolution 9 above as if Section 561(1) of the Act did not apply to any such allotment and sales of equity securities, provided this authority:

(a) shall expire at the conclusion of the next Annual General Meeting of the Company to be held in 2019 save that the Company may before such expiry make offers, agreements or arrangements which would or might require equity securities to be allotted or sold after such expiry and so that the Directors of the Company may allot and sell equity securities in pursuance of such offers, agreements or arrangements as if the authority conferred hereby had not expired;

(b) shall be limited to the allotment of equity securities and/or sale of equity securities held in treasury for cash up to an aggregate nominal amount of £2,830 (or such other amount as shall be equivalent to 5% of the Company's issued Ordinary Share capital (excluding treasury shares) as at the date of passing the Resolution; and

(c) shall be limited to the allotment of equity securities and/or sale of equity securities held in treasury at a price not less than the cum income net asset value per share as close as practicable to the allotment or sale.

11. THAT in substitution of any authorities previously granted to make market purchases of Ordinary shares of 0.001 pence in the Company (ordinary shares), the Company be and it is hereby authorised in accordance with section 701 of the Companies Act 2006 (the Act) to make market purchases of ordinary shares (within the meaning of section 693 of the Act) provided that:

(a) the maximum number of ordinary shares hereby authorised to be purchased is 8,340,000 (being the equivalent of 14.99% of the issued Ordinary Share capital (excluding treasury shares) or such other amount as shall be equivalent to 14.99% of the Company's issued Ordinary share capital (excluding treasury shares) as at the date of passing the Resolution;

(b) the minimum price (exclusive of expenses) which may be paid for an Ordinary share shall be 0.001 pence;

(c) the maximum price (exclusive of expenses) which may be paid for an ordinary share shall be the higher of (i) an amount equal to 5% above the average of the market values of the ordinary shares for the five business days immediately preceding the date of purchase as derived from the Daily Official List of the London Stock Exchange and (ii) the higher of the price quoted for (a) the last independent trade of, and (b) the highest current independent bid for any number of ordinary shares on the trading venue where the purchase is carried out; and

(d) unless revoked, varied or renewed prior to such time, the authority hereby conferred shall expire at the conclusion of the next Annual General Meeting of the Company to be held in 2019 save that the Company may, prior to such expiry enter into a contract to purchase ordinary shares which will or may be completed or executed wholly or partly after such expiry.

All ordinary shares purchased pursuant to the above authority shall either be:

(i) held, sold, transferred or otherwise dealt with as treasury shares in accordance with the provisions of the Act; or

(ii) cancelled immediately upon completion of the purchase.

Dated 23 May 2018

By Order of the Board

Maitland Administration Services Limited

Secretary

Registered Office:

Springfield Lodge
Colchester Road
Chelmsford
Essex
CM2 5PW

Notes

(i) This Report and Financial Statements is sent to holders of Ordinary Shares, all of whom are entitled to attend, speak and vote at the above Annual General Meeting (AGM).

(ii) Members entitled to attend and vote at the AGM are also entitled to appoint one or more proxies to exercise all or any of their rights to attend and speak and vote on their behalf. Where multiple proxies are appointed they must be appointed to exercise the rights in relation to different Ordinary Shares. Proxies need not be members of the Company.

(iii) A form of proxy is sent to members with the Annual Report and Financial Statements. To be valid the form of proxy and any power of attorney or other authority (if any) under which it is signed (or a notarially certified copy of that power of attorney or authority) must be completed and returned to the office of the Company's Registrar as soon as possible but so as to arrive no later than 2:30pm on 25 June 2018. Where multiple proxies are being appointed additional forms should be obtained from the Company's Registrar and a separate form completed for each proxy identifying, that the proxy is a multiple form and the different Ordinary Shares that each proxy represents. Completion and return of form(s) of proxy will not preclude a member from attending, speaking and voting in person at the AGM.

(iv) CREST members who wish to appoint a proxy or proxies by utilising the CREST electronic proxy appointment service may do so for the meeting and any adjournment(s) thereof by utilising the procedures described in the CREST Manual. 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.

(v) In order for a proxy appointment made by means of CREST to be valid, the appropriate CREST message (a "CREST Proxy Instruction") must be properly authenticated in accordance with Euroclear UK & Ireland Limited's ("EUI") specifications and must contain the information required for such instructions, as described in the CREST Manual. The message must be transmitted so as to be received by the issuer's agent Computershare (ID: 3RA50) by 2:30pm on 25 June 2018. In this respect the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by the CREST Applications Host) from which the issuer's agent is able to retrieve the message in the manner prescribed by CREST.

(vi) CREST members and, where applicable, their CREST sponsors or voting service providers should note that EUI does not make available special procedures in CREST for any particular messages. 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 such action as shall be necessary to ensure that a message is transmitted by means of the CREST system by the particular time the CREST member requires.

(vii) 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.

(viii) A person who is not a member of the Company and receives this notice of meeting as a person nominated by a member to enjoy information rights under Section 146 of the Companies Act 2006 ("Act") does not have a right to appoint proxies. However, if a nominated person has an agreement with the member who nominated them, the nominated person may have a right to be appointed as a proxy or a right to instruct the member as to the exercise of voting rights at the AGM.

(ix) Shareholders entered on the Register of Members of the Company at the close of business on 25 June 2018, or the close of business on the day two days prior to the time of an adjourned meeting, shall be entitled to attend and vote at the AGM. Any changes to the Register of Members after such dates shall be disregarded in determining the rights of any Shareholders to attend and vote at the AGM.

(x) Under Section 319(A) of the Act, the Company must cause to be answered any question relating to the business being dealt with at the AGM put by a member attending the AGM unless answering the question would interfere unduly with the preparation for the meeting, would involve the disclosure of confidential information, an answer has already been given on a website, or is undesirable in the interests of the Company or the good order of the AGM.

(xi) Members may not use any electronic address provided in this notice or any related document(s) to communicate with the Company for any purpose other than as specifically stated.

(xii) As at 17 May 2018, the latest practicable date prior to the publication of this notice, the Company's issued share capital comprised 55,600,002 Ordinary Shares of 0.1 pence each, of which none are held in treasury. Each Ordinary Share carries a right to one vote at general meetings of the Company and accordingly the total number of voting rights in the Company as at 17 May 2018 is 55,600,002.

(xiii) Information regarding the AGM, including the information required by Section 311A of the Act, can be found on the Company's web-pages by following the appropriate links at www.downingstrategic.co.uk.

(xiv) No Director has a service agreement with the Company. Directors' letters of appointment will be available for inspection at the AGM venue from 15 minutes before the time for the meeting until the conclusion of the meeting.

(xv) Member(s) have a right in accordance with Section 338 of the Act to require the Company to give to members of the Company entitled to receive the above notice of meeting, notice of any resolution which they may properly move at the meeting. Under Section 338A of the Act member(s) may request the Company to include in the business to be dealt with at the meeting any matter, other than a proposed resolution, which may be properly included in that business.

(xvi) Members may require the Company, under Section 527 of the Act, to publish on a website a statement setting out any matter relating to the audit of the Company's Financial Statements being laid before the meeting, including the Auditor's report and the conduct of the audit at the Company's expense. Where the Company is required to place such a statement on a website it must forward the statement to the Auditor not later than the time it makes the statement available on that website, and include the statement in the business to be dealt with at the meeting.

Contact details of the advisers

Company Secretary and Registered Office

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CM2 5PW

Telephone: 01245 398950

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Broker

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