

DOWNING PLANNED EXIT VCT 2 PLC DOWNING PLANNED EXIT VCT 3 PLC

INVESTOR GUIDE

Key Points

- **Tax Relief:** 30% income tax relief subject to circumstances and five year holding period
- **Planned Exit:** expected within six years
- **Managing Risk:** objective of reducing the risks normally associated with VCTs
- **Regular Income:** 7.1% p.a. tax-free target annual dividends on net of tax cost

Important Notice

An investment in Downing Planned Exit VCT 2 & 3 plc ("the Trust") is suitable only for investors who are capable of evaluating the risks (see overleaf) and merits of such an investment and who have sufficient resources to bear any loss that might arise. Investors are advised to take appropriate financial advice before investing in the Trust.

Introduction

Venture Capital Trusts ("VCTs") were introduced by the Government to encourage individuals to invest in a high risk portfolio of unquoted small businesses, by offering them substantial tax benefits.

To date, the Trust has raised £55 million and distributed over £20 million by way of dividends. It has now launched a new offer seeking to raise up to a further £20 million in a separate share class ("F Shares").

Investment Strategy

The funds awaiting investment (Non-Qualifying Investments) initially represent 100% of the funds raised and will progressively decline as Qualifying Investments are made, such that, after three years, less than 30% of each Trust's funds will be held in Non-Qualifying Investments.

Downing is continuing to see a strong flow in investment opportunities, which is being enhanced by the lack of alternative sources of finance.

Non-Qualifying Investments

The Trust will continue to seek to minimise cash deposits by making loans to businesses, typically secured by a charge over freehold or long leasehold property. This strategy has proved successful to date, as evidenced by the performance of the 2008 shares and the 2009 shares in the table in the next column.

Qualifying Investments

Downing has specialised in investing in businesses owning freehold or long leasehold property since the launch of its first VCT in 1997. The F Shares will focus on asset-backed investments and may also invest in businesses with predictable revenue streams.

Examples: children's nurseries, health clubs, pubs, conference centres and renewable energy businesses.

Track Record: Ordinary Shares

The Trust's ordinary shares (launched in 2004/05) have sold all their material investments and returned the proceeds to investors. These proceeds equated to an increase over the net (of tax relief) cost of 51% and provided a tax-free compound return of 11.2% per annum.

Track Record: 2008 & 2009 Shares

These share classes have only recently been launched and it is too early to judge performance. However, the strategy of minimising cash balances has resulted in modest increases in values, especially when compared to declining values in most other VCTs launched at the same time.

Downing Planned Exit VCT 2 & 3	Movement Since Inception ¹	Position in Peer Group ²
2008 Shares	+4.8%	Joint 2nd out of 14
2009 Shares	+2.6%	Joint 3rd out of 17

¹ Movement since inception is the latest published total return compared to the initial NAV at inception of 94.5p per share.
² This ranking is based on total return (net asset value plus cumulative dividends paid) out of all new VCTs or new VCT share classes launched in the relevant tax year. The total return for each VCT has been sourced by Downing from announcements made through a regulatory information service.

(Source: Downing)

It should be noted that past performance is not a reliable indicator of future performance.

Investment Example



In June 2011, Downing's VCTs invested £1.9 million in, and committed a further £2.77 million to, Kidspace Adventures Limited. The initial investment was used to repay the existing (non-management) funders of the business and repay debt. The existing business consists of two well established and profitable children's play centres in Croydon and Romford. The further commitment is to acquire the long lease of Horton Farm - an existing children's farm based in Epsom, Surrey. It is intended that Horton Farm will be redeveloped and re-launched in line with the high standards achieved at the existing two sites.

Note: this example is provided to illustrate the types of businesses in which Downing's VCTs invest. It is unlikely that the F Shares will invest in Kidspace Adventures Limited.



Illustrative Returns

Set out below is a table illustrating the hypothetical returns to investors at four different levels of shareholder proceeds, paid out within six years from the close of the Offers.

Illustrative returns based on an Offer Price of £1 per Share				
Shareholder proceeds	90p	100p	110p	120p
Less: net cost of investment (assuming 30% income tax relief)	(70p)	(70p)	(70p)	(70p)
Tax-free cash profit	20p	30p	40p	50p
Tax-free profit (as a % of net cost of investment)	+29%	+43%	+57%	+71%
Net return ¹	5.2% p.a.	7.4% p.a.	9.3% p.a.	11.1% p.a.
Gross equivalent return ² to:				
■ 40% taxpayers	8.7% p.a.	12.3% p.a.	15.5% p.a.	18.5% p.a.
■ 50% taxpayers	10.4% p.a.	14.8% p.a.	18.6% p.a.	21.2% p.a.
The returns set out above are for illustrative purposes only and no forecast or projection is implied or should be inferred.				
¹ The Net Return is the internal rate of return based on an investment of 100p deemed to be made on 5 April 2012, 30p income tax relief deemed to be received six months later on 5 October 2012 and either 90p, 100p, 110p or 120p of shareholder proceeds, comprising dividends of 5.0p payable on 30 November 2012 and dividends of 2.5p payable on 31 July 2013 and 30 November 2013 and on the same dates each year until 30 November 2016, 50% of the balance of the shareholder proceeds on 31 July 2017 and the remaining funds on 30 April 2018.				
² The gross equivalent return is compared to a source of income that is subject to income tax at an investor's marginal tax rate. It has been calculated by dividing the Net Return by 0.6 for 40% taxpayers and by 0.5 for 50% taxpayers.				

Risk Factors

The key risks are set out below (please read page 1 of the Securities Note for a full list of risk factors):

- **Tax reliefs:** the availability of the tax reliefs depends on the companies invested in maintaining their qualifying status. If the Trust does not maintain VCT qualifying status investors could lose the upfront 30% income tax relief and all other tax reliefs. All tax reliefs are subject to change in the future and personal circumstances. Please refer to HM Revenue & Customs' website for further guidance on the tax reliefs available on VCT investments.
- **Liquidity:** it may prove difficult for shareholders to sell their shares at a fair price, or at all.
- **Investment performance:** the Trust will invest in small unlisted companies which, by their nature, are higher risk than larger "blue-chip" companies. Shares in such companies may be difficult to sell.
- **Investment restrictions:** the Trust's ability to obtain maximum value from its investments may be limited by the VCT rules. Changes in the VCT rules may be applied retrospectively and may reduce the level of returns for investors.
- **Speculative risk:** the value of shares may go down as well as up and shareholders may not receive back the full amount invested. In addition, there is no certainty as to the level of dividends.

Exit Policy

The Trust will seek to sell all its investments after 5 years, paying the proceeds to investors at full value and completing the process in approximately 6 years. Prior to 5 years, the Trust will buy back shares at net asset value (nil discount), subject to regulations and having sufficient cash resources.

Taxation Benefits to Investors

The principal UK tax reliefs, which are available on a maximum investment of £200,000 in each of the 2011/12 and 2012/13 tax years, are set out below:

- **Income tax relief at 30%** of the amount subscribed provided the VCT shares are held for at least 5 years. Relief is restricted to the investor's tax liability.
- **Tax-free distributions and capital gains.**

This is a very brief summary of the current UK tax reliefs on VCTs. Potential investors are recommended to consult their own appropriate professional adviser as to the taxation consequences of their investing in a VCT.

Income

The Trust has a stated objective of paying annual dividends of 5p per share. This represents a tax-free income of 7.1% p.a. based on a net of tax offer price of 70p per share (100p less 30% income tax relief). It should be noted that dividend levels are not guaranteed and their payment will reduce the net assets remaining in the Trust.

IMPORTANT NOTICE

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