



Herald
LEADING-EDGE INVESTING

Herald Investment Trust plc

Half-yearly financial report
For the six months ended 30 June 2018

INVESTMENT POLICY AND OBJECTIVE

Herald's objective is to achieve capital appreciation through investments in smaller quoted companies in the areas of telecommunications, multimedia and technology ('TMT'). Investments may be made across the world. The business activities of investee companies will include information technology, broadcasting, printing and publishing and the supply of equipment and services to these companies.

PRINCIPAL RISKS AND UNCERTAINTIES

The principal risks facing Herald Investment Trust plc ('the Company') relate to the Company's investment activities. These risks are market risk (comprising other price risk, interest rate risk and foreign currency risk), credit risk and liquidity risk. An explanation of these risks and how they are managed is contained in note 18 of the Company's annual report and financial statements for the year to 31 December 2017. The principal risks and uncertainties have not changed since the publication of the Annual Report which can be obtained free of charge from Herald Investment Management Limited ('the Manager') (see contact details on page 13) and is available on its website: www.heralduk.com. Other risks facing the Company include the following: regulatory risk (that the loss of investment trust status or a breach of applicable legal and regulatory requirements could have adverse financial consequences and cause reputational damage); operational/financial/custody risk (failure of service providers' accounting and/or settlement systems could lead to inaccurate reporting or financial loss); the risk that the discount can widen; and gearing risk (the use of borrowings can magnify the impact of falling markets). Further information can be found on page 35 of the annual report and financial statements.

RESPONSIBILITY STATEMENT

We confirm that to the best of our knowledge:

- a) the condensed set of financial statements has been prepared in accordance with FRS104 'Interim Financial Reporting' published by the Financial Reporting Council and gives a true and fair view of the assets, liabilities, financial position and profit of the Company;
- b) the Half-yearly financial report and interim management report (Chairman's Statement) includes a fair review of the information required by Disclosure and Transparency Rules 4.2.7R (indication of important events during the first six months, and their impact on the financial statements and a description of principal risks and uncertainties for the remaining six months of the year); and
- c) the Half-yearly financial report includes a fair review of the information required by Disclosure and Transparency Rules 4.2.8R (disclosure of related party transactions and changes therein – see note 3 on page 10).

By order of the board

JULIAN CAZALET
CHAIRMAN
17 July 2018

SUMMARY OF PERFORMANCE

	At inception 16 February 1994	At 30 June 2018	At 31 December 2017	Performance since 31 December 2017	Performance since inception
Net asset value per ordinary share (including current year income)	98.7p	1,506.5p	1,374.9p	9.6%	1,426.3%
Net asset value per ordinary share (excluding current year income)	98.7p	1,506.1p	1,374.2p	9.6%	1,425.9%
Share price	90.9p	1,345.0p	1,171.0p	14.9%	1,379.6%
Numis Smaller Companies Index plus AIM (ex. investment companies)	1,750.0	5,898.4	6,001.8	(1.7%)	237.1%
Russell 2000 (small cap) Technology Index (in sterling terms)†	688.7*	2,867.8	2,480.2	15.6%	316.4%

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

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

Past performance is not a guide to future performance.

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



Source: Thomson Reuters

- Fully diluted NAV
- Share price
- Numis Smaller Companies Index plus AIM (excluding investment companies)
- Russell 2000 (small cap) Technology Index (in sterling terms, commenced March 1996)

CHAIRMAN'S STATEMENT

The Company's NAV per share rose 9.6% to 1,506.45p in the first half of 2018. This represents another good performance both relatively and absolutely. The UK, which still accounts for 56% of the Company's portfolio, returned 9.1% relative to the Numis Smaller Companies Index plus AIM (excluding investment companies) return of -0.4%. The North American component of the portfolio returned 18.7% against the sterling return for the Russell 2000 Technology Index of 15.8%. The smaller Asian segment returned 8.6% and the EMEA region returned 2.6%.

UK

GB Group is now the largest holding in the UK, as well as being the Company's single largest position. It delivered the biggest appreciation in assets, adding £9.4m of value (+37%). Wandisco was the second biggest winner, adding £6.5m. In percentage terms, the biggest returns came from Seeing Machines, Lombard Risk, Elektron Technology and Versarien; all of these more than doubled.

Takeover activity remains high. SQS (announced last year), Fidessa, Lombard Risk and Cityfibre have all been acquired. The period was more noticeable for the extremely large number of placings, together with a few new issues. This breathtaking level of activity normally signals that we are near a peak. Nevertheless, AIM is a vibrant market and the UK a fertile environment for entrepreneurs and underlying trading in our investee companies has generally been good. Our main concern is that the majority of interesting companies have a market capitalisation below £200m. Not many professional investors participate in such small companies. In contrast, private clients have been more conspicuously active. It is difficult to determine how much this is a structural shift, with the internet enabling a greater participation from savvy investors using platforms and disintermediating advisers, and how much of it is cyclical enthusiasm.

The manager has purposefully taken profits, selling £65.6m of UK company shares, including takeovers, and only made purchases of £27m during the half year. The manager believes it to be important to have cash to take advantage of any weakening of markets.

OVERSEAS

Takeovers in the US continue to outpace new issues and IPO activity has been relatively low, and performance stronger. The strong performers in the North American portfolio were LivePerson, Attunity, Radware, Five9, Mellanox Technologies and Varonis Systems. This list has a surprisingly high proportion of NASDAQ-listed Israeli companies, which have a more disciplined approach to share dilution from the issue of restricted stock units to staff and lower valuations than US based companies, together with a greater focus on delivering profits. Takeovers in North America have included Barracuda (announced last year), Callidus, Orbotech and Web.com which has received an offer from private equity.

The star performers in Asia were the two largest holdings, Kingdee International Software and 51job, which together accounted for the Asian return. There has been an increased focus on Australia, where software companies are flourishing.

The European performance was adversely affected by the largest holding, BE Semiconductor, which has delivered wonderful returns over a number of years but experienced profit taking in the first half as investors anticipated a semiconductor downturn. Elsewhere Nordic Semiconductor, Devoteam, Isra Vision, WALLIX and Data Respons all provided useful returns.

MARKET BACKGROUND

The market has now adopted MiFID II. As long-term investors with low trading volumes, we have always suffered from the inability to generate adequate commissions to receive a full service from as broad a range of brokers as the manager would prefer. It is helpful that the manager has expanded access to research and corporates with payments from the manager's own resources. Historically, larger investment houses covered the overheads of brokers with their client commissions, so proportional to funds under management, commissions cost a similar percentage for clients of large houses as for small. Now the costs are being carried by the manager, it is a harsher environment for small investment managers and for investors in small companies. The aggregate payments to brokers and research providers from the manager's direct research payments and trading commissions in 2018 is expected to be two and a half times the level of 2016, which was the last full year at higher commission rates. Fortunately, this increase in costs has coincided with a period of strong performance (which has itself contributed to some of the increase). Over 90% of research payments will be to global and overseas brokers because we are more reliant on their help for corporate access. It will be a challenge for smaller managers operating globally, particularly for investing in small companies which the global investment banks do not cover. However, we are aware that many of the larger investment houses are aggressively cutting research payments, and the fear is that their reductions will exceed the increased payments by smaller investment managers. The full extent of the squeeze on brokers has yet to emerge. Significantly, a number of analysts and salesmen in the broking fraternity have opted to leave the industry and work for corporations, which is a worrying development. Although MiFID-type rules have not been formally adopted in North America, many houses are adopting a global strategy and the pressure on smaller North American brokers is intense.

It is hard to determine quite what the motives of the regulator are, but it seems inconceivable that the regulator intended to challenge the smaller companies market in the way that it seems to be doing, when these markets provide essential capital for small businesses.

Cash balances have risen to about £100m (including short-dated government bonds). Receipts from takeovers have been £46m, with a potential further £23m from takeovers pending. Interestingly, nearly half the proceeds have come from bids by private equity groups. The Company undertook share buybacks during the period amounting to £9.5m.

Our manager continues to find good value companies, but some valuations have become quite full, so profits have been taken in some cases.

Politics continues to provide an unhelpful background, but I am pleased to say that companies are in general continuing to make strong progress. The valuation premia for growth companies in the portfolio seems surprisingly low. The world seems to be set for some monetary tightness, but the technology and media sectors which this Company targets should not suffer from rising interest rates as much as yield stocks, or those sensitive to interest rate hikes. The sector remains relatively attractive.

JULIAN CAZALET
CHAIRMAN
17 July 2018

TOP TWENTY EQUITY HOLDINGS

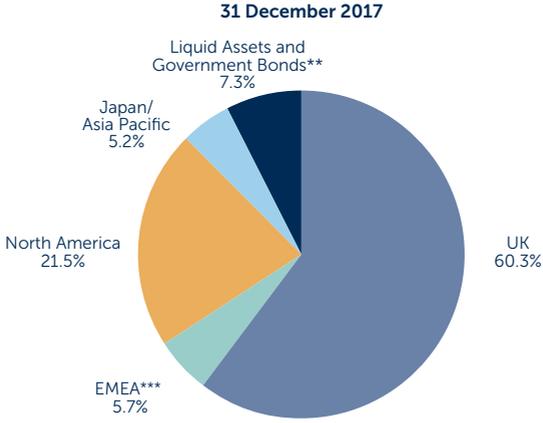
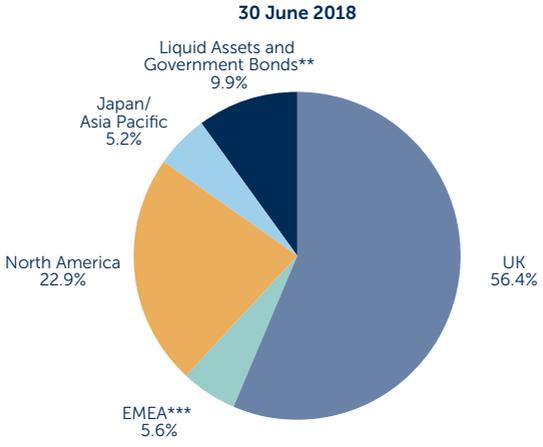
At 30 June 2018

Company	Business	Value £'000	% of total assets
GB Group	Intelligent identity data, software and services	33,294	3.2
Diploma	Distributor of components and systems	24,269	2.3
Next Fifteen Communications	Supplier of marketing communications services	19,313	1.8
IQE	Design and manufacture of compound semiconductor wafers	16,565	1.6
Bango	Provider of carrier billing and other alternative payment methods	15,688	1.5
Silicon Motion Technology ADR*	Develops controllers used in flash memory	15,346	1.5
YouGov	International opinion data surveys and analytics	14,950	1.4
Radware	Developer of application delivery and cyber security solutions	13,792	1.3
M&C Saatchi	Global marketing services business	13,619	1.3
Craneware	Automated revenue integrity software and solutions	13,248	1.3
Pegasystems	Develops applications for sales, marketing and operations	13,163	1.3
Statpro	Provider of portfolio analytics and risk management software	12,848	1.2
First Derivatives	Developer of database technology and software solutions	12,232	1.2
Descartes Systems	Supplier of logistics management software	11,771	1.1
LoopUp	Remote meetings collaboration solutions	11,730	1.1
Mellanox Technologies	Supplier of Ethernet and InfiniBand interconnect products	11,395	1.1
Euromoney Institutional Investor	Business to business media group	11,323	1.1
Boingo Wireless	Construction of Wi-Fi, cellular (DAS) and small cell networks	11,297	1.1
Microgen	Provider of financial management software and services	10,775	1.0
Seeing Machines	Developer of driver monitoring systems and solutions	10,733	1.0
		297,351	28.4

* American Depositary Receipt.

GEOGRAPHICAL SPREAD OF INVESTMENTS

(Distribution of total assets*)



* Total assets before deduction of bank loans.
 ** Cash, current assets and liabilities excluding bank loan.
 *** EMEA stands for Europe, Middle East and Africa.

INCOME STATEMENT

(Unaudited)

	For the six months ended 30 June 2018			For the six months ended 30 June 2017		
	Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
Gains on investments	–	56,845	56,845	–	22,830	22,830
Movements in unrealised gains on investments	–	31,176	31,176	–	81,809	81,809
Currency gains/(losses)	–	1,332	1,332	–	(2,255)	(2,255)
Income	5,855	–	5,855	5,649	–	5,649
Investment management fee – note 3	(4,998)	–	(4,998)	(4,242)	–	(4,242)
Other administrative expenses	(325)	(4)	(329)	(240)	(1)	(241)
Profit before finance costs and taxation	532	89,349	89,881	1,167	102,383	103,550
Finance costs of borrowings	(85)	–	(85)	(259)	–	(259)
Profit before taxation	447	89,349	89,796	908	102,383	103,291
Tax	(184)	–	(184)	(193)	–	(193)
Profit after taxation	263	89,349	89,612	715	102,383	103,098
Profit per ordinary share – note 4	0.38p	127.76p	128.14p	0.99p	142.14p	143.13p
Weighted average number of ordinary shares in issue during each period	69,930,886			72,031,127		

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

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

BALANCE SHEET

(Unaudited)

	As at 30 June 2018 (unaudited) £'000	As at 31 December 2017 (audited) £'000
Fixed assets		
Investments held at fair value through profit or loss	973,637	925,541
Current assets		
Cash and cash equivalents	66,248	41,870
Other receivables	8,816	1,682
	75,064	43,552
Current liabilities		
Other payables	(1,936)	(2,443)
Net current assets	73,128	41,109
TOTAL NET ASSETS	1,046,765	966,650
Capital and reserves		
Called up share capital	17,371	17,577
Share premium	73,738	73,738
Capital redemption reserve	4,581	4,375
Capital reserve	949,651	869,799
Revenue reserve	1,424	1,161
SHAREHOLDERS' FUNDS	1,046,765	966,650
NET ASSET VALUE PER ORDINARY SHARE (including current year income)	1,506.45p	1,374.88p
NET ASSET VALUE PER ORDINARY SHARE (excluding current year income)	1,506.07p	1,374.20p
Ordinary shares in issue	69,485,583	70,307,785

STATEMENT OF CHANGES IN EQUITY

(Unaudited)

FOR THE SIX MONTHS ENDED 30 JUNE 2018

	Called up share capital £'000	Share premium £'000	Capital redemption reserve £'000	Capital reserve £'000	Revenue reserve £'000	Shareholders' funds £'000
Shareholders' funds at 1 January 2018	17,577	73,738	4,375	869,799	1,161	966,650
Profit after taxation	–	–	–	89,349	263	89,612
Shares bought back – note 8	(206)	–	206	(9,497)	–	(9,497)
Shareholders' funds at 30 June 2018	17,371	73,738	4,581	949,651	1,424	1,046,765

FOR THE SIX MONTHS ENDED 30 JUNE 2017

	Called up share capital £'000	Share premium £'000	Capital redemption reserve £'000	Capital reserve £'000	Revenue reserve £'000	Shareholders' funds £'000
Shareholders' funds at 1 January 2017	18,266	73,738	3,686	695,049	675	791,414
Profit after taxation	–	–	–	102,383	715	103,098
Shares bought back – note 8	(374)	–	374	(13,882)	–	(13,882)
Shareholders' funds at 30 June 2017	17,892	73,738	4,060	783,550	1,390	880,630

NOTES TO THE CONDENSED FINANCIAL STATEMENTS

(Unaudited)

1. FINANCIAL STATEMENTS

The condensed financial statements for the six months to 30 June 2018 within the Half-yearly financial report comprise the statements set out on pages 7 to 9 together with the related notes on pages 10 to 12. The condensed financial statements do not constitute statutory accounts as defined in sections 434 to 436 of the Companies Act 2006 and have been neither audited nor reviewed by the Company's auditors. Financial information in relation to the year ended 31 December 2017 has been extracted from the statutory accounts which have been filed with the Registrar of Companies. The auditors' report on those accounts was unqualified and did not contain a statement under section 498 (2) or (3) of the Companies Act 2006.

The Company's assets, the majority of which are investments in quoted securities, exceed its liabilities significantly. All borrowings require the prior approval of the board. Gearing levels and compliance with loan covenants are reviewed by the board on a regular basis. In accordance with the Company's articles of association, shareholders have the right to vote on the continuation of the Company every three years with the next vote being in April 2019. Accordingly, the financial statements have been prepared on the going concern basis as it is the directors' opinion that the Company will continue in operational existence for the foreseeable future.

2. ACCOUNTING POLICIES

The condensed financial statements have been prepared in accordance with applicable United Kingdom Accounting Standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland, FRS 104 Interim Financial Reporting and the Statement of Recommended Practice Financial Statements of Investment Trust Companies and Venture Capital Trusts, issued by the Association of Investment Companies in November 2014, as amended in January 2017.

The accounting policies applied for the condensed financial statements are as set out in the Company's annual report and financial statements for the year ended 31 December 2017.

3. INVESTMENT MANAGEMENT FEE

Herald Investment Management Limited is appointed investment manager under a management agreement which is terminable on 12 months' notice. Its annual remuneration is 1.0% of the Company's net asset value based on middle market prices, calculated on a monthly basis payable in arrears. The management fee is levied on all assets except the holding in Herald Ventures II Limited Partnership managed by Herald Investment Management Limited.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS CONTINUED (Unaudited)

4. NET RETURN PER ORDINARY SHARE

	Six months ended 30 June 2018 £'000	Six months ended 30 June 2017 £'000
Revenue profit after taxation	263	715
Capital profit after taxation	89,349	102,383
Total net return	89,612	103,098
Weighted average number of ordinary shares	69,930,886	72,031,127

Net return per ordinary share is based on the above totals of revenue and capital and the weighted average number of ordinary shares in issue during each period.

There are no dilutive or potentially dilutive shares in issue.

5. DIVIDENDS

In accordance with FRS 102 section 32 'Events After the End of the Reporting Period', the final dividend payable on ordinary shares is recognised as a liability when approved by shareholders. Interim dividends are recognised only when paid.

No dividends were paid for the year ended 31 December 2017 (2016: same), nor declared for the interim (2017: same).

6. BORROWINGS

The Company had a sterling loan facility of £25 million which was repaid in full on 29 December 2017 and has a £25 million multi-currency revolving credit facility maturing 31 December 2019.

At the period end no drawings had been made.

7. FINANCIAL INSTRUMENTS

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

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

The three levels set out in FRS 102 are as follows:

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

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

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

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

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

	As at 30 June 2018		As at 31 December 2017	
	Assets £'000	Liabilities £'000	Assets £'000	Liabilities £'000
Level 1	1,033,052	(1,936)	956,214	(2,443)
Level 3	15,649	–	12,879	–
Total net assets	1,048,701	(1,936)	969,093	(2,443)

The fair value of listed security investments is bid value. Investments on the Alternative Investment Market are included at their bid value. The fair value of unlisted investments uses valuation techniques determined by the directors on the basis of latest information in line with the relevant principles of the International Private Equity and Venture Capital Valuation Guidelines.

8. SHARE CAPITAL

At the AGM held on 19 April 2018 the Company's authority to buy back up to 14.99% of its issued share capital at that date was renewed. In the six months to 30 June 2018 a total of 822,202 (30 June 2017 – 1,494,919) ordinary shares of 25p each were bought back at a total cost of £9,496,743 (30 June 2017 – £13,881,514). At 30 June 2018 the Company had authority to buy back a further 9,593,686 ordinary shares.

9. FIXED ASSET INVESTMENTS

During the period, cost of purchases amounted to £65,029,000 (30 June 2017 – £61,924,000) and proceeds of sales amounted to £104,931,000 (30 June 2017 – £60,752,000).

	Six months ended 30 June 2018 £'000	Six months ended 30 June 2017 £'000
Transaction costs		
Commission costs:		
Purchases	115	192
Sales	179	195
Total commission costs	294	387
Custody transaction costs	4	1
Other transaction costs	21	46
Total transaction costs	319	434

FURTHER SHAREHOLDER INFORMATION

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The Bank of New York Mellon

COMPANY NUMBER

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applicable international rate; lines are
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