

A large, stylized oak leaf graphic in a lighter shade of blue, positioned on the left side of the page. The leaf has several lobes and a central vein, extending from the top left towards the bottom center.

# FAIR OAKS INCOME LIMITED

(FORMERLY FAIR OAKS INCOME FUND LIMITED)

ANNUAL REPORT AND AUDITED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2016



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# Highlights

- NAV up 26.4% in 2016 on a total return basis (with dividends reinvested), outperforming the Credit Suisse Leveraged Loan Index (+9.9%), the Credit Suisse High Yield Index (+18.4%) and the JP Morgan B rated CLO index (+23.7%).
- Market capitalisation of US\$302 million as at 30 December 2016.
- The Company's shares traded at an average premium to NAV of 2.6% in 2016.
- The Company declared 13.45 US cents per ordinary share in dividends in 2016, equivalent to a 13.9% dividend yield on the closing mid-share price on 30 December 2016. Cumulative dividend of 27.6 US cents per share since inception.
- US\$9.3 million of principal returned to shareholders in 2016.
- On 29 March 2017, Fair Oaks Income Fund Limited changed its name to Fair Oaks Income Limited.
- On 3 April 2017, the First Placing and Offer raised US\$68.85 million.
- On 5 April 2017, 263.51 million 2017 shares, 47.43 million 2014 shares and 68.85 million C shares were admitted to the Specialist Fund Segment of the Main Market of the London Stock Exchange.

<b>Financial Highlights</b>	<b>31 December 2016</b>	<b>31 December 2015</b>
Total Net Assets	US\$311,683,895	US\$277,591,973
Net Asset Value per ordinary share	US\$1.0024	US\$0.8663
Net Asset Value per C share	N/A	US\$0.9191
Ordinary share price at year end	US\$0.9700	US\$0.9500
C share price at year end	N/A	US\$0.9900
(Discount)/premium to Net Asset Value (ordinary shares)	(3.23%)	9.66%
Premium to Net Asset Value (C shares)	N/A	7.71%
Ongoing charges figure*	0.27%	0.49%

\*Total ongoing charges at the Company level only for the year divided by the average NAV for the year.



# Summary Information

## Principal Activity

Fair Oaks Income Limited (formerly Fair Oaks Income Fund Limited) (the "Company" or "FOIF") was registered in Guernsey under the Companies (Guernsey) Law, 2008 on 7 March 2014. The Company's registration number is 58123 and it is regulated by the Guernsey Financial Services Commission as a registered closed-ended collective investment scheme under The Registered Collective Investment Scheme Rules 2015. The Company is listed and began trading on the Specialist Fund Segment (previously Specialist Fund Market) ("SFS") of the London Stock Exchange on 12 June 2014.

The Company is a feeder fund and during the year under review pursued its investment objective and policy by investing in FOIF LP ("the Master Fund"), in which the Company is a limited partner. During prior periods, the only other limited partner was Fair Oaks Founder LP (the "Founding Partner"). During the year ended 31 December 2016, the Master Fund accepted a new limited partner. The new limited partner was drawn down during March 2016 and April 2016. In accordance with the Limited Partnership Agreement dated and restated 15 May 2014 (the "LPA"), the share allocated to the new limited partner was calculated as at the time of drawdown of their commitments by reference to the amount drawn as a percentage of the adjusted Net Asset Value ("NAV") of the Master Fund. The adjusted NAV is the latest available NAV as at the date of drawdown, adjusted for establishment costs. At 31 December 2016, the Company had a 74.13% (31 December 2015: 100%) holding in the Master Fund. The general partner of the Master Fund is Fair Oaks Income Fund (GP) Limited (the "General Partner" or "GP"). Consequently, the Company's investment objective and policy mirror those of the Master Fund.

Fair Oaks Founder LP, a Guernsey limited partnership has been established to act as the Founder Limited Partner of the Master Fund.

## Investment Objective and Policy

The investment objective of the Company is to generate attractive, risk-adjusted returns, principally through income distributions.

The investment policy of the Company is to seek exposure to US and European Collateralised Loan Obligations ("CLOs") or other vehicles and structures which provide exposure to portfolios consisting primarily of US and European floating-rate senior secured loans and which may include non-recourse financing.

If at any time the Company holds any uninvested cash, the Company may also invest on a temporary basis in the following Qualifying Short Term Investments:

- cash or cash equivalents;
- government or public securities (as defined in the Financial Conduct Authority ("FCA") Rules);
- money market instruments;
- bonds;
- commercial paper; or
- other debt obligations with banks or other counterparties having a "single A" (or equivalent) or higher credit rating as determined by any internationally recognised rating agency selected by the Board (which may or may not be registered in the EU).

The aggregate amount deposited or invested by the Company with any single bank or other non-government counterparty (including their associates) shall not exceed 20% of the NAV at the time of investment. The Company cannot make any other types of investments without shareholder consent to a change of investment policy by ordinary resolution at a general meeting of the Company.



# Chairman’s Statement

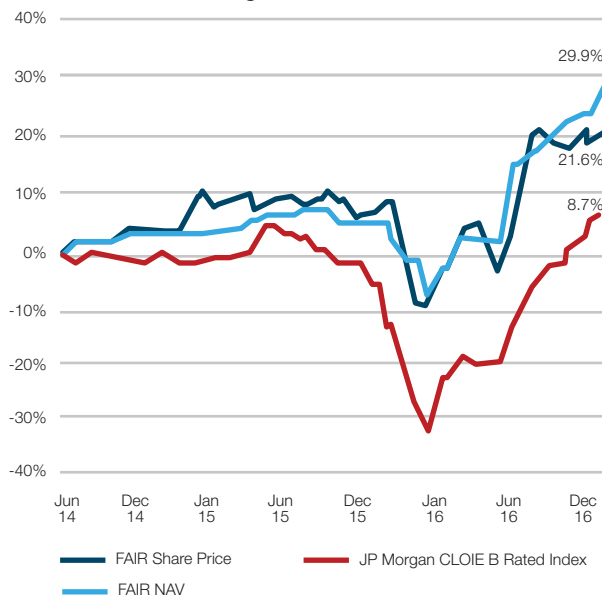
## Introduction

The independent Board of the Company is pleased to present its Annual Report and Financial Statements for the year ended 31 December 2016. The first half of 2016 saw weak credit markets and the outcome of the Brexit referendum which resulted in significant volatility for the Company’s NAV and share price. The second half of 2016, however, saw a significant market recovery which resulted in full year returns for the Credit Suisse Leveraged Loan Index, the Credit Suisse High Yield Index and the JP Morgan B rated CLO index of 9.9%, 18.4% and 23.7% respectively. The Company’s NAV ended the year up 26.4% on a total return basis, that is with dividends reinvested, outperforming all three indices.

The Company’s share price closed at a mid-price of 97.0 US cents on 30 December 2016.

The Company’s shares traded at an average premium to NAV of 2.6% in 2016<sup>1</sup>.

Total return on Fair Oaks Income Limited vs. JP Morgan CLOIE B Rated Index

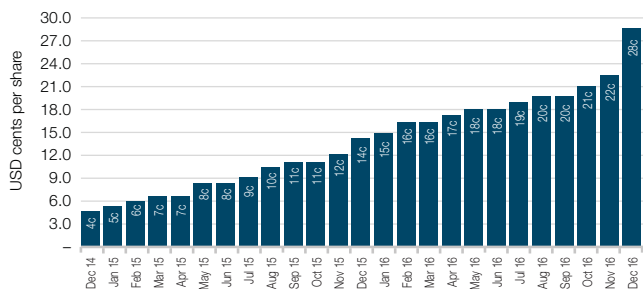


## Cash flow and dividends

The Company declared and paid a 0.70 US cents per ordinary share dividend monthly from January to November and announced a dividend of 5.75 US cents per ordinary share for December, totalling 13.45 US cents per ordinary share in dividends during 2016, equivalent to a 13.9% dividend yield on the closing mid-share price on 30 December 2016.

The Master Fund ended its investment period in June 2016 and, as a result, two principal distributions were received by the Company which were used to fund partial redemptions of shares. A total of US\$9.3 million of principal was returned to shareholders in 2016. The Master Fund received US\$72.4 million worth of cash flows from its investments during 2016, above original expectations of US\$66.2 million.

Total dividends per share since inception



## Material events

On 22 January 2016, the Company announced the conversion ratio for the C Shares issued in August 2015. The net asset values attributable to the ordinary shares and the C shares as at 14 January 2016 were US\$0.8578 per ordinary share and US\$0.9102 per C share respectively. The conversion ratio was 1.0611 ordinary shares for every one C share held at close on the conversion record date of 26 January 2016. Entitlements to new ordinary shares were rounded down to the nearest whole share.

On 16 March 2016, the Directors of the Company announced that Fair Oaks Income Fund (GP) Limited (the “General Partner”) of FOIF LP (the “Master Fund”) had applied to reinvest into the Company’s ordinary shares an amount equivalent to 25% of the advisory and management fees paid to Fair Oaks Capital Limited (the “Investment Adviser”) from 1 December 2015 to 29 February 2016. As a consequence, 215,207 new ordinary shares were issued on 21 March 2016 at US\$0.7682, being the NAV per ordinary share as at 29 February 2016 minus the February dividend to which the new ordinary shares were not entitled.

<sup>1</sup>Average premium of daily share mid-price from Bloomberg over published NAV as at each date.



## Chairman's Statement (continued)

On 4 July 2016, the Company announced that the commitment period of the Master Fund, in which the Company is invested, ended on 12 June 2016. The Company announced that, *inter alia*, to the extent that the Company was to hold surplus realised capital following distributions from the Master Fund, it intended to return such capital to shareholders on a timely basis and in a cost and tax efficient manner.

On 25 August 2016, shareholders approved changes to the rights of the ordinary shares so as to make them redeemable at the option of the Company.

On 14 September 2016, the Master Fund made a US\$5.9 million first principal payment to the Company, equivalent to 1.85 US cents per ordinary share. The Company distributed this to shareholders as a partial redemption of shares on 29 September 2016 (Redemption Date).

On 7 November 2016, the Company announced it was considering proposals under which shareholders would be offered an option (but would not have an obligation) to extend the duration of their investment in the Company through a share class which would retain a pro-rata interest in the Master Fund and reinvest its capital distributions into a new Master Fund. The Company also announced that it was considering its options to raise further equity for the Company through a new C share class which, if issued, would convert into that extended duration share class once substantially invested.

On 15 November 2016, the Master Fund made a US\$3.3 million second principal payment to the Company, equivalent to 1.061 US cents per ordinary share. The Company distributed this to shareholders as a partial redemption of shares on 30 November 2016 (Redemption Date).

### Subsequent events

Further to the event dated 7 November 2016 above and following consultations with shareholders, on 10 January 2017 the Company announced its intention to proceed with the proposals under which shareholders would be offered an option (but would not have an obligation) to extend the duration of their investment, and also with a further equity raise through a C share.

On 9 March 2017, the Company announced proposals which included shareholders being offered an option (but not an obligation) to extend the duration of their investment in the Company and also a further equity raise. On 28 March 2017, the Company announced that 47,428,202 ordinary shares had been elected for re-designation as 2014 shares at the effective date, representing 15.3% of the ordinary shares currently in issue and that 263,510,368 ordinary shares would be re-designated as 2017 shares, representing the balance of 84.7% of the ordinary shares in issue.

On 29 March 2017, the Board of the Company announced that, at the Extraordinary General Meeting of the Company, the following proposed resolutions were approved by shareholders:

- that the articles of incorporation be approved and adopted
- that on the effective date all ordinary shares of no par value each in the capital of the Company ("ordinary shares") be re-designated on a one-for-one basis as "2017 ordinary shares" of no par value each in the capital of the Company ("2017 shares") pursuant to the proposals set out in the Circular, except that where and to the extent that a shareholder has made a valid election for the re-designation of some or all of their ordinary shares as "2014 ordinary shares" of no par value each in the capital of the Company ("2014 shares") pursuant to an election contemplated under the Circular and in the case of the ordinary shares held by an excluded shareholder (as defined in the Circular), such ordinary shares be instead re-designated on a one-for-one basis as 2014 shares.
- that the Directors of the Company be empowered to issue shares in the Company or rights to subscribe for such shares in the Company for cash as if the pre-emption provisions contained under Article 6.2 did not apply to any such issues provided that this power shall be limited to the issue of the below-mentioned shares or of rights to subscribe for the below-mentioned shares:
  - up to a maximum number of 200 million C shares of no par value in the capital of the Company ("C shares") under the Issue;
  - up to a maximum number of 250 million C shares under the Placing Programme; and
  - up to such number of 2017 shares under the Placing Programme as represents 10 per cent. of the 2017 shares then in issue following the effective date, and
- the name of the Company be changed to Fair Oaks Income Limited.

On 3 April 2017, the Company announced the completion of a US\$68.85 million Placing and Offer for shares. Application was made for 68,850,000 C Shares to be admitted to the Specialist Fund Segment of the Main Market of the London Stock Exchange. Following Admission on 5 April 2017, the Company has 263,510,368 2017 shares, 47,428,202 2014 shares and 68,850,000 C shares in issue.

### Professor Claudio Albanese

Chairman

5 April 2017



# Investment Adviser's Report

The Investment Adviser believed that the CLO market dislocation in the first half of 2016 was not due to fundamental changes in the credit markets, but that it was the result of temporary technical factors. The Master Fund took advantage of the opportunity in the secondary market acquiring US\$144 million par of CLO mezzanine securities, at a weighted average target return to expected call date of 25.4%.

During the course of 2016, the strength in broader capital markets, low loan market defaults and constructive technical factors supported a strong recovery in the CLO market. The Company estimates that, as at the end of December 2016, the weighted average target return to expected call date of the mezzanine positions acquired in early 2016 had tightened to 19.8%.

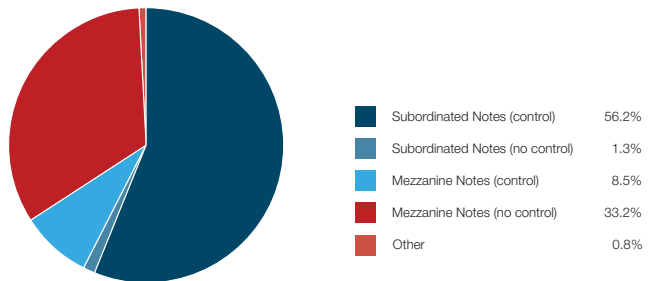
The fundamental performance of the Master Fund control equity positions continued to be strong with actual default losses in the underlying CLO portfolios well below original base case assumptions. The Master Fund's CLO equity portfolio had experienced cumulative defaults of 0.1%<sup>2</sup> as at 30 December 2016, significantly below the 1.2% expected cumulative defaults (as per the underlying investments' base case assumptions) and the US loan market 2016 issuer-weighted default rate of 2.1%. Exposure to energy and metals/mining issuers in the Master Fund's CLO equity positions was limited to 1.9% and 0.8% respectively. The average price for the loans in the Master Fund's portfolio was 99.1 US cents compared with an average price of 97.2 US cents for the Credit Suisse Leveraged Loan Index.

The Master Fund completed the refinancing of AMMC CLO 15 on 9 December 2016. The cost of AAA-rated financing for this investment was reduced from Libor+1.53% to Libor+1.35% while the cost of AA rated and A rated financing was reduced from Libor+2.45% to Libor+1.90% and from Libor+3.46% to Libor+2.80% respectively. The weighted average cost of AAA-A financing decreased by an estimated 28 bps or US\$1.14 million per year. The reduction in the cost of CLO liabilities (net of refinancing expenses) resulted in an increase in the estimated future return on this investment by over 2.0%. The Master Fund completed the refinancing of Allegro CLO II, Arrowpoint 2014-3 and the reset of Harvest VII, in early 2017. The Company continues to monitor closely the potential for refinancing further CLO investments in the short and medium term.

## Portfolio Update

The Company as at 30 December 2016<sup>3</sup>, via its investment in the Master Fund, had exposure to 904 issuers across 41 CLOs managed by 22 managers. Control CLO equity positions represented 56.2% of the portfolio. CLO mezzanine debt investments represented an additional 41.7%, composed of 8.5% mezzanine investments in CLOs in which the Master Funds owned a control equity position, and 33.2% where it did not. The remaining 0.8% comprised fee notes associated with equity investments.

Seniority (% NAV)



## Bank Loan Market Overview

The Credit Suisse Leverage Loan Index returned 9.9% during 2016. As at 30 December 2016, the US loan market twelve month rolling default rate by number of issuers stood at 2.1%, up from 1.1% as at the end of 2015, though down slightly from October when it stood at 2.4%. The decline in late 2016 was due to several commodity-exposed issuers which defaulted in 2015 being removed from the relevant twelve month period. JP Morgan expects default rates in the US loan market to remain relatively flat at 2% through 2017<sup>4</sup>, with a shift away from energy and commodity-related defaults.

The Investment Adviser continues to believe that increased bank loan price volatility is now a structural feature of the market due primarily to technical factors such as reduced dealer inventories and the importance of retail funds as the marginal buyer or seller in the loan market. The loan market's reaction to political and other macro events can benefit CLOs, as their closed-ended nature and lack of mark-to-market requirements allow them to take advantage of dips in loan prices.

<sup>2</sup>Cumulative default rate defined as payment defaults on loans in CLOs in which the Master Fund holds an equity interest, weighted by the Master Fund's percentage equity holding.

<sup>3</sup>Based on the underlying loans in CLOs in which the Master Fund holds equity.

<sup>4</sup>J.P Morgan "2017 High Yield Bond and Leveraged Loan Outlook", 2 December 2016.

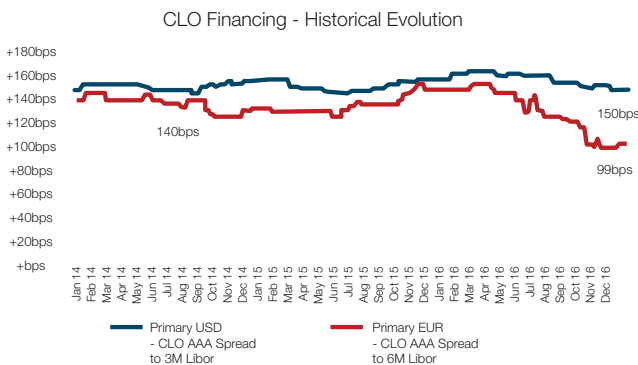


## Investment Adviser’s Report (continued)

### CLO Market Overview

2016 new issue volume in the United States reached US\$72.4 billion, down from US\$99.1 billion in 2015 but ahead of expectations for the year. In Europe, new issue volume reached €18.0 billion, up from 2015’s €13.5 billion<sup>5</sup> as European CLO liabilities tightened towards the end of 2016, improving the arbitrage for CLO equity investors.

US CLO equity arbitrage started to become attractive again in late 2016 as the cost of CLO AAA liabilities tightened. Anecdotal evidence points at an increase in the AAA investor base, driven primarily by Asian institutions. US and European CLO AAA spreads tightened from 160 bps and 150 bps respectively<sup>6</sup> at the beginning of the year to 150 bps and 99 bps at the end of December. As at the end of February 2017, US and European CLO AAA spreads have tightened further to 133 bps and 92 bps respectively<sup>6</sup>.



Source: JP Morgan

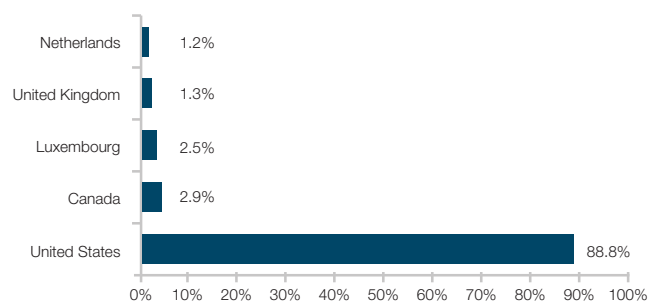
The second half of 2016 also saw an upward trend in CLO refinancing activity, bringing 2016 global refinancing volumes to US\$43.6 billion (US\$39.4 billion US, US\$4.2 billion Europe)<sup>6</sup>.

Risk retention regulations officially came into effect in the United States on 24 December 2016. We believe that the impact in the market will be marginal given the availability of solutions which minimise the capital required to be provided by the CLO manager to comply with the 5% retention requirement.

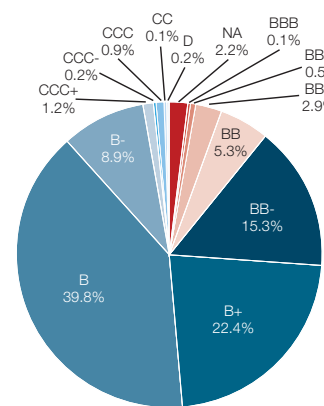
### Risk management

The Master Fund benefits from an experienced and dedicated team of research analysts who continue to monitor the underlying portfolios of the CLO investments. Close relationships with the CLO managers help to monitor and forecast the performance of the underlying portfolios of the CLO investments, as well as serving as ongoing due diligence of the CLO managers.

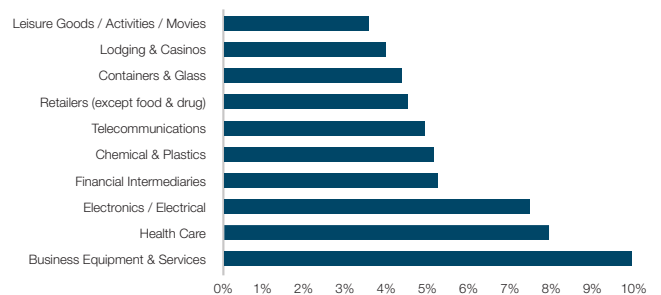
Geographical and Currency Breakdown (based on par value of loans in gross portfolio)



Rating Breakdown (based on par value of loans in gross portfolio)



Industry Diversification (Top 10)\*



Source: CLO trustee reports. Based on the Master Fund’s equity positions and weighted by CLO size and Master Fund’s equity ownership percentage

\*This forms an integral part of the financial statements.

<sup>5</sup>JP Morgan Research.

<sup>6</sup>JP Morgan Research. Primary USD CLO AAA spreads to 3M Libor. Primary EUR CLO AA spread to 6M Euribor.





## Investment Adviser's Report (continued)

### **Outlook**

The Investment Adviser believes that the Master Fund's CLO investments are well positioned to continue to generate attractive returns, given the quality of the underlying portfolios and the continuous active monitoring and management of the underlying credit risk.

The Master Fund will also continue to benefit from the optionality inherent in the funding of its control CLO equity investments. We expect to refinance the CLO liabilities of additional CLO positions, increasing the future cash distributions to the CLO equity.

We further expect the "tactical" mezzanine investments to continue to perform strongly as we believe that the weighted average target return as at the end of 2016 (19.8%) still represents a very attractive risk-reward proposition in the current market environment.

### **Fair Oaks Capital Limited**

5 April 2017





## Board of Directors

The Directors of the Company, all of whom are non-executive and independent, are listed as follows:

**Professor Claudio Albanese** (Chairman) (age 54) is the Head of Analytics at IMEX Synchronised Risk and Honorary Professor of Finance at CASS School of Business, London (since Autumn 2008). He received a PhD in Theoretical Physics from ETH Zurich in 1988. He has held faculty positions at numerous academic institutions including ETH Zurich, UCLA, the Courant Institute at NYU, and Princeton University. In 1994 he joined the University of Toronto as Associate Professor of Mathematical Physics and in that year he redirected his career towards Mathematical Finance. In 1998 he spent one year at Morgan Stanley at the credit derivatives trading desk. In 2004 he joined Imperial College London as Professor of Mathematical Finance. Claudio consults for several banks, financial service organisations and hardware manufacturers, speaks at numerous conferences and has published over 50 articles in academic and professional journals. Claudio funded Global Valuation Limited, a software firm dedicated to the simulation of banks' OTC portfolios and XVA metrics. Claudio was non-executive director at Carador Income Fund Plc from 2006 to 2013. Claudio is a UK resident.

**Jonathan (Jon) Bridel** (Chairman of the Audit Committee) (age 52) is currently a non-executive chairman or director of various listed and unlisted investment funds and private equity investment managers. Listings include the premium segment of the Official List of the UK Listing Authority and the Specialist Fund Segment of the London Stock Exchange. He was until 2011 Managing Director of Royal Bank of Canada's investment businesses in Guernsey and Jersey. This role had a strong focus on corporate governance, oversight, regulatory and technical matters and risk management. After qualifying as a Chartered Accountant in 1987, Jon worked with Price Waterhouse Corporate Finance in London and subsequently served in a number of senior management positions in Australia and Guernsey in corporate and offshore banking and specialised in credit. He was also chief financial officer of two private multi-national businesses, one of which raised private equity. He holds qualifications from the Institute of Chartered Accountants in England and Wales where he is a Fellow, the Chartered Institute of Marketing and the Australian Institute of Company Directors. He graduated with an MBA from Durham University in 1988. Jon is a chartered marketer and a member of the Chartered Institute of Marketing, the Institute of Directors and is a chartered fellow of the Chartered Institute for Securities and Investment. Jon is a Guernsey resident.

**Nigel Ward** (Chairman of the Risk Committee) (age 60) has over 40 years' experience in international investment markets, credit and risk analysis, portfolio management, corporate and retail banking, corporate governance, compliance and the managed funds industry gained at NatWest, TSB Bank, Baring Asset Management and Bank Sarasin. He is currently an independent non-executive chairman or director on the board of several investment funds and companies, including London and CISE listings, with investment mandate experience ranging across private equity, distressed debt, European SME private debt, ground rents, agricultural land, student accommodation, commodities, equity income and UK activist equity. Nigel was a founding Commissioner of the Guernsey Police Complaints Commission, and is an Associate of the Institute of Financial Services, a member of the Institute of Directors and holder of the IoD Diploma in Company Direction. Nigel is a Guernsey resident.



# Disclosure of Directorships in Public Companies Listed on Recognised Stock Exchanges

The following summarises the Directors' directorships in other public companies:

<b>Company Name</b>	<b>Stock Exchange</b>
<b>Claudio Albanese</b> None	
<b>Jon Bridel</b> Alcentra European Floating Rate Income Fund Limited DP Aircraft 1 Limited Funding Circle SME Income Fund Sequoia Economic Infrastructure Income Fund Limited Starwood European Real Estate Finance Limited The Renewables Infrastructure Group Limited	London Stock Exchange – Main Market London Stock Exchange – SFS London Stock Exchange – Main Market London Stock Exchange – Main Market London Stock Exchange – Main Market London Stock Exchange – Main Market
<b>Nigel Ward</b> Acorn Income Fund Limited Braemar Group PCC Limited Crystal Amber Fund Limited Emerging Manager PCC Limited Hadrian's Wall Secured Investments Limited	London Stock Exchange – Main Market The International Stock Exchange London Stock Exchange – AIM The International Stock Exchange London Stock Exchange – Main Market



# Directors' Report

The Directors of Fair Oaks Income Limited (formerly Fair Oaks Income Fund Limited) (the "Company") are pleased to submit their Annual Report and the Audited Financial Statements (the "Financial Statements") for the year ended 31 December 2016. In the opinion of the Directors, the Annual Report and Audited Financial Statements are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's performance, business model and strategy.

## The Company

The Company was incorporated and registered in Guernsey on 7 March 2014 under the Companies (Guernsey) Law, 2008. The Company's registration number is 58123 and it is regulated by the Guernsey Financial Services Commission ("GFSC") as a registered closed-ended collective investment scheme. The ordinary shares were listed on the SFS of the London Stock Exchange ("LSE") on 12 June 2014.

## Going Concern

The Company has been incorporated with an unlimited life. On or before 31 May 2019, being the planned end date of the Master Fund, an ordinary resolution will be proposed by the Board to shareholders that the Company continues as a registered closed-ended collective investment scheme ("Continuation Resolution"). If the Continuation Resolution is passed by shareholders, a further Continuation Resolution will be proposed on the nearest Business Day falling every two years thereafter. If the Continuation Resolution is not passed, the Board shall draw up proposals for the voluntary liquidation of the Company.

After a review of the Company's holdings in cash and cash equivalents, investments and a consideration of the income deriving from those investments the Directors believe that it is appropriate to adopt the going concern basis in preparing the Financial Statements as the Company has adequate financial resources to meet its liabilities as they fall due.

## Risks and uncertainties

In respect to the Company's system of internal controls and reviewing its effectiveness, the Directors:

- are satisfied 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; and
- have reviewed the effectiveness of the risk management and internal control systems including material financial, operational and compliance controls (including those relating to the financial reporting process) and no significant failings or weaknesses were identified.

The Risk Committee reviews the Company's overall risks at least four times a year and monitors the risk control activity designed to mitigate these risks.

The risks associated with the Company include:

- **Operational risk** - The Board is ultimately responsible for all operational facets of performance including cash management, asset management, regulatory and listing obligations. The Company has no employees and so enters into a series of contracts/legal agreements with a series of service providers to ensure that both operational performance and regulatory obligations are met. The Board performs on-going internal monitoring of operational processes and controls and receives regular reports from the administrators of the Company, along with a report from the Auditors.
- **Investment risk** - The Risk Committee formally monitors the investment performance of the Company four times a year, when the Investment Adviser reports on the performance of the Company's portfolio at the Board meetings. The Investment Adviser carries out extensive due diligence on the Master Fund's underlying investments and monitors performance regularly. The investment guidelines and restrictions, as detailed in the prospectus of the Company, ensures adequate diversification of the Master Fund's underlying investments is regularly monitored by the Investment Adviser.
- **Regulatory risk** - The Company is required to comply with the Prospectus Rules, the Disclosure and Transparency Rules and the Market Abuse Directive (as implemented in the UK through Financial Services and Markets Authority). Any failure to comply could lead to criminal or civil proceedings. The Investment Adviser and Administrator monitor compliance with regulatory requirements and the Administrator presents a report at quarterly Board meetings.
- **Financial risk** - The financial risks faced by the Company, including market, credit and liquidity risk, where appropriate, are set out in note 5. These risks and the controls in place to mitigate these risks are reviewed at each Risk Committee meeting.



## Directors' Report (continued)

### Viability Statement

The Directors have conducted a robust assessment of the viability of the Company over a three year period to May 2020, taking account of the Company's current position and the potential impact of the principal risks documented above.

In making this statement, the Directors have considered the resilience of the Company, taking into account its current position, the principal risks facing the Company in severe but plausible scenarios and the effectiveness of any mitigating actions. This assessment has considered the potential impacts of these risks on the business model, future performance, solvency and liquidity over the period.

The Directors have determined that the three year period to May 2020 is an appropriate period over which to provide its viability statement as this is a reasonable period of which risks relating to the asset class should be considered. On 10 January 2017, the Company announced that it intended to implement proposals which included shareholders being offered an option (but not obligation) to extend the duration of their investment and also a further equity raise. The purpose of the proposal is to allow those shareholders who wish to extend the life of their investment in the Company beyond the planned end date of the Master Fund, to be able to do so by having their ordinary shares re-designated as 2017 shares, with such 2017 shares effectively investing in and having exposure to a new master fund ("Master Fund II"), which will have a planned end date of June 2024 and an investment objective and policy substantially similar to that of the Master Fund. The General Partner will act as the general partner of Master Fund II as well as the Master Fund.

In making their assessment, factors taken into consideration by the Directors included the Company's NAV, net income, capital repayments and resulting cash flows and dividend cover over the period. These metrics were subjected to stress tests which involved flexing a number of main assumptions underlying the forecast and default rates modestly higher than the five year average. Where appropriate, this analysis was carried out to evaluate the potential impact of the Company's principal risks actually occurring, primarily, severe changes to macro economic conditions, increased defaults, deterioration in underlying credit ratings and downgrading or illiquidity of non-investment grade loans.

Based on this assessment, the Directors 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 to May 2020.

### Results and Dividends

The results for the year are shown in the Statement of Comprehensive Income on page 24.

The Directors declared dividends of US\$24,492,044 during 2016 followed by an additional dividend declaration of US\$18,055,284, declared on 4 January 2017 in relation to the year ended 31 December 2016 (31 December 2015: Ordinary shareholders: US\$24,642,883, C shareholders: US\$2,396,372). Further details of dividends declared or paid are detailed in note 4.

The Board paid or declared dividends to shareholders representing an amount in aggregate at least equal to the gross income from investments, which are received from the Master Fund in the relevant financial period attributable to the Company's investment in the Master Fund, and Qualifying Short Term Investments less expenses of the Company.

### Independent Auditor

KPMG Channel Islands Limited were appointed on 12 May 2014 and served as Auditor during the financial year. A resolution to re-appoint KPMG Channel Islands Limited as Auditor will be put to the forthcoming Annual General Meeting ("AGM").

### Investment Adviser

The Directors are responsible for the determination of the Company's investment policy and have overall responsibility for the Company's activities. The Company has, however, entered into an Investment Advisory Agreement with Fair Oaks Capital Limited (the "Investment Adviser") under which the Investment Adviser has been appointed to provide investment advisory services, which include analysing the progress of all assets and investments of the Company and advising the Company on liquidity and working capital retention issues, subject to the overriding supervision of the Directors.

The Directors consider that the interests of shareholders, as a whole, are best served by the continued appointment of the Investment Adviser to achieve the Company's investment objectives. A summary of these terms, including the investment advisory fee and notice of termination period, is set out in note 8 of the Financial Statements.



## Directors' Report (continued)

### Custody Arrangements

The Company's assets, excluding the investment into the Master Fund, are held in custody by BNP Paribas Securities Services S.C.A., Guernsey Branch (the "Custodian"), pursuant to an agreement dated 15 December 2015. A summary of the terms, including fees and notice of termination period, is set out in note 8 of the Financial Statements.

The Company's assets, excluding the investment into the Master Fund, are registered in the name of the Custodian in each case within a separate account designation and may not be appropriated by the Custodian for its own account.

The Board conducts an annual review of the custody arrangements as part of its general internal control review. The Board also monitors the credit rating of the Custodian, to ensure the financial stability of the Custodian is being maintained to acceptable levels. As at 31 December 2016, the credit rating of the Custodian was A1 as rated by Moody's (31 December 2015: Aa1) and A by Standard & Poor's (31 December 2015: AA+).

### Directors and Directors' Interests

The Directors, all of whom are independent and non-executive, are listed on page 7.

None of the Directors has a service contract with the Company and no such contracts are proposed. Each independent non-executive Director is entitled to a basic fee of £37,000 each per annum.

The Directors had the following interests in the Company at 31 December 2016 and 31 December 2015, held either directly or beneficially:

Name	31 December 2016		31 December 2015	
	No. of ordinary shares	Percentage	No. of ordinary shares	Percentage
Claudio Albanese (Chairman)	9,697	0.01%	10,000	0.01%
Jon Bridel	9,697	0.01%	10,000	0.01%
Nigel Ward	19,393	0.01%	20,000	0.02%

### Substantial Shareholdings

As at 7 March 2017, the Company had the following shareholdings in excess of 5% of the issued share capital:

Name	No. of ordinary shares	Percentage
Old Mutual Global Investors	53,199,414	17.11%
Coller Investment Management	33,258,370	10.70%
Seven Investment Management	27,872,611	8.96%
Smith & Williamson Holdings	19,508,264	6.27%
Merseyside Pension Fund	15,776,008	5.07%

### Related Parties

Details of transactions with related parties are disclosed in note 8 to these Financial Statements.

### Listing Requirements

Throughout the period, since being admitted to the SFS of the London Stock Exchange, the Company has complied with the Prospectus Rules, the Disclosure and Transparency Rules and the Market Abuse Directive (as implemented in the UK through Financial Services and Markets Authority).



## Directors' Report (continued)

### Foreign Account Tax Compliance Act

The Foreign Account Tax Compliance Act ("FATCA") became effective on 1 January 2013. The legislation is aimed at determining the ownership of US assets in foreign accounts and improving US tax compliance with respect to those assets. On 13 December 2013, the States of Guernsey entered into an intergovernmental agreement ("IGA") with US Treasury, in order to facilitate the requirements under FATCA. The Company registered with the Internal Revenue Service ("IRS") on 21 November 2014 as a Foreign Financial Institution ("FFI").

### United Kingdom-Guernsey Intergovernmental Agreement

On 22 October 2013, the Chief Minister of Guernsey signed an intergovernmental agreement with the United Kingdom ("UK-Guernsey IGA") under which certain disclosure requirements may be imposed in respect of certain shareholders in the Company who are, or are entities that are controlled by one or more, residents of the United Kingdom. The UK-Guernsey IGA is implemented through Guernsey's domestic legislation, in accordance with guidance which came into force with effect from July 2014.

### Common Reporting Standard

The Common Reporting Standard ("CRS"), formerly the Standard for Automatic Exchange of Financial Account Information, became effective on 1 January 2016. CRS is an information standard for the automatic exchange of information developed by the Organisation for Economic Co-operation and Development ("OECD"). CRS is a measure to counter tax evasion and it builds upon other information sharing legislation, such as FATCA, the UK-Guernsey IGA for the Automatic Exchange of Information and the European Union Savings Directive. The first reporting under CRS for Guernsey will be made during 2017.

### Alternative Investment Fund Managers Directive ("AIFMD")

The Company is categorised as a non-EU Alternative Investment Fund (as defined in the AIFMD) ("AIF") and the Board of the Company is a non-EU Alternative Investment Fund Manager ("AIFM") (as defined in the AIFMD) for the purposes of the AIFMD and as such neither it nor the Investment Adviser will be required to seek authorisation under the AIFMD. However, following national transposition of the AIFMD in a given EU member state, the marketing of ordinary shares in AIFs (as defined in the AIFMD) that are established outside the EU (such as the Company) to investors in that EU member state will be prohibited unless certain conditions are met. Certain of these conditions are outside the Company's control as they are dependent on the regulators of the relevant third country and the relevant EU member state entering into regulatory co-operation agreements with one another.

The Directors have appointed the Risk Committee to manage the relevant disclosures to be made to investors and the necessary regulators. On 18 February 2015, the FCA confirmed that the Company was eligible to be marketed via the FCA's National Private Placement Regime and the Company complied with Article 22 and 23 of the AIFMD for the year ended 31 December 2016. In January 2017, the Company has been authorised to market in Sweden, Finland and Luxembourg.

There have been no material changes to the Company's Prospectus, other principal documents and operations since the Company disclosed to its investors the matters it is required to disclose to them under Article 23 of AIFMD on 28 May 2015. As the Board of the Company is the AIFM, the details of the Company's remuneration policy for the Directors is outlined on page 19 and accords with the principles established by AIFMD.

### Non-Mainstream Pooled Investments

The Company's ordinary shares are considered as "excluded securities" for the purposes of the FCA Rules regarding the definition and promotion of non-mainstream pooled investments ("NMPI") because the returns to investors holding the Company's ordinary shares are, and are expected to continue to be, predominantly based on the returns from ordinary shares and debentures held indirectly by the Company. The Board therefore believes that independent financial advisers can recommend the Company's ordinary shares to retail investors, although financial advisers should seek their own advice on this issue.



## Directors' Report (continued)

### **Reporting Fund regime**

The Company was accepted into the UK Reporting Fund regime with effect from 7 March 2014. Under this regime, which effectively replaced the UK Distributor Status regime, an offshore investment fund operates by reference to whether it opts into the reporting regime ("Reporting Funds") or not ("Non-reporting Funds").

A UK investor who disposes of an interest in a Reporting Fund should be subject to tax on any gains realised as capital gains rather than income. Such investors will also be subject to income tax on the distributions received from the offshore fund and their share of the excess of the offshore fund's reported income over the distributions made (i.e. they will be subject to income tax on their share of the offshore fund's income regardless of whether this is distributed or not). Shareholders should seek their own professional advice as to the tax consequences of the UK Reporting Fund regime.

By order of the Board

**Jon Bridel**

Director

5 April 2017





# Corporate Governance

## Compliance

The Board has taken note of the Code of Corporate Governance issued by the Guernsey Financial Services Commission ("Guernsey Code"). The Guernsey Code provides a governance framework for GFSC licensed entities, authorised and registered collective investment schemes. Companies reporting in compliance with the UK Corporate Governance Code (the "UK Code") or the Association of Investment Companies Code of Corporate Governance ("AIC Code"), which was published in July 2016, are deemed to satisfy the provisions of the Guernsey Code. The UK Code is available on the Financial Reporting Council website, [www.frc.org.uk](http://www.frc.org.uk).

As a Guernsey incorporated company and under the SFS Rules for companies, it is not a requirement for the Company to comply with the UK Code. However, the Directors place a high degree of importance on ensuring that high standards of corporate governance are maintained and have considered the principles and recommendations of the AIC Code by reference to the AIC Corporate Governance Guide for investment companies ("AIC Guide"). The AIC Code, as explained in the AIC Guide, addresses all the principles set out in the UK Code. The Board considers that reporting against the principles and recommendations of the AIC Code, and by reference to the AIC Guide (which incorporates the Code), will provide better information to shareholders. The AIC code is available on the AIC website, [www.theaic.co.uk](http://www.theaic.co.uk).

For the year ended 31 December 2016, the Company complied substantially with the relevant provisions of the AIC Code and it is the intention of the Board that the Company will comply with those provisions throughout the year ending 31 December 2017, with the exception of the provisions listed below:

- *The appointment of a Senior Independent Director:* Given the size and composition of the Board it is not felt necessary to separate the roles of Chairman and Senior Independent Director. The Board considers that all the independent Directors have different qualities and areas of expertise on which they may lead where issues arise and to whom concerns can be conveyed.
- *Internal audit function:* The Board has reviewed the need for an internal audit function and due to the size of the Company and the delegation of day-to-day operations to regulated service providers, an internal audit function is not considered necessary. The Directors will continue to monitor the systems of internal controls in place in order to provide assurance that they operate as intended.
- *The appointment of Executive Directors:* Due to the broad range of experience of the Board and given the nature of the Company's activity and that the majority of Directors are deemed to be independent under the AIC Code, it is not considered necessary to appoint executive Directors.
- *Chairman of the Company is also the Chairman of the Nomination and Remuneration Committee:* Due to its size and composition by only non-Executive Directors, the Board deemed it appropriate for Mr Albanese to also serve as Chairman of the Company's Nomination and Remuneration Committee. The Nomination and Remuneration Committee takes care to recognise and manage conflicts of interest and, accordingly, no Director is involved in determining their own remuneration. The Board remains satisfied that Mr Albanese possesses the necessary skills and experience to effectively discharge the duties expected from this role. This is going to be reviewed at the next quarterly Board meeting.

## Composition and Independence of Directors

As at 31 December 2016, the Board of Directors comprised three non-executive and independent Directors as set out below. The Company has no executive Directors or any employees. The biographies of the Board are disclosed on page 7.

Claudio Albanese is the Chairman of the Board, the Management Engagement Committee and of the Nomination and Remuneration Committee.

Jon Bridel is the Chairman of the Audit Committee.

Nigel Ward is the Chairman of the Risk Committee.

In considering the independence of the Chairman, the Board has taken note of the provisions of the AIC Code relating to independence and has determined that Claudio Albanese is an Independent Director.



## Corporate Governance (continued)

### **Composition and Independence of Directors** (continued)

Under the terms of their appointment, all non-executive Directors are subject to re-election annually at the Annual General Meeting ("AGM"). At the Annual General Meeting of the Company on 19 May 2016, shareholders re-elected all the Directors of the Company.

Although no formal training is given to Directors by the Company, the Directors are kept up to date on various matters such as Corporate Governance issues through bulletins and training materials provided from time to time by the Company Secretary, the AIC and other professional firms.

The Board receives quarterly reports and meets at least quarterly to review the overall business of the Company and to consider matters specifically reserved for its disposal. At these meetings the Board monitors the investment performance of the Company. The Directors also review the Company's activities every quarter to ensure that it adheres to the Company's investment policy. Additional ad hoc reports are received as required and Directors have access at all times to the advice and services of the Company Secretary, who is responsible for ensuring that the Board procedures are followed and that applicable rules and regulations are complied with.

The Board monitors the level of the share price premium or discount to determine what action is desirable (if any).

The Board and relevant personnel of the Investment Adviser acknowledge and adhere to the Market Abuse Regulation which was implemented on 3 July 2016.

### **Directors' Performance Evaluation**

The Board has established an informal system for the evaluation of its own performance and that of the Company's individual Directors. It considers this to be appropriate having regard to the non-executive role of the Directors and the significant outsourcing of services by the Company to external providers.

The Directors undertake, on an annual basis, an assessment of the effectiveness of the Board particularly in relation to its oversight and monitoring of the performance of the Investment Adviser and other key service providers. The evaluations consider the balance of skills, experience, independence and knowledge of the Company. The Board also evaluates the effectiveness of each of the Directors.

The Chairman also has responsibility for assessing the individual Board members' training and development requirements.

### **Directors' Remuneration**

With effect from 27 August 2015, it is the responsibility of the Nomination and Remuneration Committee to determine and approve the Directors' remuneration, having regard to the level of fees payable to non-executive Directors in the industry generally, the role that individual Directors fulfil in respect of Board and Committee responsibilities and the time committed to the Company's affairs. The Chairman's remuneration is decided separately and is approved by the Board as a whole.

No Director has a service contract with the Company and details of the Directors' remuneration can be found in the Directors' Remuneration Report on page 19.

### **Directors' and Officers' Liability Insurance**

The Company maintains Directors' and Officers' liability insurance on behalf of the Directors in relation to the performance of their duties as Directors.



## Corporate Governance (continued)

### Relations with Shareholders

The Company reports to shareholders twice a year by way of the Interim Report and Unaudited Condensed Financial Statements and the Annual Report and Audited Financial Statements. In addition, NAVs are published monthly and the Investment Adviser publishes monthly reports to shareholders on its website [www.fairoaksincome.com](http://www.fairoaksincome.com).

The Board receives quarterly reports on the shareholder profile of the Company and regular contact with major shareholders is undertaken by the Company's corporate brokers and the executives of the Investment Adviser. Any issues raised by major shareholders are reported to the Board on a regular basis.

The Chairman and individual Directors are willing to meet major shareholders to discuss any particular items of concern regarding the performance of the Company. Members of the Board, including the Chairman and the Audit Committee Chairman, and the Investment Adviser are also available to answer any questions which may be raised by any shareholder at the Company's Annual General Meeting.

### Directors' Meetings and Attendance

The table below shows the attendance at Board, Audit and Risk Committee and Committee meetings during the year. There were four formal Board meetings, four Audit Committee meetings, four Risk Committee meetings, one Management Engagement Committee meeting, one Nomination and Remuneration Committee meeting and five informal Board meetings held during the year ended 31 December 2016.

Name	Board	Audit Committee	Risk Committee	Management Engagement Committee	Nomination & Remuneration Committee
Number of meetings held	9	4	4	1	1
Claudio Albanese (Chairman)	9	4	N/A	1	1
Jon Bridel (Audit Committee Chairman)	9	4	4	1	1
Nigel Ward (Risk Committee Chairman)	9	4	4	1	1

### Board Committees

#### *Audit Committee*

The Audit Committee comprises all Board members, and meets at least three times a year. Jon Bridel is Chairman of the Audit Committee. As all Directors are non-executive whilst also taking into account the size and composition of the Board, it was deemed appropriate that all Board members are also members of the Audit Committee.

The key objectives of the Audit Committee include a review of the Financial Statements to ensure they are prepared to a high standard and comply with all relevant legislation and guidelines, where appropriate, and to maintain an effective relationship with the Auditor. With respect to the Auditor, the Audit Committee's role will include the assessment of their independence, review of the auditor's engagement letter, remuneration and any non-audit services provided by the Auditor. For the principal duties and report of the Audit Committee please refer to the Report of the Audit Committee on page 20.

#### *Management Engagement Committee*

The Management Engagement Committee meets at least once a year. It comprises the entire Board and is chaired by Claudio Albanese. The Management Engagement Committee is responsible for the regular review of the terms of the Investment Advisory Agreement and the performance of the Administrator and the Investment Adviser and also the Company's other service providers.



## Corporate Governance (continued)

### **Board Committees** (continued)

#### *Risk Committee*

The Risk Committee meets at least four times a year. It comprises of Nigel Ward and Jon Bridel and is chaired by Nigel Ward. The principal function of the Risk Committee is to identify, assess, monitor and, where possible, oversee the management of risks to which the Company's investments are exposed, principally to enable the Company to achieve its target investment objective of a total return of 12% to 14% per annum over the planned life of the Company, with regular reporting to the Board. As the Company is an internally managed non-EU AIFM for the purposes of AIFMD, the Directors have appointed the Risk Committee to manage the additional risks faced by the Company as well as the relevant disclosures to be made to investors and the necessary regulators. On 18 February 2015, the FCA confirmed that the Company was eligible to be marketed via the FCA's National Private Placement Regime and the Company complied with Articles 22 and 23 of the AIFMD for the year ended 31 December 2016. In January 2017, the Company has been authorised to market in Sweden, Finland and Luxembourg.

#### *Nomination and Remuneration Committee*

The Nomination and Remuneration Committee meets at least once a year. It comprises the entire Board and is chaired by Claudio Albanese. The Nomination and Remuneration Committee is responsible for reviewing the structure, size and composition of the Board, to consider the succession planning for directors and senior executives, reviewing the leadership needs of the organisation, identifying candidates for appointment to the Board, agreeing a framework for Director remuneration, ensuring management of the Company are appropriately incentivised to enhance performance and reviewing the appropriateness of the remuneration policy on an on-going basis.

### **Internal Control Review and Risk Management System**

The Board of Directors is responsible for putting in place a system of internal controls relevant to the Company and for reviewing the effectiveness of those systems. The review of internal controls is an ongoing process for identifying and evaluating the risks faced by the Company, and which are designed to manage risks rather than eliminate the risk of failure to achieve the Company's objectives.

It is the responsibility of the Board to undertake risk assessment and review of the internal controls in the context of the Company's objectives that cover business strategy, operational, compliance and financial risks facing the Company. These internal controls are implemented by the Company's three main service providers: the Investment Adviser, the Administrator and the Custodian. The Board receives periodic updates from these main service providers at the quarterly Board meetings of the Company. The Board is satisfied that each service provider has effective controls in place to control the risks associated with the services that they are contracted to provide to the Company and are therefore satisfied with the internal controls of the Company.

The Board of Directors considers the arrangements for the provision of Investment Advisory, Administration and Custody services to the Company on an ongoing basis and a formal review is conducted annually. As part of this review the Board considered the quality of the personnel assigned to handle the Company's affairs, the investment process and the results achieved to date.

### **Anti-bribery and Corruption**

The Board acknowledge that the Company's international operations may give rise to possible claims of bribery and corruption. In consideration of The Bribery Act 2010, enacted in the UK, at the date of this report the Board had conducted an assessment of the perceived risks to the Company arising from bribery and corruption to identify aspects of business which may be improved to mitigate such risks. The Board has adopted a zero tolerance policy towards bribery and has reiterated its commitment to carry out business fairly, honestly and openly.



# Statement of Directors' Responsibilities

The Directors are responsible for preparing the Directors' Report and Financial Statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and the Companies (Guernsey) Law, 2008 which give a true and fair view of the state of affairs of the Company and its profit or loss for that period.

International Accounting Standard ("IAS") 1 requires that Financial Statements present fairly for each financial period the Company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the IASB's "Framework for the preparation and presentation of financial statements". In virtually all circumstances a fair presentation will be achieved by compliance with all applicable IFRS.

In preparing the Financial Statements the Directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the Financial Statements; and
- prepare the Financial Statements on the going concern basis, unless it is inappropriate to presume that the Company will continue in business.

The Directors are also responsible for the keeping of proper accounting records which 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 (Guernsey) Law, 2008 and the Listing Rules of the SFS of the London Stock Exchange. They are also responsible for the system of internal controls, safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors confirm that they have complied with these requirements in preparing the Financial Statements.

The Directors are also responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom and Guernsey governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

So far as the Directors are aware, there is no relevant audit information of which the Company's auditor is unaware, having taken all the steps the Directors ought to have taken to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

## Responsibility Statement

Each of the Directors, whose names and functions are listed on page 7, confirms to the best of each person's knowledge and belief:

- the Financial Statements, prepared in accordance with the International Financial Reporting Standards as issued by the IASB, give a true and fair view of the assets, liabilities, financial position and result of the Company, as required by DTR 4.1.12R and are in compliance with the requirements set out in the Companies (Guernsey) Law, 2008; and
- the Annual Report, taken as a whole, is fair, balanced and understandable and 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 they face, as required by DTR 4.1.8R and DTR 4.1.11R.

Signed on behalf of the Board by:

**Jon Bridel**  
Director

5 April 2017



# Directors' Remuneration Report

The Company's policy in regard to Directors' remuneration is to ensure that the Company maintains a competitive fee structure in order to recruit, retain and motivate non-executive Directors of excellent quality in the overall interests of shareholders.

No element of the Directors' remuneration is performance related, nor does any Director have any entitlement to pensions, share options or any long term incentive plans from the Company.

The Company's Articles limit the fees payable to Directors in aggregate to US\$400,000 per annum.

The Directors have received the following remuneration during the year in the form of Directors' fees:

	Per Annum £	For the period from 1 January 2016 to 31 December 2016 Actual £	For the period from 1 January 2015 to 31 December 2015 Actual £
Claudio Albanese (Chairman)	37,000	37,000	33,250
Jon Bridel (Audit Committee Chairman)	37,000	37,000	33,250
Nigel Ward (Risk Committee Chairman)	37,000	37,000	33,250
<b>Total</b>	<b>111,000</b>	<b>111,000</b>	<b>99,750</b>

Each Director is entitled to a fee of £37,000 per annum.

The remuneration policy set out above is the one applied for the years ended 31 December 2016 and 31 December 2015 and is not expected to change in the immediate future.

Directors' and Officers' liability insurance cover is maintained by the Company on behalf of the Directors.

The Directors were appointed as non-executive Directors by letters issued in April and May 2014. Each Director's appointment letter provides that, upon the termination of his appointment, he must resign in writing and all records remain the property of the Company. The Directors' appointments can be terminated in accordance with the Articles and without compensation. The notice period for the removal of Directors is three months as specified in the Director's appointment letter. The Articles provide that the office of director shall be terminated by, among other things: (a) written resignation; (b) unauthorised absences from Board meetings for six months or more; (c) unanimous written request of the other Directors; or (d) an ordinary resolution of the Company.

Under the terms of their appointment, each Director was subject to re-election at the first Annual General Meeting ("AGM") and annually thereafter. At the Annual General Meeting of the Company on 19 May 2016, shareholders re-elected all the Directors for re-election. The Company may terminate the appointment of a Director immediately on serving written notice and no compensation is payable upon termination of office as a director of the Company becoming effective.

The amounts payable to Directors as at 31 December 2016 and 31 December 2015, shown in note 8 related to services as non-executive Directors.

No Director has a service contract with the Company, nor are any such contracts proposed.

Signed on behalf of the Board of Directors on 5 April 2017 by:

**Jon Bridel**

Director



# Report of the Audit Committee

The Company has established an Audit Committee with formally delegated duties and responsibilities within written terms of reference (which are available from the Company's website).

## Chairman and Membership

The Audit Committee is chaired by Jon Bridel, a Chartered Accountant. He and its other members, Claudio Albanese and Nigel Ward, are all independent Directors. Only independent Directors serve on the Audit Committee and members of the Audit Committee have no links with the Company's Auditor and are independent of the Investment Adviser. The membership of the Audit Committee and its terms of reference are kept under review. The relevant qualifications and experience of each member of the Audit Committee is detailed on page 7 of these Financial Statements. The Audit Committee's intention is to meet three times a year in any full year and meets the Auditor during those meetings.

## Duties

The Audit Committee's main role and responsibilities is to provide advice to the Board on whether the Annual Report and Audited Financial Statements, taken as a whole, are fair, balanced and understandable and alongside the Interim Report and Unaudited Condensed Financial Statements provide the information necessary for shareholders to assess the Company's performance, business model and strategy. The Audit Committee gives full consideration and recommendation to the Board for the approval of the contents of the Interim and Annual Financial Statements of the Company, which includes reviewing the Auditor's report.

The other principal duties include to consider the appointment of the Auditor, to discuss and agree with the Auditor the nature and scope of the audit, to keep under review the scope, results and effectiveness of the audit and the independence and objectivity of the Auditor, to review the Auditor's letter of engagement, the Auditor's planning report for the financial year and management letter and to analyse the key procedures adopted by the Company's service providers.

The Audit Committee is responsible for monitoring the financial reporting process and the effectiveness of the Company's internal control and risk management systems as they relate to the financial reporting process. The Audit Committee also focuses particularly on compliance with legal requirements, accounting standards and the relevant Listing Rules and ensuring that an effective system of internal financial and non-financial controls is maintained.

The Audit Committee also reviews, considers and, if thought appropriate, recommends for the purposes of the Company's Financial Statements valuations prepared by the Investment Adviser. These valuations are the most critical element in the Company's Financial Statements and the Audit Committee questions them carefully.

## Financial Reporting and Audit

The Audit Committee has an active involvement and oversight in the preparation of both the Interim and Annual Financial Statements and in doing so is responsible for the identification and monitoring of the principal risks associated with the preparation of the Financial Statements. The principal risks identified in the preparation of these Financial Statements are as follows:

- Valuation of the Master Fund – The Company's investment in the Master Fund had a fair value of US\$291,682,780 as at 31 December 2016 and represents substantially all the net assets of the Company and as such is the biggest factor in relation to the accuracy of the Financial Statements. This investment is valued in accordance with the Accounting Policies set out in note 2 to the Financial Statements. The Financial Statements of the Master Fund for the year ended 31 December 2016 were audited by KPMG Channel Islands Limited ("KPMG") who issued an unqualified audit opinion dated 5 April 2017. The Audit Committee has reviewed the Financial Statements of the Master Fund and the Accounting Policies and determined the Company's fair value of the investment in the Master Fund as at 31 December 2016 is reasonable.

The Audit Committee reviews the Company's accounting policies applied in the preparation of its Annual Financial Statements together with the relevant critical judgements, estimates and assumptions and, upon taking the appropriate advice from the Auditor, determined that these were in compliance with IFRS, as issued by the IASB and were reasonable. The Audit Committee reviewed the materiality levels applied by the Auditor to both the Financial Statements as a whole and to individual items and was satisfied that these materiality levels were appropriate. The Auditor reports to the Audit Committee all material corrected and uncorrected differences. The Auditor explained the results of their audit and that on the basis of their audit work, there were no uncorrected differences proposed that were material in the context of the Financial Statements as a whole.





## Report of the Audit Committee (continued)

### Financial Reporting and Audit (continued)

The Audit Committee also reviews the Company's financial reports as a whole to ensure that such reports appropriately describe the Company's activities and to ensure that all statements contained in such reports are consistent with the Company's financial results and projections. Accordingly, the Audit Committee was able to advise the Board that the Annual Report and Audited Financial Statements are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's performance, business model and strategy.

### External Auditor

The Audit Committee has responsibility for making a recommendation on the appointment, re-appointment and removal of the Auditor. KPMG was appointed as the first Auditor of the Company. During the year, the Audit Committee received and reviewed the audit plan and report from KPMG. It is standard practice for the Auditor to meet privately with the Audit Committee without the Investment Adviser being present at each Audit Committee meeting.

To assess the effectiveness of the Auditor, the Audit Committee will review:

- The Auditor's fulfilment of the agreed audit plan and variations from it;
- The Audit Committee Report from the Auditor highlighting the major issues that arose during the course of the audit; and
- Feedback from the Investment Adviser and Administrator evaluating the performance of the audit team.

Where non-audit services are to be provided to the Company by the Auditor, full consideration of the financial and other implications on the independence of the auditor arising from any such engagement will be considered before proceeding. All non-audit services are pre-approved by the Audit Committee after it is satisfied that relevant safeguards are in place to protect the auditors' objectivity and independence.

To fulfil its responsibility regarding the independence of the Auditors, the Audit Committee considered:

- a report from the Auditor describing its arrangements to identify, report and manage any conflicts of interest; and
- the extent of non-audit services provided by the Auditor.

During the year ended 31 December 2016, KPMG provided non-audit services in the form of advice to the Board on the C share conversion. At the Audit Committee meeting in November 2016, KPMG confirmed that this had not impacted their independence and outlined the reasons for this. These non-audit services comply with the Financial Reporting Council ("FRC") Revised Ethical Standard 2016. The Audit Committee considered this and were satisfied that these non-audit services had no bearing on the independence of the Auditor.

The following table summarises the remuneration paid to KPMG and to other KPMG International member firms for audit and non-audit services during the year ended 31 December 2016 and 31 December 2015, translated into the presentation currency at the exchange rate prevailing at 31 December 2016 and 31 December 2015 respectively.

	<b>For the year ended 31 December 2016 US\$</b>	<b>For the year ended 31 December 2015 US\$</b>
<b>KPMG Channel Islands Limited</b>		
– Annual Audit	80,827	71,248
– Interim review	27,765	22,104
<b>Other KPMG member firms</b>		
– Initial prospectus	9,255	-
– Reporting accountant services – issuance of C shares	-	94,997
– Tax compliance services	-	2,210



## Report of the Audit Committee (continued)

### Internal Controls

As the Company's investment objective is to invest all of its assets into the Master Fund, the Audit Committee, after consultation with the Investment Adviser and Auditor, considers the key risk of misstatement in its Financial Statements to be the valuation of its investment in the Master Fund, but are also mindful of the risk of the override of controls by its two main service providers: the Investment Adviser and Administrator.

The Investment Adviser and Administrator together maintain a system of internal control on which they report to the Board. The Board has reviewed the need for an internal audit function and has decided that the systems and procedures employed by the Investment Adviser and Administrator provide sufficient assurance that a sound system of risk management and internal control, which safeguards shareholders' investment and the Company's assets, is maintained. An internal audit function specific to the Company is therefore considered unnecessary.

The Audit Committee is responsible for reviewing and monitoring the effectiveness of the internal financial control systems and risk management systems on which the Company is reliant. These systems are designed to ensure proper accounting records are maintained, that the financial information on which the business decisions are made and which is issued for publication is reliable, and that the assets of the Company are safeguarded. Such a system of internal financial controls can only provide reasonable and not absolute assurance against misstatement or loss.

In accordance with the guidance published in the 'Turnbull Report' by the FRC, the Audit Committee has reviewed the Company's internal control procedures. These internal controls are implemented by the Investment Adviser and the Administrator. The Audit Committee has performed reviews of the internal financial control systems and risk management systems during the year. The Audit Committee is satisfied with the internal financial control systems of the Company.

On behalf of the Audit Committee

### Jon Bridel

Audit Committee Chairman

5 April 2017

# Independent Auditor's Report to the members of Fair Oaks Income Limited

We have audited the financial statements of Fair Oaks Income Limited (formerly Fair Oaks Income Fund Limited) (the "Company") for the year ended 31 December 2016 which comprise the Statement of Comprehensive Income, the Statement of Changes in Shareholders' Equity, the Statement of Financial Position, the Statement of Cash Flows and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards as issued by the IASB.

This report is made solely to the Company's members, as a body, in accordance with section 262 of the Companies (Guernsey) Law, 2008. 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.

## Respective responsibilities of directors and auditor

As explained more fully in the Statement of Directors' Responsibilities set out on page 18, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

## Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

## Opinion on the financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2016 and of its result for the year then ended;
- are in accordance with International Financial Reporting Standards as issued by the IASB; and
- comply with the Companies (Guernsey) Law, 2008.

## Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies (Guernsey) Law, 2008 requires us to report to you if, in our opinion:

- the Company has not kept proper accounting records; or
- the financial statements are not in agreement with the accounting records; or
- we have not received all the information and explanations, which to the best of our knowledge and belief are necessary for the purpose of our audit.

## Dermot A. Dempsey

For and on behalf of KPMG Channel Islands Limited  
Chartered Accountants and Recognised Auditors, Guernsey

6 April 2017



# Statement of Comprehensive Income

For the year ended 31 December 2016

	Note	1 January 2016 to 31 December 2016 US\$	1 January 2015 to 31 December 2015 US\$
<b>Revenue</b>			
Net gains/(losses) on financial assets at fair value through profit or loss	6	68,504,542	(7,164,483)
Investment income	7	16	6,427
Net foreign exchange loss		(39,677)	(5,745)
<b>Total revenue/(loss)</b>		<b>68,464,881</b>	<b>(7,163,801)</b>
<b>Expenses</b>			
Investment adviser fees	8	107,054	406,676
Audit and interim review fees		97,158	95,794
Administration fees	8	123,094	153,553
Directors' fees and expenses	8	149,216	152,450
Other expenses		303,544	283,255
<b>Total operating expenses</b>		<b>780,066</b>	<b>1,091,728</b>
<b>Profit/(loss) and total comprehensive income/(loss) for the year</b>		<b>67,684,815</b>	<b>(8,255,529)</b>
<b>Basic and diluted earnings/(loss) per ordinary share</b>	10	<b>0.2178</b>	<b>(0.0208)</b>
<b>Basic and diluted loss per C share</b>	10	–	<b>(0.0426)</b>

All items in the above statement are derived from continuing operations.

The accompanying notes on pages 28 to 55 form an integral part of the Financial Statements.



# Statement of Changes in Shareholders' Equity

For the year ended 31 December 2016

	Note	Share capital US\$	Retained earnings US\$	Total US\$
<b>At 1 January 2016</b>		<b>308,213,808</b>	<b>(30,621,835)</b>	<b>277,591,973</b>
Issue of ordinary shares during the year	9	165,322	–	165,322
Total comprehensive income for the year		–	67,684,815	67,684,815
Dividends declared during the year	4	–	(24,492,044)	(24,492,044)
Share redemptions paid during the year	9	(9,266,171)	–	(9,266,171)
<b>At 31 December 2016</b>		<b>299,112,959</b>	<b>12,570,936</b>	<b>311,683,895</b>

	Note	Share capital US\$	Retained earnings US\$	Total US\$
<b>At 1 January 2015</b>		<b>119,542,182</b>	<b>4,672,949</b>	<b>124,215,131</b>
Issue of ordinary shares during the year	9	88,398,626	–	88,398,626
Issue of C shares during the year	9	100,273,000	–	100,273,000
Total comprehensive loss for the year		–	(8,255,529)	(8,255,529)
Dividends declared during the year	4	–	(27,039,255)	(27,039,255)
<b>At 31 December 2015</b>		<b>308,213,808</b>	<b>(30,621,835)</b>	<b>277,591,973</b>

The accompanying notes on pages 28 to 55 form an integral part of the Financial Statements.



# Statement of Financial Position

At 31 December 2016

	Note	31 December 2016 US\$	31 December 2015 US\$
<b>Assets</b>			
Cash and cash equivalents	2	12,200,459	5,401,130
Prepayments		77,057	92,507
Distribution receivable		7,826,914	10,256,219
Financial assets at fair value through profit or loss	6	291,682,780	269,069,087
<b>Total assets</b>		<b>311,787,210</b>	<b>284,818,943</b>
<b>Liabilities</b>			
Other payables	11	103,315	107,889
Dividends payable	4	–	7,119,081
<b>Total liabilities</b>		<b>103,315</b>	<b>7,226,970</b>
<b>Net assets</b>		<b>311,683,895</b>	<b>277,591,973</b>
<b>Equity</b>			
Retained earnings		12,570,936	(30,621,835)
Share capital	9	299,112,959	308,213,808
<b>Total equity</b>		<b>311,683,895</b>	<b>277,591,973</b>
<b>Net asset value per ordinary share</b>		1.0024	0.8663
<b>Net asset value per C share</b>		–	0.9191
<b>Number of ordinary shares</b>	9	<b>310,938,570</b>	<b>212,426,903</b>
<b>Number of C shares</b>	9	–	<b>101,800,000</b>

The Financial Statements on pages 24 to 55 were approved and authorised for issue by the Board of Directors on 5 April 2017 and signed on its behalf by:

**Claudio Albanese**

Chairman

**Jon Bridel**

Director

The accompanying notes on pages 28 to 55 form an integral part of the Financial Statements.



# Statement of Cash Flows

For the year ended 31 December 2016

	Note	1 January 2016 to 31 December 2016 US\$	1 January 2015 to 31 December 2015 US\$
<b>Cash flows from operating activities</b>			
Profit/(loss) for the year		67,684,815	(8,255,529)
Adjustments for:			
Net (gains)/losses on financial assets at fair value through profit or loss	6	(68,504,542)	7,164,483
		<b>(819,727)</b>	<b>(1,091,046)</b>
Decrease/(increase) in prepayments		15,450	(55,265)
(Decrease)/increase in other payables		(4,574)	51,811
Income distributions received from Master Fund		45,553,904	18,503,664
Capital distributions received from Master Fund	6	9,266,250	–
Purchases into Master Fund at cost during the year	6	(6,500,000)	(181,103,099)
Purchases of US Treasury Bills during the year		–	(149,985,186)
Proceeds from sale of US Treasury Bills during the year		–	149,996,969
		<b>47,511,303</b>	<b>(163,682,152)</b>
<b>Cash flows from financing activities</b>			
Ordinary shares issued		165,322	88,398,626
C shares issued	9	–	100,273,000
Dividends paid during the year		(31,611,125)	(19,920,174)
Share redemptions paid during the year	9	(9,266,171)	–
		<b>(40,711,974)</b>	<b>168,751,452</b>
		<b>6,799,329</b>	<b>5,069,300</b>
<b>Net increase in cash and cash equivalents</b>			
		5,401,130	331,830
<b>Cash and cash equivalents at beginning of year</b>			
		<b>12,200,459</b>	<b>5,401,130</b>
<b>Cash and cash equivalents at end of year</b>			

The accompanying notes on pages 28 to 55 form an integral part of the Financial Statements.





# Notes to the Financial Statements

For the year ended 31 December 2016

## 1. GENERAL INFORMATION

The Company was incorporated and registered in Guernsey under the Companies (Guernsey) Law, 2008 on 7 March 2014. The Company's registration number is 58123 and it is regulated by the Guernsey Financial Services Commission as a registered closed-ended collective investment scheme under The Registered Collective Investment Scheme Rules 2015. The Company is listed and began trading on the Specialist Fund Segment (previously Specialist Fund Market) ("SFS") of the London Stock Exchange on 12 June 2014.

The Company makes its investments through FOIF LP (the "Master Fund"), in which the Company is a limited partner. During prior periods, the only other limited partner was Fair Oaks Founder LP (the "Founding Partner"). During the year ended 31 December 2016, the Master Fund accepted a new limited partner. The new limited partner was drawn down during March 2016 and April 2016. In accordance with the Limited Partnership Agreement dated and restated 15 May 2014 (the "LPA") the share allocated to the new limited partner was calculated as at the time of drawdown of their commitments by reference to the amount drawn as a percentage of the adjusted Net Asset Value ("NAV") of the Master Fund. The adjusted NAV is the latest available NAV as at date of drawdown, adjusted for establishment costs. At 31 December 2016, the Company had a 74.13% (31 December 2015: 100%) holding in the Master Fund. The general partner of the Master Fund is Fair Oaks Income Fund GP Limited (the "General Partner or GP"). The Master Fund invests in a portfolio consisting primarily of Collateral Loan Obligations ("CLOs"). The Company may also invest in Qualifying Short Term Investments if at any time the Company holds any uninvested cash.

With effect from 15 May 2014, Fair Oaks Capital Limited (the "Investment Adviser") was appointed as the Investment Adviser.

## 2. SIGNIFICANT ACCOUNTING POLICIES

### Statement of Compliance

The Financial Statements, which give a true and fair view, have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC") and are in compliance with the Companies (Guernsey) Law, 2008 and the Prospectus Rules, the Disclosure and Transparency Rules and the Market Abuse Directive (as implemented in the UK through the Financial Services and Markets Authority).

### Basis of Preparation

The Company's Financial Statements have been prepared on a historical cost basis, except for financial assets measured at fair value through profit or loss.

The preparation of Financial Statements in conformity with IFRS requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the Financial Statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates and judgements are discussed in note 3. The principal accounting policies adopted are set out below.

The Directors believe that the Annual Report and Financial Statements contains all of the information required to enable shareholders and potential investors to make an informed appraisal of the investment activities and profit or loss of the Company for the period to which it relates and does not omit any matter or development of significance.

As explained below, the Company qualifies as an investment entity and is therefore only required under IFRS to prepare individual Financial Statements under IFRS.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES *continued*

#### **New Accounting Standards effective and adopted**

- IFRS 10 (amended), "Consolidated Financial Statements" (amendments effective for periods commencing on or after 1 January 2016);
- IFRS 12 (amended), "Disclosure of Interests in Other Entities" (amendments effective for periods commencing on or after 1 January 2016);
- IAS 1 (amended) "Presentation of Financial Statements" (amendments effective 1 January 2016); and
- IAS 28 (amended), "Investments in Associates and Joint Ventures" (amendments regarding the application of the consolidation exception, effective for periods commencing on or after 1 January 2016).

In addition, the IASB completed its Disclosure Initiative project in January 2016 and its September 2014 Annual Improvements to IFRSs project in September 2014. These projects have amended a number of existing standards and interpretations effective for accounting periods commencing on or after 1 January 2016.

The adoption of these amended standards has had no material impact on the Financial Statements of the Company.

#### **New Accounting Standards and interpretations applicable to future reporting periods**

At the date of approval of these Financial Statements, the following standards and interpretations, which may be relevant to the Company but have not been applied in these Financial Statements, were in issue but not yet effective:

- IFRS 7 (amended), "Financial Instruments: Disclosures" (amendments relating to additional hedge accounting disclosures resulting from the introduction of the hedge accounting chapter in IFRS 9, effective for periods commencing on or after 1 January 2018, or on application of IFRS 9 if earlier);
- IFRS 9, 'Financial Instruments' (relating to the classification and measurement of financial assets and liabilities, effective for periods commencing on or after 1 January 2018). This standard specifies how an entity should classify and measure financial assets and liabilities, including some hybrid contracts. The standard improves and simplifies the approach for classification and measurement of financial assets compared with the requirements of IAS 39 'Financial Statements: Recognition and Measurement' ("IAS 39");
- IFRS 15, "Revenue from Contracts with Customers" (effective for periods commencing on or after 1 January 2018);
- IAS 39 (amended), "Financial Instruments: Recognition and Measurement" (amendments to permit an entity to elect to continue to apply the hedge accounting requirements in IAS 39 for a fair value hedge of the interest rate exposure of a portion of a portfolio of financial assets or financial liabilities when IFRS 9 is applied, and to extend the fair value option to certain contracts that meet the 'own use' scope exception, effective for periods commencing on or after 1 January 2018, or on application of IFRS 9 if earlier).

In addition, the IASB completed its Disclosure Initiative project in January 2016 and its Annual Improvements 2014-2016 Cycle project in December 2016. These projects have amended a number of existing standards and interpretations effective for accounting periods commencing on or after 1 January 2017 or 1 January 2018.

The Board expects that the adoption of these standards in a future period will not have a material impact on the Financial Statements of the Company as the majority of the Company's financial assets are designated at fair value through profit or loss.

#### **Investment income**

Other income relates to interest income. Interest income is recognised on a time-proportionate basis using the effective interest method and includes interest income from cash and cash equivalents.

The effective interest rate is calculated using estimated cash flows, considering the expected life of the financial asset and future potential credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate and all other premiums or discounts.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES *continued*

#### **Net Gains and losses on Financial Assets at Fair Value through Profit or Loss**

Net gains/(losses) on financial assets at fair value through profit or loss includes all realised and unrealised fair value changes, foreign exchange gains/(losses) and income and capital distributions received.

Net realised gains/(losses) from financial assets at fair value through profit or loss are calculated using the average cost method.

#### **Expenses**

Expenses of the Company are charged through profit or loss in the Statement of Comprehensive Income on an accruals basis.

#### **Ordinary Shares and C Shares**

The ordinary shares and C shares of the Company are classified as equity based on the substance of the contractual arrangements and in accordance with the definition of equity instruments under IAS 32.

The proceeds from the issue of participating shares are recognised in the Statement of Changes in Shareholders' Equity, net of incremental issuance costs.

#### **Cash and Cash Equivalents**

Cash comprises current deposits with banks. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash, are subject to an insignificant risk of changes in value, and are held for the purpose of meeting short-term cash commitments rather than for investments or other purposes.

#### **Financial Instruments**

##### *Classification*

The Company classifies its financial assets and financial liabilities into categories in accordance with IAS 39.

The category of financial assets and financial liabilities at fair value through profit or loss comprises:

##### *Financial assets at fair value through profit or loss*

Financial assets classified in this category are designated by management on initial recognition as part of a group of financial assets which are managed and their performance evaluated on a fair value basis, in accordance with a documented investment strategy. During the prior year, the term "financial assets designated at fair value through profit or loss" included investments in US Treasury Bills which were purchased and sold during that year. The Investment Entities exception to consolidation ("Investment entities exception") in IFRS 10 'Consolidated Financial Statements' ("IFRS 10") requires subsidiaries of an investment entity to be accounted for at fair value through profit or loss in accordance with IAS 39. As the Company's investment in the Master Fund is not held for trading, it is presented in the Financial Statements with the "designated at fair value" financial assets, as all are managed together on a fair value basis.

##### *Financial assets at amortised cost*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, and they are carried at amortised cost. The Company includes in this category cash and cash equivalents and other receivables. The amortised cost of a financial asset is the amount at which the instrument is measured at initial recognition (its fair value) adjusted for initial direct costs, minus principal repayments, plus or minus the cumulative amortisation, using effective interest rate method, of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES continued

#### Financial Instruments continued

##### *Classification continued*

##### *Financial liabilities at amortised cost*

The Company includes in this category expenses payable.

##### *Recognition and initial measurement*

Financial assets and financial liabilities are measured initially at fair value, being the transaction price, including transaction costs for items that will subsequently be measured at amortised cost, on the trade date. Transaction costs on financial assets at fair value through profit or loss are expensed immediately.

##### *Subsequent measurement*

After initial measurement, the Company measures financial instruments classified at fair value through profit or loss at their fair values. Changes in fair value are recognised in "Net gains/(losses) on financial assets at fair value through profit or loss" in the Statement of Comprehensive Income.

##### *Derecognition*

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire or it transfers the financial asset and the transfer qualifies for derecognition in accordance with IAS 39. A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expires.

#### Investment in the Master Fund

The Board has determined that the Company has all the elements of control as prescribed by IFRS 10 in relation to the Master Fund as the Company is the main limited partner, is exposed and has rights to the returns of the Master Fund and has the ability either directly or through the Investment Adviser to affect the amount of its returns from the Master Fund.

The Investment Entities exception requires that an investment entity that has determined that it is a parent under IFRS 10 shall not consolidate certain of its subsidiaries; instead it is required to measure its investment in these subsidiaries at fair value through profit or loss in accordance with IAS 39.

The criteria which defines an investment entity are as follows:

- An entity has obtained funds from one or more investors for the purpose of providing those investors with investment management services;
- An entity has committed to its investors that its business purpose is to invest funds solely for the returns from capital appreciation, investment income or both; and
- An entity measures and evaluates the performance of substantially all of its investments on a fair value basis.

The Company provides investment management services and has a number of investors who pool their funds to gain access to these services and investment opportunities that they might not have had access to individually. The Company, being listed on the SFS of the London Stock Exchange, obtains funding from a diverse group of external shareholders.

Consideration is also given to the time frame of an investment. An investment entity should not hold its investments indefinitely but should have an exit strategy for their realisation. As the Master Fund's investments have documented maturity/redemption dates or will be sold if other investments with better risk/reward profile are identified, the Directors consider that this demonstrates a clear exit strategy.

The Master Fund measures and evaluates the performance of substantially all of its investments on a fair value basis. The fair value method is used to represent the Company's performance in its communication to the market, including investor presentations. In addition, the Company reports fair value information internally to Directors, who use fair value as a significant measurement attribute to evaluate the performance of its investments and to make investment decisions for mature investments.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES *continued*

#### **Investment in the Master Fund** *continued*

The Company has determined that the fair value of the Master Fund is the Master Fund's Net Asset Value ("NAV").

The Company has concluded that the Master Fund, which is fully drawn down at the year end, meets the definition of an unconsolidated subsidiary under IFRS 12 and has made the necessary disclosures.

#### **Foreign Currency**

##### *Functional and presentation currency*

The Financial Statements of the Company are presented in the currency of the primary economic environment in which the Company operates (the "functional currency"). The Directors have considered the primary economic currency of the Company and considered the currency in which the original finance was raised and distributions will be made, and ultimately what currency would be returned if the Company was wound up. The Directors have also considered the currency to which the underlying investments are exposed. On balance, the Directors believe the US Dollar best represents the functional currency of the Company during the year. Therefore, the books and records are maintained in US Dollars and for the purpose of the Financial Statements the results and financial position of the Company are presented in US Dollars, which has been selected as the presentation currency of the Company. All foreign exchange differences relating to monetary items, including cash, are presented in 'Net foreign exchange loss' in the Statement of Comprehensive Income.

##### *Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Statement of Comprehensive Income.

Non-monetary items measured at historical cost are translated using the exchange rates at the date of the transaction (not retranslated). Non-monetary items measured at fair value are translated using the exchange rates at the date when fair value was determined.

#### **Taxation**

The Company is exempt from Guernsey income tax and is charged an annual exemption fee of £1,200 (31 December 2015: £1,200).

#### **Dividends**

Dividends payable to the holders of ordinary shares and C shares are recorded through the Statement of Changes in Shareholders' Equity when they are declared to shareholders. The payment of any dividend by the Company is subject to the satisfaction of a solvency test as required by the Companies (Guernsey) Law, 2008.

#### **Segmental Reporting**

The Board has considered the requirements of IFRS 8 – "Operating Segments". The Company has entered into an Investment Advisory Agreement with the Investment Adviser under which the Investment Adviser is responsible for the management of the Company's investment portfolio, subject to the overall supervision of the Directors. Subject to its terms and conditions, the Investment Advisory Agreement requires the Investment Adviser to manage the Company's investment portfolio in accordance with the Company's investment guidelines as in effect from time to time, including the authority to purchase and sell securities and other investments and to carry out other actions as appropriate to give effect thereto. However, the Board retains full responsibility to ensure that the Investment Adviser adheres to its mandate. Moreover, the Board is fully responsible for the appointment and/or removal of the Investment Adviser. Accordingly, the Board is deemed to be the "Chief Operating Decision Maker" of the Company.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES *continued*

#### **Segmental Reporting** *continued*

In the Board's opinion, the Company is engaged in a single segment of business, being the investment into the Master Fund, a Guernsey registered Limited Partnership.

Segment information is measured on the same basis as that used in the preparation of the Company's Financial Statements.

The Company receives no revenues from external customers, nor holds any non-current assets, in any geographical area other than Guernsey.

### 3. USE OF JUDGEMENTS AND ESTIMATES

The preparation of Financial Statements in accordance with IFRS requires the Board to make judgements, estimates and assumptions that affect the application of policies and the reported amounts of assets, liabilities, income and expenses, disclosure of contingent assets and liabilities at the date of the Financial Statements and income and expenses during the period. The estimates and associated assumptions are based on various factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the 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. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The principal estimates and judgements made by the Board are as follows:

#### **Judgements**

##### *Going Concern*

The Board has assessed the Company's financial position as at 31 December 2016 and the factors that may impact its performance in the forthcoming year and are of the opinion that it is appropriate to prepare these Financial Statements on a going concern basis.

##### *Investment Entity*

In accordance with the Investment entities exception contained in IFRS 10, the Board has determined that the Company satisfies the criteria to be regarded as an investment entity and that the Company provides investment related services and as a result measures its investment in the Master Fund at fair value. This determination involves a degree of judgement (see note 2).

#### **Estimates**

##### *Fair Value*

The Company records its investment in the Master Fund at fair value. Fair value is determined as the Company's share of the Master Fund's NAV. This share is net of any notional carried interest due to the Founder Partner of the Master Fund. The Investment Adviser has reviewed the NAV of the Master Fund and determined that no adjustments regarding liquidity discounts were required.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 4. DIVIDENDS

The Company declares dividends payable to shareholders representing an amount in aggregate at least equal to the gross income from investments received by the Company in the relevant financial period attributable to the Company's investment in the Master Fund and Qualifying Short Term Investments, less expenses of the Company.

The Company had declared eleven monthly dividends of a minimum of 0.7 US cents per ordinary share and a larger twelfth interim dividend such that, in the opinion of the Directors, substantially all net income generated by the Company in 2016 will be distributed to shareholders.

The Company declared the following dividends to ordinary shareholders relating to the year ended 31 December 2016:

Period to	Payment date	Dividend rate per share (cents)	Net dividend payable (US\$)	Record date	Ex-dividend date
31 January 2016	26 February 2016	0.70	2,243,127	12 February 2016	11 February 2016
29 February 2016	24 March 2016	0.70	2,243,128	4 March 2016	3 March 2016
31 March 2016	21 April 2016	0.70	2,244,635	8 April 2016	7 April 2016
30 April 2016	19 May 2016	0.70	2,244,635	6 May 2016	5 May 2016
31 May 2016	23 June 2016	0.70	2,244,635	3 June 2016	2 June 2016
30 June 2016	21 July 2016	0.70	2,247,019	8 July 2016	7 July 2016
31 July 2016	18 August 2016	0.70	2,235,526	5 August 2016	4 August 2016
31 August 2016	22 September 2016	0.70	2,236,521	9 September 2016	8 September 2016
30 September 2016	20 October 2016	0.70	2,194,321	7 October 2016	6 October 2016
31 October 2016	24 November 2016	0.70	2,193,806	4 November 2016	3 November 2016
30 November 2016	22 December 2016	0.70	2,164,691	9 December 2016	8 December 2016
		7.70	24,492,044		
<i>Dividend declared after 31 December 2016:</i>					
31 December 2016	2 February 2017	5.75	18,055,284	13 January 2017	12 January 2017
		13.45	42,547,328		





## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 4. DIVIDENDS continued

The Company declared the following dividends to ordinary shareholders during the year ended 31 December 2015:

Period to	Payment date	Dividend rate per share (cents)	Net dividend payable (US\$)	Record date	Ex-dividend date
31 December 2014	12 February 2015	4.25	5,173,478	30 January 2015	29 January 2015
31 January 2015	19 February 2015	0.70	853,289	6 February 2015	5 February 2015
28 February 2015	19 March 2015	0.70	1,168,288	6 March 2015	5 March 2015
31 March 2015	23 April 2015	0.70	1,168,288	10 April 2015	9 April 2015
30 April 2015	21 May 2015	0.70	1,168,288	8 May 2015	7 May 2015
31 May 2015	25 June 2015	0.70	1,483,289	12 June 2015	11 June 2015
30 June 2015	23 July 2015	0.70	1,483,289	10 July 2015	9 July 2015
31 July 2015	20 August 2015	0.70	1,483,289	7 August 2015	6 August 2015
31 August 2015	24 September 2015	0.70	1,483,289	11 September 2015	10 September 2015
30 September 2015	22 October 2015	0.70	1,485,129	9 October 2015	8 October 2015
31 October 2015	19 November 2015	0.70	1,485,129	6 November 2015	5 November 2015
30 November 2015	24 December 2015	0.70	1,485,129	11 December 2015	10 December 2015
		7.70	19,920,174		
31 December 2015	13 January 2016	2.226	4,722,709	29 December 2015	24 December 2015
		9.926	24,642,883		

The Company also declared the following dividend to C shareholders for the period 17 August 2015 to 31 December 2015:

Period to	Payment date	Dividend rate per share (cents)	Net dividend payable (US\$)	Record date	Ex-dividend date
31 December 2015	13 January 2016	2.354	2,396,372	29 December 2015	24 December 2015

The default payment for dividends is US Dollars. However, with effect from 29 June 2016, shareholders can elect to receive their dividends in Sterling by registering under the Company's Dividend Currency Election.

The rate per ordinary share to be used to pay shareholders who elected to receive their dividend in Sterling will be announced on the London Stock Exchange each month prior to the payment date.

Under Guernsey law, companies can pay dividends in excess of accounting profit provided they satisfy the solvency test prescribed by the Companies (Guernsey) Law, 2008. The solvency test considers whether a company is able to pay its debts when they fall due, and whether the value of a company's assets is greater than its liabilities. The Company passed the solvency test for each dividend paid.

Total dividends payable as at 31 December 2016 were US\$Nil (31 December 2015: US\$7,119,081).



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 5. FINANCIAL RISK MANAGEMENT

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Company's risk management policies are established to identify and analyse the risks faced by the Company, to set appropriate risk limits and controls and to monitor risks and adherence to limits. Risk management policies are reviewed regularly to reflect changes in market conditions and the Company's activities. Below is a non-exhaustive summary of the risks that the Company is exposed to as a result of its use of financial instruments:

#### Market Risk

Market risk is the risk of changes in market prices, such as foreign exchange rates, interest rates and equity prices, affecting the Company's income and/or the value of its holdings in financial instruments.

The Company's exposure to market risk comes mainly from movements in the value of its investment in the Master Fund and on a look-through basis to the underlying loans in each CLO. Changes in credit spreads may further affect the Company's net equity or net income directly through their impact on unrealised gains or losses on investments within the Master Fund and on a look-through basis to the underlying loans in each CLO.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters while optimising the return on risk. The Company's strategy for the management of market risk mirrors the strategy of the Master Fund, driven by their investment objective to generate attractive, risk-adjusted returns, principally through income distributions by seeking exposure to US and European CLOs or other vehicles and structures which provide exposure to portfolios consisting primarily of US and European floating rate senior secured loans and which may include non-recourse financing. The Company's market risk is managed on a daily basis by the Investment Adviser in accordance with policies and procedures in place.

The Company intends to mitigate market risk generally by not making investments that would cause it to have exposure to a single corporate issuer exceeding 5% of the Master Fund's aggregate gross assets at the time of investment. Special Purpose Vehicles such as CLOs are not considered corporate issuers. The Company's market positions are monitored on a quarterly basis by the Board of Directors.

#### Interest Rate Risk

The Company is exposed to interest rate risk through the investments held by the Master Fund and on a look-through basis to the underlying assets in the CLOs.

A majority of the Company's financial assets comprises an investment into the Master Fund, which invests in Income Notes and Mezzanine tranches of cash flow CLOs. The Master Fund's exposure to interest rate risk is significantly mitigated by the fact that the majority of the underlying loans in each CLO bear interest at floating Libor-based rates.

Interest receivable on bank deposits or payable on bank overdraft positions will be affected by fluctuations in interest rates, however, the underlying cash positions will not be affected.

The following table shows the portfolio profile of the Master Fund at 31 December 2016 and 31 December 2015:

	<b>31 December 2016</b>	<b>31 December 2015</b>
	<b>US\$</b>	<b>US\$</b>
Investments with a floating interest rate	411,806,313	275,519,805
Financial assets at fair value through profit or loss (note 6)	<b>411,806,313</b>	<b>275,519,805</b>



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 5. FINANCIAL RISK MANAGEMENT continued

#### Market Risk continued

##### Interest Rate Risk continued

The following table shows the Directors' best estimate of the Company's share of the sensitivity of the portfolio of the Master Fund to stressed changes in interest rates, with all other variables held constant. The table assumes parallel shifts in the respective forward yield curves.

Possible reasonable change in rate	31 December 2016 effect on net assets and profit or loss US\$	Possible reasonable change in rate	31 December 2015 effect on net assets and profit or loss US\$
-1%	7,895,548	-1%	7,330,466
1%	3,370,449	1%	952,930

The change in methodology is to calculate the impact of a 1% interest rate change on the annual income generated by the Master Fund's CLO mezzanine and equity investments by using Intex to generate cash flow projections.

##### Currency risk

The Company is exposed to very limited currency risk, as the majority of its assets and liabilities are denominated in US Dollars.

The Company is exposed indirectly to currency risk through its investment into the Master Fund. The Master Fund's portfolio is predominantly denominated in US Dollar. However, the Master Fund may also invest in underlying assets which are denominated in currencies other than the US Dollar (e.g. Euro). Accordingly, the value of such assets may be affected, favourably or unfavourably, by fluctuations in currency rates which, if unhedged, could have the potential to have a significant effect on returns. To reduce the impact of currency fluctuations and the volatility of returns which may result from currency exposure, the Investment Adviser may hedge the currency exposure of the assets of the Master Fund.

The Company's share of the Master Fund's total net foreign currency exposure at the year end was as follows:

	31 December 2016 US\$	31 December 2015 US\$
<b>EUR Exposure</b>		
Financial assets at fair value through profit or loss	3,948,044	5,298,923
Forward foreign exchange contracts	(3,900,790)	(5,433,294)
Other payables	(29,162)	(40,719)
<b>Net EUR Exposure</b>	<b>18,092</b>	<b>(175,090)</b>
	31 December 2016 US\$	31 December 2015 US\$
<b>GBP Exposure</b>		
Cash at bank	708	-
Other receivables	6,751	17,992
Other payables	(13,095)	(21,761)
<b>Net GBP Exposure</b>	<b>(5,636)</b>	<b>(3,769)</b>
<b>NET EXPOSURE</b>	<b>12,456</b>	<b>(178,859)</b>



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 5. FINANCIAL RISK MANAGEMENT *continued*

#### Market Risk *continued*

##### Currency risk *continued*

	Possible change in exchange rate	31 December 2016 net exposure US\$	31 December 2016 effect on net assets and profit or loss US\$
EUR/US Dollar	+/- 5%	18,092	(+/-) 905
GBP/US Dollar	+/- 15%	(5,636)	(+/-) (845)

The sensitivity rate of 5% is regarded as reasonable due to the recent volatility of US Dollar against Euro.

The sensitivity rate of 15% is regarded as reasonable due to the recent volatility of US Dollar against Sterling.

	Possible change in exchange rate	31 December 2015 net exposure US\$	31 December 2015 effect on net assets and profit or loss US\$
EUR/US Dollar	+/- 5%	(175,090)	(+/-) (8,755)
GBP/US Dollar	+/- 5%	(3,769)	(+/-) (188)

##### Other price risks

There is a risk that the fair value or future cash flows, on a look-through basis to the underlying CLOs, will fluctuate due to changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market. The Directors do not believe that the returns on investments are correlated to any specific index or other price variable.

If the value of the Company's investment in the Master Fund were to increase or decrease by 1%, the impact on the NAV of the Company would be +/- US\$2,916,828 (31 December 2015: US\$2,690,691).

#### Credit and Counterparty Risk

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Company, the Master Fund or a vehicle in which the Master Fund invests, resulting in a financial loss to the Company. Credit risk arises principally from debt securities held, and also from derivative financial assets and cash and cash equivalents. For risk management reporting purposes, the Company considers and aggregates all elements of credit risk exposure (such as individual obligation default risk, country risk and sector risk).

The Company's policy on credit risk mirrors that of the Master Fund, which is to minimise its exposure to counterparties with perceived higher risk of default by dealing only with counterparties that meet the credit standards set out in the Company's prospectus, and by taking collateral.

The table below analyses the Company's maximum exposure to credit risk in relation to the components of the Statement of Financial Position.

	31 December 2016 US\$	31 December 2015 US\$
Cash and cash equivalents	12,200,459	5,401,130
Prepayments	77,057	92,507
Distribution receivable	7,826,914	10,256,219
Financial assets at fair value through profit or loss	291,682,780	269,069,087
	<b>311,787,210</b>	<b>284,818,943</b>



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 5. FINANCIAL RISK MANAGEMENT continued

#### Credit and Counterparty Risk continued

At 31 December 2016, the cash and cash equivalents and other assets of the Company, excluding its investment into the Master Fund, and substantially all of the assets of the Master Fund are held by BNP Paribas Security Services (the "Custodian"). Bankruptcy or insolvency of the Custodian may cause the Company's rights with respect to securities held by the Custodian to be delayed or limited. This risk is managed by monitoring the credit quality and financial positions of the Custodian. The long-term rating of the Custodian as at 31 December 2016 was A1 as rated by Moody's (31 December 2015: Aa1) and A by Standard & Poor's (31 December 2015: AA+).

Credit risk is assessed from time to time by the Investment Adviser on a look-through basis to the underlying loans in each CLO. The Investment Adviser seeks to provide diversification in terms of underlying assets, issuer sector, geography and maturity profile. Please refer to the graph on page 5 for the concentration of credit risk by industry for the CLO investments on a look-through basis as at 31 December 2016. The Company's credit risk is monitored on a quarterly basis by the Board of Directors.

The Master Fund's exposure to credit risk relating to the underlying CLO investments based on the country of registration (not necessarily asset class exposure) as at 31 December 2016 and 31 December 2015 is summarised below:

	<b>31 December 2016</b>	<b>31 December 2015</b>
	<b>US\$</b>	<b>US\$</b>
United States of America	406,480,474	270,220,882
Europe	5,325,839	5,298,923
Master Fund financial assets at fair value through profit or loss (note 6)	<b>411,806,313</b>	<b>275,519,805</b>

The geographical breakdown of the underlying CLO investments is as follows:

	<b>31 December 2016</b>	<b>31 December 2015</b>
<b>Country</b>	<b>%</b>	<b>%</b>
United States of America	88.8	91.9
Other	3.3	2.3
Canada	2.9	1.6
Luxembourg	2.5	2.2
United Kingdom	1.3	1.2
Netherlands	1.2	0.8
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

The table below summarises the Master Fund's portfolio concentrations as of 31 December 2016 and 31 December 2015:

	<b>Maximum portfolio</b>	<b>Average portfolio</b>
	<b>holdings of a single</b>	<b>holdings % of</b>
	<b>asset % of total</b>	<b>total portfolio</b>
	<b>portfolio</b>	<b></b>
31 December 2016	5.68%	1.79%
31 December 2015	8.61%	4.00%



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 5. FINANCIAL RISK MANAGEMENT *continued*

#### Credit and Counterparty Risk *continued*

The tables below summarises the Master Fund's portfolio by asset class portfolio ratings as at 31 December 2016 and 31 December 2015:

<b>By Asset Class</b>	<b>31 December 2016</b> <b>US\$</b>	<b>31 December 2015</b> <b>US\$</b>
Equity CLO	240,178,427	215,819,398
Mezzanine CLO	171,627,886	52,283,397
Term loan	-	7,417,010
Master Fund financial assets at fair value through profit or loss (note 6)	<b>411,806,313</b>	<b>275,519,805</b>

The breakdown of the underlying CLO investments by rating is as follows:

<b>Rating</b>	<b>31 December 2016</b> <b>%</b>	<b>31 December 2015</b> <b>%</b>
B	39.8	46.0
B+	22.4	22.0
BB-	15.3	13.0
B-	8.9	7.0
BB	5.3	5.0
BB+	2.9	3.0
NR	2.2	2.0
CCC+	1.2	1.0
CCC	0.9	-
BBB-	0.5	1.0
CCC-	0.2	-
D	0.2	-
BBB	0.1	-
CC	0.1	-
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

Further information regarding the geographical, currency, rating and industry diversification breakdown is provided in the tables on page 5 in the Investment Adviser's Report.

Activities undertaken by the Company and Master Fund may give rise to settlement risk. Settlement risk is the risk of loss due to the failure of a counterparty to honour its obligations to deliver cash, securities or other assets as contractually agreed.

For the majority of transactions, settlement risk is mitigated by conducting settlements through a broker to ensure that a trade is settled only when both parties have fulfilled their contractual settlement obligations. Settlement limits form part of the credit approval and limit monitoring processes.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 5. FINANCIAL RISK MANAGEMENT continued

#### Liquidity Risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

The Company's policy and the Investment Adviser's approach to managing liquidity is to ensure, as far as possible, that the Company will always have sufficient liquidity to meet its liabilities when due, under both normal and stress conditions, including estimated redemptions of shares, without incurring unacceptable losses or risking damage to the Company's reputation.

The Company's liquidity risk is managed on a daily basis by the Investment Adviser on a look-through basis to the underlying loans in each CLO. The Investment Adviser monitors and considers the Company's and the Master Fund's cash balances, projected expenses and projected income from investments when making any new investment recommendations.

Given the Company's permanent capital structure as a closed-ended fund, it is not exposed to redemption risk. However, the Company's financial instruments include investments in collateralised debt obligations and derivative contracts (if any) traded over-the-counter, which are not traded in an organised public market and which may be illiquid.

The Company's overall liquidity risk is monitored on a quarterly basis by the Board of Directors. Shareholders have no right of redemption and must rely, in part, on the existence of a liquid market in order to realise their investment.

All liabilities of the Company are due within one financial year.

#### Operational Risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the processes, technology and infrastructure supporting the Company's activities relating to financial instruments, either internally or on the part of service providers, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of investment management behaviour.

Operational risk is managed so as to balance the limiting of financial losses and damage to its reputation with achieving its investment objective of generating returns to investors.

The primary responsibility for the development and implementation of controls over operational risk rests with the Board of Directors. This responsibility is supported by the development of overall standards for the management of operational risk, which encompasses the controls and processes at the service providers and the establishment of service levels with the service providers.

The Directors' assessment of the adequacy of the controls and processes in place at the service providers with respect to operational risk is carried out via regular discussions with the service providers and a review of the service providers' Service Organisation Controls ("SOC") 1 reports on internal controls, if available.

Substantially all of the assets of the Company and Master Fund are held by BNP Paribas Securities Services S.C.A., Guernsey Branch, in its capacity as Custodian. The bankruptcy or insolvency of the Custodian may cause the Company's rights with respect to the securities held by the Custodian to be limited. The Investment Adviser monitors the credit ratings and capital adequacy of the Custodian on a quarterly basis, and reviews the findings documented in the SOC 1 report on the internal controls annually.

#### Capital Management

The Board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the Company. The Company's capital is represented by the ordinary shares and C shares. Capital is managed in accordance with the investment policy, in pursuit of its investment objectives.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 6. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	<b>31 December 2016</b>	<b>31 December 2015</b>
	<b>US\$</b>	<b>US\$</b>
Cost at the start of the year	299,827,883	118,724,784
Purchases into the Master Fund at cost during the year	6,500,000	181,103,099
Purchases of US Treasury Bills at cost during the year	–	149,985,186
Proceeds from sale of US Treasury Bills during the year	–	(149,996,969)
Realised gain/(loss) on sale of US Treasury Bills	–	11,783
Capital distributions received from Master Fund	(9,266,250)	–
Cost of investment into the Master Fund at the end of the year	297,061,633	299,827,883
Net unrealised losses on investments at the end of the year	(5,378,853)	(30,758,796)
Financial assets at fair value through profit or loss at the end of the year	<b>291,682,780</b>	<b>269,069,087</b>
Realised gain on sales during the year	–	13,392
Realised loss on sales during the year	–	(1,609)
Movement in net unrealised (loss)/gain during the year	25,379,943	(35,936,149)
Income distributions declared by Master Fund	43,124,599	28,759,883
Net gains/(losses) on financial assets at fair value through profit or loss	<b>68,504,542</b>	<b>(7,164,483)</b>

During the year ended 31 December 2016, the Master Fund accepted a new limited partner. The new limited partner was drawn down during March 2016 and April 2016. At 31 December 2016, the Company had a 74.13% (31 December 2015: 100%) holding in the Master Fund. The following table reconciles the Company's proportionate share of the Master Fund's financial assets at fair value through profit or loss to the Company's financial assets at fair value through profit or loss:

	<b>31 December 2016</b>	<b>31 December 2015</b>
	<b>US\$</b>	<b>US\$</b>
Master Fund - Financial assets at fair value through profit or loss	305,272,020	275,519,805
Less: Master Fund's net current liabilities	(13,589,240)	(6,450,718)
Company's financial assets at fair value through profit or loss	<b>291,682,780</b>	<b>269,069,087</b>

As at 31 December 2016 US\$Nil (31 December 2015: US\$Nil) carried interest was allocated to the Master Fund's Founder Partner.





## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 6. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS *continued*

The Company's net unrealised losses on investment at the end of year comprises the following:

<b>Master Fund</b>	<b>31 December 2016</b>	<b>31 December 2015</b>
	<b>US\$</b>	<b>US\$</b>
Net unrealised (losses)/gains on investments at the beginning of the year	(30,758,796)	5,177,353
Investment income	46,378,238	24,387,904
Unrealised gains/(losses) on financial assets at fair value through profit or loss	30,753,925	(27,804,710)
Realised losses on financial assets at fair value	(315,693)	(2,121,116)
Net gains on derivative financial instruments and foreign exchange	134,730	629,681
Other income	–	861
Expenses	(8,446,658)	(2,268,886)
Income distributions declared during the year	(43,124,599)	(28,759,883)
Net unrealised losses on investments at the end of the year	<b>(5,378,853)</b>	<b>(30,758,796)</b>

IFRS 13 requires that a fair value hierarchy be established that prioritises the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under IFRS 13 are set as follows:

- Level 1: inputs that are quoted market prices (unadjusted) in active markets for identical instruments;
- Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.
- Level 3: Inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments but for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The level in the fair value hierarchy within which the fair value measurement is categorised is determined on the basis of the lowest level input that is significant to the fair value measurement. For this purpose, the significance of an input is assessed against 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 requires judgement, considering factors specific to the asset or liability.

The determination of what constitutes 'observable' requires significant judgement. Observable data is considered to be that market data that is readily available, regularly distributed or updated, reliable, not proprietary, and provided by independent sources that are actively involved in the relevant market.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 6. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS *continued*

The following table analyses within the fair value hierarchy the Company's financial assets (by class, excluding cash and cash equivalents, prepayments, distribution receivable, dividends payable and other payables) measured at fair value:

	31 December 2016			Total US\$
	Level 1 US\$	Level 2 US\$	Level 3 US\$	
<b>Assets:</b>				
Financial assets at fair value through profit or loss	–	–	291,682,780	291,682,780
<b>Total</b>	<b>–</b>	<b>–</b>	<b>291,682,780</b>	<b>291,682,780</b>

	31 December 2015			Total US\$
	Level 1 US\$	Level 2 US\$	Level 3 US\$	
<b>Assets:</b>				
Financial assets at fair value through profit or loss	–	–	269,069,087	269,069,087
<b>Total</b>	<b>–</b>	<b>–</b>	<b>269,069,087</b>	<b>269,069,087</b>

The investment in the Master Fund, which is fair valued at each reporting date, has been classified within Level 3 as it is not traded and contains unobservable inputs.

The following table presents the movement in Level 3 instruments:

	31 December 2016 US\$	31 December 2015 US\$
Opening Balance	269,069,087	123,902,137
Purchases	6,500,000	181,103,099
Movement in net unrealised gain/(loss) during the year	25,379,943	(35,936,149)
Capital distributions received from Master Fund	(9,266,250)	–
Closing Balance	<b>291,682,780</b>	<b>269,069,087</b>

#### *Transfers between Level 1, 2 and 3*

There have been no transfers between levels during the year ended 31 December 2016 or 31 December 2015. Transfers between levels of the fair value hierarchy are recognised as at the end of the reporting period during which the change has occurred.

On a look-through basis, the following table analyses within the fair value hierarchy the Company's proportionate share of the Master Fund's financial assets and derivatives (by class, excluding cash and cash equivalents, other receivables and prepayments, distribution payable, carried interest payable and trade and other payables) measured at fair value:

	31 December 2016			Total US\$
	Level 1 US\$	Level 2 US\$	Level 3 US\$	
Financial assets at fair value through profit or loss	–	127,227,752	178,044,268	305,272,020
Derivatives at fair value through profit or loss	–	196,375	–	196,375
<b>Total</b>	<b>–</b>	<b>127,424,127</b>	<b>178,044,268</b>	<b>305,468,395</b>



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 6. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS continued

	31 December 2015			Total US\$
	Level 1 US\$	Level 2 US\$	Level 3 US\$	
Financial assets at fair value through profit or loss	–	59,700,407	215,819,398	275,519,805
Derivatives at fair value through profit or loss	–	(51,294)	-	(51,294)
<b>Total</b>	<b>–</b>	<b>59,649,113</b>	<b>215,819,398</b>	<b>275,468,511</b>

The following table analyses within the fair value hierarchy the Company's assets and liabilities not measured at fair value but for which fair value is disclosed:

	31 December 2016			Total US\$
	Level 1 US\$	Level 2 US\$	Level 3 US\$	
<b>Assets:</b>				
Cash and cash equivalents	–	12,200,459	–	12,200,459
Prepayments	–	77,057	–	77,057
Distribution receivable	–	7,826,914	–	7,826,914
<b>Total</b>	<b>–</b>	<b>20,104,430</b>	<b>–</b>	<b>20,104,430</b>
<b>Liabilities</b>				
Other payables	–	103,315	–	103,315
<b>Total</b>	<b>–</b>	<b>103,315</b>	<b>–</b>	<b>103,315</b>

	31 December 2015			Total US\$
	Level 1 US\$	Level 2 US\$	Level 3 US\$	
<b>Assets:</b>				
Cash and cash equivalents	–	5,401,130	–	5,401,130
Prepayments	–	92,507	–	92,507
Distribution receivable	–	10,256,219	–	10,256,219
<b>Total</b>	<b>–</b>	<b>15,749,856</b>	<b>–</b>	<b>15,749,856</b>
<b>Liabilities</b>				
Other payables	–	107,889	–	107,889
Dividends payable	–	7,119,081	–	7,119,081
<b>Total</b>	<b>–</b>	<b>7,226,970</b>	<b>–</b>	<b>7,226,970</b>



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 6. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS continued

The assets and liabilities included in the above table are carried at amortised cost; their carrying values are a reasonable approximation of fair value.

Cash and cash equivalents include deposits held with banks.

Other payables represent the contractual amounts and obligations due by the Company for settlement of trades and expenses.

The following table summarises the valuation methodologies used for the Company's investments categorised in Level 3 as at 31 December 2016:

Security	Fair Value US\$	Valuation methodology	Unobservable inputs	Ranges
Master Fund	291,682,780	NAV	Zero % discount	N/A

The following table summarises the valuation methodologies used for the Company's investments categorised in Level 3 as at 31 December 2015:

Security	Fair Value US\$	Valuation methodology	Unobservable inputs	Ranges
Master Fund	269,069,087	NAV	Zero % discount	N/A

The Master Fund has engaged an independent third party to provide valuations for its CLO investments. The following table summarises, in the Company's opinion, the valuation methodologies used by the independent third party to value the Company's proportionate share of the Master Fund's investments categorised in Level 3 as at 31 December 2016:

Asset Class	Fair Value US\$	Unobservable inputs	Ranges	Average	Sensitivity to changes in significant unobservable inputs
<u>Income Note CLOs</u>					
United States of America	172,993,836	Prices provided by a third party agent	US\$0.5800 – US\$0.9000	US\$0.7896	1% increase/decrease will have a fair value impact of +/- US\$1,729,938
Europe	3,948,045	Prices provided by a third party agent	€0.8300	€0.8300	1% increase/decrease will have a fair value impact of +/- US\$39,480
<u>Sub Fee Notes</u>					
United States of America	1,102,387	Prices provided by a third party agent	US\$0.0260 – US\$0.0480	US\$0.0373	1% increase/decrease will have a fair value impact of +/- US\$11,024
	<b>178,044,268</b>				



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 6. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS *continued*

The following table summarises, in the Company's opinion, the valuation methodologies used by the independent third party to value the Master Fund's investments categorised in Level 3 as at 31 December 2015:

Asset Class	Fair Value US\$	Unobservable inputs	Ranges	Average	Sensitivity to changes in significant unobservable inputs
<u>Income Note CLOs</u>					
United States of America	208,663,900	Prices provided by a third party agent	US\$0.5500 – US\$0.8500	US\$0.7372	1% increase/decrease will have a fair value impact of +/- US\$2,086,639
Europe	5,298,923	Prices provided by a third party agent	€0.8000	€0.8000	1% increase/decrease will have a fair value impact of +/- US\$52,989
<u>Sub Fee Notes</u>					
United States of America	1,856,575	Prices provided by a third party agent	US\$0.0345 – US\$0.0580	US\$0.0466	1% increase/decrease will have a fair value impact of +/- US\$18,566
	<b>215,819,398</b>				

### 7. INVESTMENT INCOME

	For the year ended 31 December 2016 US\$	For the year ended 31 December 2015 US\$
Interest income on financial assets carried at amortised cost:		
Cash and cash equivalents	16	2,315
Investment income on financial assets at fair value through profit or loss	–	4,112
	<b>16</b>	<b>6,427</b>



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 8. RELATED PARTIES AND OTHER KEY CONTACTS

#### Transactions with Investment Adviser and Investment Portfolio Investor

##### Investment Adviser

Fair Oaks Capital Limited (the "Investment Adviser") is entitled to receive an investment advisory fee from the Company of 1% per annum of the NAV of the Company, in accordance with the Investment Advisory Agreement dated 15 May 2014. The investment advisory fee is calculated and payable on the last business day of each month or on the date of termination of the agreement. The base management fee will be reduced to take into account any fees received by the Investment Adviser incurred by the Company in respect of its investment in the Master Fund (taking into account any rebates of such Management Fees to the Company) in respect of the same relevant period.

The net investment advisory fee during the year is as follows:

	<b>For the year ended 31 December 2016 US\$</b>	<b>For the year ended 31 December 2015 US\$</b>
Company investment advisory fee	2,833,535	2,205,252
Less: Master fund rebate	(2,726,481)	(1,798,576)
Net investment advisory fee	<b>107,054</b>	<b>406,676</b>

The Investment Adviser has agreed to reinvest and/or procure the reinvestment by the General Partner or by an Affiliate of it of (a) 25% of the fees which it receives annually from the Company pursuant to the Investment Advisory Agreement and (b) 25% of the Management Fee which the General Partner receives annually from the Master Fund in relation only to the Company's interest in the Master Fund by, in each case, subscribing for or procuring the subscription for ordinary shares issued by the Company at the then-prevailing NAV per ordinary share, provided that it shall instead use its best endeavours to purchase or procure the purchase of such ordinary shares in the secondary market in circumstances where to, at the time of any such subscription or purchase, the ordinary shares are trading at a discount of 5% or more of the NAV per ordinary share of the period to which it relates. If, having used best endeavours as mentioned above, ordinary shares cannot be purchased on the secondary market, ordinary shares shall be subscribed for from the Company. The obligation to subscribe for or purchase or procure the subscription for or purchase of these ordinary shares shall be fulfilled by the Investment Adviser by no later than one month after the end of the relevant financial period of the Company.

On 2 February 2015, the General Partner of the Master Fund reinvested US\$165,701 into the Company's ordinary shares which is equivalent to 25% of the investment advisory and management fees paid to the Investment Adviser and the General Partner during the period ended 31 December 2014.

On 4 September 2015, the General Partner of the Master Fund reinvested US\$254,440 into the Company's ordinary shares which is equivalent to 25% of the investment advisory and management fees paid to the Investment Adviser and the General Partner during the period 1 January 2015 to 31 July 2015.

On 31 December 2015, the General Partner of the Master Fund reinvested US\$237,930 into the Company's ordinary shares which is equivalent to 25% of the investment advisory and management fees paid to the Investment Adviser and the General Partner during the period 1 August 2015 to 30 November 2015.

On 21 March 2016, the General Partner of the Master Fund reinvested US\$165,322 into the Company's ordinary shares which is equivalent to 25% of the investment advisory and management fees paid to the Investment Adviser and the General Partner during the period 1 December 2015 to 29 February 2016.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 8. RELATED PARTIES AND OTHER KEY CONTACTS *continued*

#### Transactions with Investment Adviser and Investment Portfolio Investor *continued*

##### *Investment Adviser continued*

As the Commitment Period ended on 12 June 2016, any proceeds raised by the Company from the purchase of new ordinary shares by the Investment Adviser will currently have to be kept in cash or be redistributed to shareholders. On 25 August 2016, an amended and restated Investment Advisory Agreement was agreed between the Company and the Investment Adviser which amended the arrangement for which management fees are reinvested by the Investment Adviser. The changes to those arrangements were applied retrospectively from 29 February 2016.

To avoid the potential dilutive effects of these purchases, the Directors have amended the terms of the Investment Advisory Agreement regarding the reinvestment of fees as follows:

- The Investment Adviser will instead agree, in circumstances where the ordinary shares trade at any discount to the then-prevailing NAV per ordinary share, to reinvest its fees for a calendar quarter at the end of such quarter.
- More specifically, the amended Investment Advisory Agreement will provide that in circumstances where, as at the date of publication of the NAV per ordinary share with respect to the last calendar month of a calendar quarter (the "Quarter End NAV"), the price of the ordinary shares in the Company, adjusted for any dividends declared, traded at close in the secondary market below the then-prevailing Quarter End NAV, to reinvest and/or procure the reinvestment by an associate of it of (a) 25% of the fees which it shall receive with respect to that quarter from the Company pursuant to the Investment Advisory Agreement and (b) 25% of the Management Fee which the General Partner shall receive with respect to that quarter from the Master Fund in relation only to the Company's interest in the Master Fund by, in each case, using its best endeavours to purchase or procure the purchase of ordinary shares in the Company in the secondary market.
- The amended obligation to purchase or procure the purchase of such ordinary shares shall be fulfilled by the Investment Adviser by no later than one month after the end of such calendar quarter. The Investment Adviser will have no obligation to reinvest and/or procure the reinvestment of fees it receives with respect to a calendar quarter in circumstances where either (i) the ordinary shares in the Company did not trade at close in the secondary market at a discount to the then-prevailing Quarter End NAV; or (ii) where the ordinary shares in the Company did trade at close in the secondary market at a discount to the then-prevailing Quarter End NAV and it is unable to purchase or procure the purchase of ordinary shares in the Company in the secondary market at a discount to the then-prevailing Quarter End NAV despite having used its reasonable endeavours to do so and, in either case, the Investment Adviser shall retain all fees it receives for such quarter.

The Investment Advisory Agreement can be terminated by either party giving not less than 6 months written notice.

#### **Founder Partner**

The Master Fund also pays the Founder Partner a carried interest equal to 15 per cent of cash available to be distributed (after payment of expenses and management fees) after Limited Partners have received a Preferred Return. The calculation of the Preferred Return threshold will be based solely on distributions and not on NAV calculations so the Master Fund will not pay any carried interest until its investors have realised the amounts drawn down for investments and their Preferred Returns. As at 31 December 2016, US\$10,016,796 (31 December 2015: US\$Nil) carried interest was accrued at the Master Fund level.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 8. RELATED PARTIES AND OTHER KEY CONTACTS *continued*

#### Other Material Contracts

##### Administrator

Praxis Fund Services Limited (the "Administrator") shall be entitled to receive a time based fee quarterly in arrears for all Company Secretarial services. The Administrator is also entitled to an annual fee of US\$25,000, payable quarterly in arrears for Administration and Accounting services. This was increased to US\$31,000 per annum during the launch of the C shares and was reduced back to US\$25,000 when the C shares were converted to ordinary shares.

##### Custodian

BNP Paribas Securities Services S.C.A., Guernsey Branch (the "Custodian") and The Royal Bank of Canada (Channel Islands) Limited (the "former Custodian") waived all fees on the basis that all assets are invested into the Master Fund.

##### Directors' Fees

The Company's Directors are entitled to a fee in remuneration for their services as Directors at a rate of £37,000 each per annum.

The overall charge for the above-mentioned fees for the Company and the amounts due are as follows:

	For the year ended 31 December 2016 US\$	For the year ended 31 December 2015 US\$
<b>CHARGE FOR THE YEAR</b>		
Investment adviser fee	107,054	406,676
Administration fee	123,094	153,553
Directors' fees and expenses	149,216	152,450
<b>OUTSTANDING FEES</b>		
Investment adviser fee	8,363	7,039
Administration fee	10,800	9,777
Directors' fee	–	–

##### Shares held by related parties

The shareholdings of the Directors' in the Company were as follows:

Name	31 December 2016		31 December 2015	
	No. of ordinary shares	Percentage	No. of ordinary shares	Percentage
Claudio Albanese (Chairman)	9,697	0.01%	10,000	0.01%
Jon Bridel	9,697	0.01%	10,000	0.01%
Nigel Ward	19,393	0.01%	20,000	0.02%

As at 31 December 2016, the Investment Adviser, the General Partner and principals of the Investment Adviser and General Partner held an aggregate of 1,370,344 shares (31 December 2015: 1,197,987), which is 0.44% (31 December 2015: 0.56%) of the issued ordinary share capital.





## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 9. SHARE CAPITAL

The Company's ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares are recognised as a deduction in equity and are charged to the share capital account, including the initial set up costs.

The authorised share capital of the Company is represented by an unlimited number of ordinary shares of nil par value and have the following rights:

- (a) Dividends: Shareholders are entitled to receive, and participate in, any dividends or other distributions resolved to be distributed in respect of any accounting period or other period, provided that no calls or other sums due by them to the Company are outstanding.
- (b) Winding Up: On a winding up, the shareholders shall be entitled to the surplus assets remaining after payment of all the creditors of the Company.
- (c) Voting: Subject to any rights or restrictions attached to any shares, at a general meeting of the Company, on a show of hands, every holder of voting shares present in person or by proxy and entitled to vote shall have one vote, and on a poll every holder of voting shares present in person or by proxy shall have one vote for each share held by him, but this entitlement shall be subject to the conditions with respect to any special voting powers or restrictions for the time being attached to any shares which may be subject to special conditions. Refer to the Memorandum and Articles of Incorporation for further details.
- (d) Buyback: The Company may acquire its own shares (including any redeemable shares). Any shares so acquired by the Company may be cancelled or held as treasury shares provided that the number of shares of any class held as treasury shares must not at any time exceed any limitation set out in Guernsey company law. Any shares acquired in excess of this limit shall be treated as cancelled.

The C share capital of the Company is represented by a maximum of 200 million C shares of nil par value and have the following rights:

- (a) Dividends: Holders of C shares shall be entitled to receive, and participate in, any dividends declared only insofar as such dividend is attributed, at the sole discretion of the Directors, to the C share surplus of that class. The holders of ordinary shares, which shall arise after conversion of any C shares in issue, shall rank in full for all dividends and other distributions declared, made or paid after conversion and otherwise pari passu with the ordinary shares in issue at the time of conversion.
- (b) Winding Up: On a winding up or return of capital prior to conversion, the capital and assets of the Company shall be applied as follows:
  - (i) the ordinary share surplus shall be divided amongst the holders of ordinary shares according to the rights attaching thereto as if the ordinary share surplus comprised the assets of the Company available for distribution; and
  - (ii) the C share surplus attributable to each class of C shares shall be divided amongst the holders of such class pro rata according to their holdings of C shares of that class.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 9. SHARE CAPITAL continued

(c) Voting: The C shares shall carry the right to receive notice of, and to attend or vote at, any general meeting of the Company in the same manner as the ordinary shares (notwithstanding any difference in the respective NAV of the C shares and ordinary shares).

With effect from 25 August 2016, ordinary shares may be redeemed subject to the provisions of the Law and upon and subject to the following terms and conditions.

The Company shall have the right, at any time after the date of issue to redeem such number of ordinary shares as it shall, in its sole discretion, determine at the NAV of such shares applying at the valuation date and, in the case of partial redemption, proportionately in respect of each holding of ordinary shares.

The Company shall send to each shareholder a notice not less than 10 business days in advance of the relevant redemption date which will include details of the redemption, including:

- the redemption date;
- the total amount to be distributed;
- a statement that the redemption will be made at the net asset value of such shares;
- any additional information that the Directors deem necessary in connection with the proposed redemption including any necessary arrangements in respect of certificated shares.

Upon the redemption of an ordinary share being effected pursuant to the Articles the former holder thereof shall cease to be entitled to any rights in respect thereof (excepting always the right to receive a dividend which has become due and payable in respect thereof prior to such redemption being effected and to receive the proceeds of such redemption) and accordingly his name shall be removed from the Register with respect thereto.

Any ordinary share so redeemed will be treated as cancelled on redemption and the amount of the Company's share capital will be reduced accordingly.

### Issued Share Capital

Ordinary Shares

	31 December 2016		31 December 2015	
	Shares	US\$	Shares	US\$
Share capital at the beginning of the year	212,426,903	207,940,808	121,728,916	119,542,182
Share capital issued during the year	215,207	165,322	90,697,987	89,879,572
Conversion of C shares to ordinary shares during the year	108,019,980	100,273,000	–	–
Share redemptions	(9,723,520)	(9,266,171)	–	–
Share issue costs	–	–	–	(1,480,946)
Total share capital at the end of the year	<b>310,938,570</b>	<b>299,112,959</b>	<b>212,426,903</b>	<b>207,940,808</b>



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 9. SHARE CAPITAL *continued*

#### Issued Share Capital *continued*

*C shares*

	31 December 2016		31 December 2015	
	Shares	US\$	Shares	US\$
Share capital at the beginning of the year	101,800,000	100,273,000	–	–
Issued share capital	–	–	101,800,000	101,800,000
Conversion of C shares to ordinary shares during the year	(101,800,000)	(100,273,000)	–	–
Share issue costs	–	–	–	(1,527,000)
Total share capital at the end of the year	–	–	<b>101,800,000</b>	<b>100,273,000</b>

In August 2015, 101,800,000 C shares were issued at an issue price of 100 cents per C share for cash consideration.

The conversion ratio was 1.0611 ordinary shares for every one C share held as at close on the conversion record date of 26 January 2016. Entitlements to new ordinary shares were rounded down to the nearest whole share.

### 10. EARNINGS PER SHARE

	31 December 2016	31 December 2015
	<b>Number of ordinary shares</b>	<b>Number of ordinary shares</b>
Weighted average number of ordinary shares	310,756,998	189,598,173
Profit/(loss) for the financial year	US\$67,684,815	(US\$3,942,231)
Basic and diluted earnings/(loss) per ordinary share	<b>US\$0.2178</b>	<b>(US\$0.0208)</b>
	<b>31 December 2016</b>	<b>31 December 2015</b>
	<b>Number of C shares</b>	<b>Number of C shares</b>
Weighted average number of C shares	–	101,181,818
Loss for the financial period	–	(US\$4,313,298)
Basic and diluted loss per C share	–	<b>(US\$0.0426)</b>

The weighted average number of ordinary shares as at 31 December 2016 and 31 December 2015 is based on the number of ordinary shares in issue during the period under review, as detailed in note 9.

### 11. TRADE AND OTHER RECEIVABLES

	31 December 2016	31 December 2015
	US\$	US\$
Investment advisory fees payable (note 8)	8,363	7,039
Audit fees payable	61,752	53,293
Administration fees payable (note 8)	10,800	9,777
Sundry expenses payable	22,400	37,780
	<b>103,315</b>	<b>107,889</b>



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 12. RECONCILIATION OF ACCOUNTING NAV AND PUBLISHED NAV PER SHARE

	NAV US\$	Number of ordinary shares No.	NAV per ordinary share US\$
Published NAV	312,401,359	310,938,570	1.0047
Fair value adjustment	(717,464)	310,938,570	(0.0023)
Financial statements NAV	<b>311,683,895</b>	<b>310,938,570</b>	<b>1.0024</b>

At 31 December 2015, there was no difference between the Accounting NAV of the Company and the published NAV of the Company.

### 13. CONTINGENT LIABILITIES AND COMMITMENTS

The Company entered into a Subscription Agreement with the Master Fund and agreed to become a Limited Partner and made a commitment to the Master Fund of US\$306,327,883 (31 December 2015: US\$299,827,883).

At 31 December 2016 and 31 December 2015, the Company had no further outstanding commitments.

### 14. SUBSEQUENT EVENTS

On 4 January 2017, the Company declared a monthly dividend of 5.75075 US cents per ordinary share in respect of the month ended 31 December 2016, which was paid on 2 February 2017. The ex dividend date was 12 January 2017.

On 10 January 2017, the Company announced that following consultations with Shareholders, it intends to proceed with the proposals under which Shareholders will be offered an option (but will not have an obligation) to extend the duration of their investment, and also with a further equity raise through a C share.

On 3 February 2017, the Company declared a monthly dividend of 0.7 US cents per ordinary share in respect of the month ended 31 January 2017, which was paid on 28 February 2017. The ex dividend date was 16 February 2017.

On 3 March 2017, the Company declared a monthly dividend of 0.7 US cents per ordinary share in respect of the month ended 28 February 2017, which was paid on 30 March 2017. The ex dividend date was 16 March 2017.

On 9 March 2017, the Company published a prospectus and circular in relation to the reorganisation proposal, share issue proposal and name change proposal.

On 28 March 2017, the Company announced 47,428,202 ordinary shares have been elected for re-designation as 2014 shares at the Effective Date, representing 15.3% of the ordinary shares currently in issue. Consequently, 263,510,368 ordinary shares will be re-designated as 2017 shares, representing the balance of 84.7% of the ordinary shares currently in issue. Based on the above election results and the ordinary share price as at close of business on 27 March 2017, the 2017 share class would have an opening market capitalisation of approximately US\$262.2 million.

On 28 March 2017, the Company announced they have applied for 47,428,202 2014 shares and 263,510,368 2017 shares to be admitted to trade on the Specialist Fund Segment of the Main Market of the London Stock Exchange. Admission will be effective at 8 a.m. on 5 April 2017.

On 29 March 2017, a resolution was passed to change the Company's name from Fair Oaks Income Fund Limited to Fair Oaks Income Limited.

On 29 March 2017, the Company announced that at the Extraordinary General Meeting of the Company, all proposed resolutions were approved by shareholders.



## Notes to the Financial Statements (continued)

For the year ended 31 December 2016

### 14. SUBSEQUENT EVENTS *continued*

On 3 April 2017, the Company announced that the First Placing and Offer had raised US\$68.85 million. The Company has also applied for 68,850,000 C shares to be admitted to trade on the Specialist Fund Segment of the Main Market of the London Stock Exchange. Admission will be effective at 8 a.m. on 5 April 2017.

The Company intends to invest substantially all of the net issue proceeds in Master Fund II following admission, subject to retaining appropriate levels of liquidity for working capital purposes. At the level of the Company, the assets representing the net proceeds of the issue will be accounted for and managed as a separate pool of C share assets, distinct from the assets attributable to the 2017 shares until their date of conversion into 2017 shares and distinct from the assets attributable to the 2014 shares. It is currently anticipated that C shares issued pursuant to the issue will be converted into new 2017 shares (therefore merged with the existing 2017 share class) within 6 months from admission, although such conversion is entirely at the Directors' discretion.

On 3 April 2017, the Company declared a monthly dividend of 0.7 US cents per ordinary share in respect of the month ended 31 March 2017, which will be paid on 28 April 2017. The ex dividend date is 13 April 2017.

There were no other significant events since the period end which would require revision of the figures or disclosures in the Financial Statements.



# Management and Administration

## Directors

Claudio Albanese (Independent non-executive Chairman)  
Jon Bridel (Independent non-executive Director)  
Nigel Ward (Independent non-executive Director)

## Registered Office and Business Address

Sarnia House  
Le Truchot  
St Peter Port  
Guernsey GY1 1GR

## Investment Adviser

Fair Oaks Capital Limited  
67-68 Jermyn Street  
London SW1Y 6NY

## Legal Advisers in Guernsey

Carey Olsen  
Carey House  
Les Banques  
St Peter Port  
Guernsey GY1 4BZ

## Custodian and Principal Bankers

BNP Paribas Securities Services S.C.A.  
(appointed 15 December 2015)  
BNP Paribas House  
St Julian's Avenue  
St Peter Port  
Guernsey GY1 1WA

## Independent Auditor

KPMG Channel Islands Limited  
Gategny Court  
Gategny Esplanade  
St Peter Port  
Guernsey GY1 1WR

## Administrator and Secretary

Praxis Fund Services Limited  
Sarnia House  
Le Truchot  
St Peter Port  
Guernsey GY1 1GR

## Registrar

Capita Registrars (Guernsey) Limited  
Mont Crevelt House  
Bulwer Avenue  
St Sampson  
Guernsey GY2 4LH

## Legal Advisers in United Kingdom

Stephenson Harwood LLP  
1 Finsbury Circus  
London EC2M 7SH

## Bookrunner, Broker and Financial Adviser

Numis Securities Limited  
10 Paternoster Square  
London EC4M 7LT



