BARONSMEAD

Baronsmead VCT 2 plc

2008

Annual report & accounts
for the year ended
30 September 2008

Investment Objective

Baronsmead VCT 2 is a tax efficient listed company which aims to achieve long-term capital growth and generate tax-free dividends and capital distributions for private investors.

Investment Policy

- To invest primarily in a diverse portfolio of UK growth businesses, whether unquoted or traded on AiM.
- Investments are made selectively across a range of sectors in companies that have the potential to grow and enhance their value.

Further details on the investment policy and risk management are contained in the Directors' Report on pages 17 and 18.

Contents

Dividend policy

The Board of Baronsmead VCT 2 aims to sustain a minimum annual dividend level at an average of 5.5p per Ordinary Share, mindful of the need to maintain net asset value. The ability to meet these twin objectives depends significantly on the level and timing of profitable realisations and cannot be guaranteed. There will be variations in the amounts of dividends paid year on year.

Since launch, the average annual tax-free dividend paid to Shareholders has been 6.5p per share (equivalent to a pre-tax return of 9.6p per Ordinary Share for a higher rate tax payer). For Shareholders who claimed tax reliefs of 20 per cent. or 40 per cent., their returns would have been higher.

www.baronsmeadvct2.co.uk

Secondary market in the shares of Baronsmead VCT 2

Shares can be bought and sold using a stockbroker, just like shares in any other listed company. Qualifying purchasers (individuals over the age of 18 and UK resident for tax purposes) can receive VCT dividends (including capital distributions of realised gains on investments) that are not subject to income tax, and capital gains tax is not payable on disposal of the VCT shares.

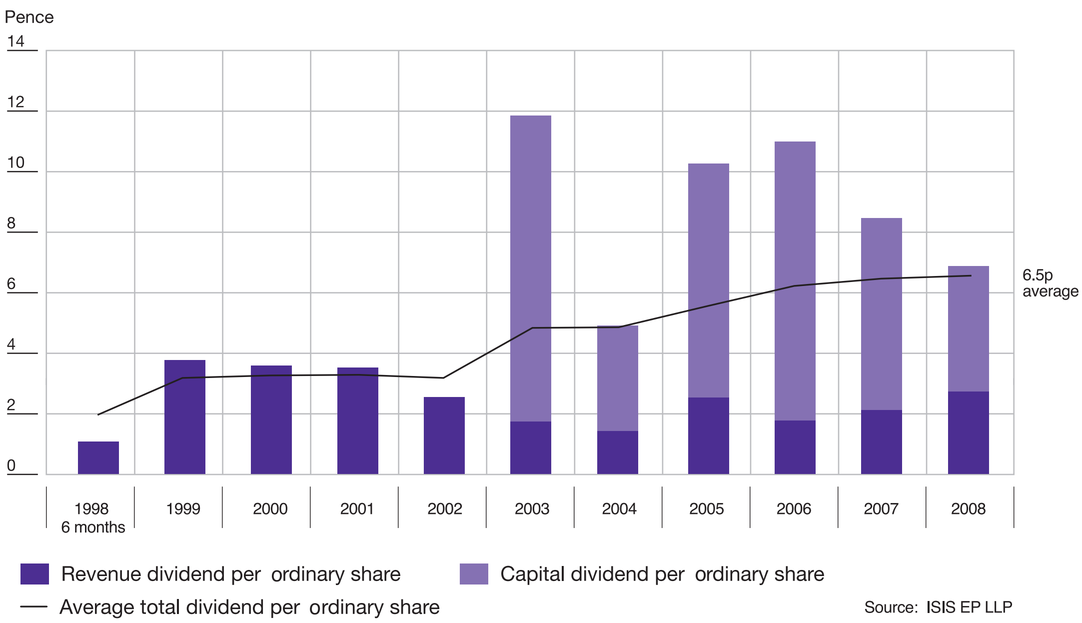
There is no minimum time for which VCT shares bought in the secondary market need to be held, and they can be sold in the normal way. The UK tax treatment of VCTs is on a first in first out basis and therefore tax advice should be obtained before shareholders dispose of their shares and also if they deferred Capital Gains Tax in respect of new shares acquired prior to 6 April 2004.

If you have sold or otherwise transferred all of your ordinary shares in Baronsmead VCT 2 plc, please forward this document and the accompanying form of proxy as soon as possible to the purchaser or transferee, or to the stockbroker, bank or other agent through whom the sale or transfer was, or is being, effected, for delivery to the purchaser or transferee.

Financial Highlights

–12.0%	**NAV per share decrease** to 98.68p before deduction of dividends. After payment of dividends totalling 7p per share in the year to 30 September 2008, the NAV was 91.68p. The FTSE All-Share index fell 25.12% over the same period.
84%	**NAV total return since launch** in 1998, representing an annualised total return of 6.0% (on original subscription at launch) before taking account of tax relief and 7.5% after allowing for initial income tax relief of 20%.
6.5p	**Average annual tax free dividend** of 6.5p per share since inception, equivalent to 9.6p for higher rate taxpayers.
£3.4m	**net capital profits** from 14 exits; **£11.8m new investment.**
£8m	**prospectus fund raising** launched in September 2008.

Dividend history since launch

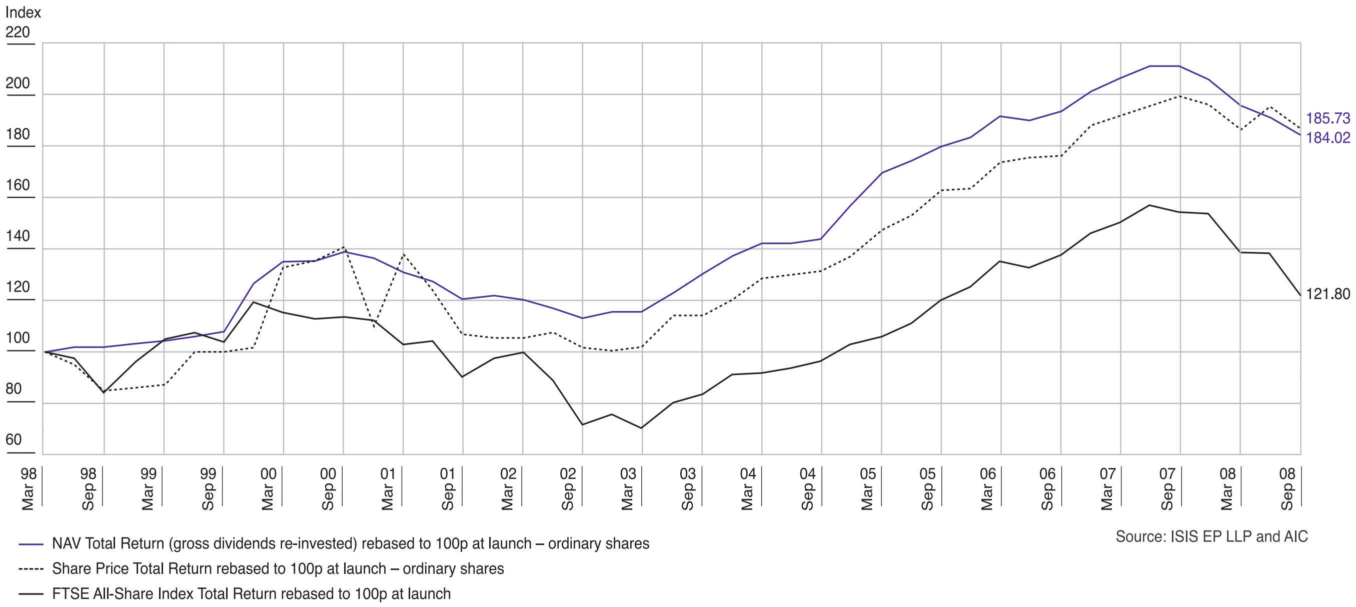


Source: ISIS EP LLP

Summary Since Launch

Baronsmead VCT 2 plc

Net asset value total return and share price total return since launch against the FTSE All-share Index total return



AIC methodology: The NAV total return to the investor, including the original amount invested (rebased to 100) from launch, assuming that dividends paid were re-invested at NAV of the Company at the time the shares were quoted ex-dividend. Transaction costs are not taken into account.

Performance Summary to 30 September 2008

Total return*	1 year %	5 year %	10 Year %	Since launch (2 April 1998) %
Net asset value†	(12.2)	+41.3	+80.4	+84.0
Share price†	(9.6)	+48.1	+91.2	+85.7
FTSE All-share	(22.3)	+44.5	+43.3	+21.8

* Source: ISIS EP LLP and AIC.
† These returns for Baronsmead VCT2 ignore up front tax reliefs and the impact of receiving dividends tax free.

Performance Record

As at 30 September 2008

Year ended	Total net assets £m	Ordinary Share: Net asset value p	Ordinary Share: Share price (mid) p	Ordinary Share: Net asset value total return* %	FTSE All-Share total return %	Combined total expense ratio† %
31/03/1999	9.50	95.65	85.0	104.44	105.06	2.90
31/03/2000	31.00	119.59	125.0	134.62	115.45	3.40
31/03/2001	45.00	112.30	125.0	130.66	103.02	3.10
31/03/2002	41.20	100.54	92.5	120.15	99.76	2.70
31/03/2003	36.70	89.65	80.0	115.49	70.02	2.70
31/03/2004	41.10	100.63	90.0	141.80	91.72	2.70
31/03/2005	69.60	116.92	100.5	168.70	105.99	2.70
31/03/2006	69.60	114.62	100.5	190.51	135.69	2.90
30/09/2007	68.70	112.19	101.0	209.62	154.89	3.00
30/09/2008	54.80	91.68	84.5	184.02	121.80	2.85

* Source: ISIS EP LLP.
† As a percentage of average total shareholders' funds (excluding performance fees).

Summary Since Launch

Dividends Paid Since Launch

As at 30 September 2008

Year ended	Revenue dividend p	Capital dividend p	**Total annual dividend p**	Cumulative dividends p	Average total annual dividend p
6 months to 30/09/1998	1.00	0.00	**1.00**	1.00	0.50
30/09/1999	3.80	0.00	**3.80**	4.80	3.20
30/09/2000	3.60	0.00	**3.60**	8.40	3.36
30/09/2001	3.50	0.00	**3.50**	11.90	3.40
30/09/2002	2.50	0.00	**2.50**	14.40	3.20
30/09/2003	1.70	10.20	**11.90**	26.30	4.78
30/09/2004	1.40	3.50	**4.90**	31.20	4.80
30/09/2005	2.50	7.70	**10.20**	41.40	5.52
30/09/2006	1.80	9.20	**11.00**	52.40	6.16
30/09/2007	2.10	6.40	**8.50**	60.90	6.41
30/09/2008	2.80	4.20	**7.00**	67.90	6.47

Cash Returned to Shareholders

The table below shows the cash returned to shareholders dependent on their subscription cost, including their income tax reclaimed on subscription.

Year subscribed	Subscription price p	Income tax reclaim p	Net cash invested p	Cumulative dividends paid p	Net annual yield* %	Gross equivalent yield† %
1998 (April) – Ordinary	100	20.0	80.0	67.9	8.1	12.0
1999 (May) – Ordinary	102	20.4	81.6	64.4	8.4	12.4
2000 (February) – Ordinary	137	27.4	109.6	61.2	6.4	9.5
2000 (March) – Ordinary	130	26.0	104.0	61.2	6.9	10.2
2004 (October) – C	100	40.0	60.0	19.9	8.3	12.3

C share dividend calculated using conversion ratio of 0.9657.

*Net annual yield represents the cumulative dividends paid expressed as a percentage of the net cash invested.

†The gross equivalent yield had the dividends been subject to higher rate taxation.

Chairman's Statement

Clive Parritt Chairman

The credit crunch which we faced in late 2007 has now become a major issue for UK smaller companies. Many small companies and most of our unquoted investees continue to trade satisfactorily. However market sentiment has deteriorated still further and this has materially reduced the value of the AiM companies in the portfolio and consequently our Net Asset Value per share.

Reducing valuation multiples also affected our unquoted investees and despite improving results, this part of the portfolio did not quite hold its overall value.

Despite the economic turmoil of the last year there was a satisfactory level of net profits from realisations which has enabled good dividends to be paid, while also generating capital for a high level of investment in 2008 and the future. The current prospectus fund raising will increase liquidity and the Board believes it will also place us in a good position to invest advantageously.

INVESTMENT PERFORMANCE

Results to 30 September 2008

In the 12 months to 30 September 2008, the Net Asset Value (NAV) per share decreased by 12.0% from 112.19p to 98.68p before payment of two interim dividends totalling 7p per share. These dividends include 2.8p per share generated from net revenue while the balance came from net realised capital profits. Over the same period the FTSE All-Share index fell by 25.12%.

The six VCT tests relating to the management of Baronsmead VCT 2 were met during the year. At the period end, 79.7% of the ordinary share capital raised prior to 30 September 2006 was invested in qualifying investments.

Longer term performance

Tax free Dividends paid to founder shareholders now total 67.9p per share. This is an average annual tax free dividend throughout the 10.5 year period of 6.5p per share. For those C shareholders who subscribed in winter 2004/2005, they have received 19.9p of tax-free dividends for each £1 invested.

The table on page 2 shows the total returns generated over 1, 5, 10 years and since launch compared against the FTSE All-Share index. The share price total return of Baronsmead VCT 2 is the most directly comparative.

These total returns are stated before the inclusion of VCT tax reliefs. These reliefs are designed to redress the VCT constraints as well as the higher risks associated with investing in smaller unquoted and AiM-traded companies.

The up front income tax reliefs over the years have been 20%, 40% and are now 30%, so any adjusted performance measure including this relief will vary depending on the date of subscription. The benefit from receiving dividends tax free is also sizeable and for a 'higher rate taxpayer' adds the equivalent of another 32.7p per share to the net dividend over the period for a founder shareholder.

THE IMPACT OF PRIVATE EQUITY

Portfolio trends

We value the unquoted portfolio by looking at comparable companies in the quoted markets and using their price/earnings ratios and multiples from comparable transactions. Despite the fall in these ratios, the 21 unquoted portfolio investments were only down 1.8%. Some companies were down rated but others performed strongly with a rise in profits which meant that the valuations of those companies more than offset the reduction in value. This can be observed best from the top ten investments on pages 12 and 13 where nine out of these ten all show year on year profits growth. In contrast the portfolio of 66 AiM investees suffered a severe fall in market value by 42% from their peak value in summer 2007. The Manager's report comments further on this phenomenon and shows how much of this is attributed to falling market confidence and how much to poorer trading by investees.

The private equity disciplines developed by ISIS over the last ten years have generated a series of successful realisations of unquoted investments. The oldest unquoted investment is now one made in 2004. The Board believes that this experience will be especially valuable as the economic situation gets tougher.

Chairman's Statement

Access to private equity

The Board aims to build the proportion of private equity in the portfolio recognising that

- VCTs enable private investors to access a selected diversified portfolio of private equity investments, tax efficiently.
- VCTs as fully listed companies on the London Stock Exchange provide high standards of investor transparency and protection.
- ISIS has a national resource seeking out selected entrepreneurial teams in chosen sectors that it is difficult for other investors to replicate across the UK.

Asset allocation

At the year end unquoted (private equity) investments represented 49% of NAV and this percentage is expected to continue increasing gradually as realisation opportunities at premium prices are likely to slow in the near term. However as we are likely to be well above the 70% VCT qualifying test this higher level of retention will enable the manager to more effectively manage the AiM portfolio when the opportunity arises. This higher weighting will also enable the Manager to sell AiM investments more actively once more confidence returns to the market and there is a rebound element in the pricing of these AiM holdings.

We continue to have a large pool of capital resources within the fund available for unexpected eventualities. A significant proportion of the cash available was raised prior to April 2006 so it can be used for larger qualifying investments with gross assets up to £15m pre-investment.

FUND RAISING AND INVESTMENT TIMING

Joint offer prospectus launched in September 2008

The Board's recommendation to raise additional capital was agreed by shareholders at the EGM held on 31 July 2008. The ensuing joint offer Securities Note was sent to all Shareholders in September aiming to raise up to £8m for each of Baronsmead VCT and Baronsmead VCT 2. The final closing date is 16 January 2009.

Subscriptions to date

The first allotment date takes place after the announcement of these results but by 10 November 2008 over 300 shareholders had subscribed approximately £4m of new capital to the joint offer to be split between Baronsmead VCT and Baronsmead VCT 2. The allocation price is non-dilutive to existing shareholders as it is based on the audited NAV per share at the year end adjusted for any subsequent change in the valuations as at 31 October 2008, rounded up by the launch cost of 5.5%.

Investment timing

One of the key messages in the Securities Note is ''the Directors and Manager believe that now is an advantageous time in the UK economic cycle to be investing in smaller companies. Prices of assets are expected to be lower and further funds are sought to enable investments in the attractive opportunities that are expected to arise''.

While no two economic cycles or recessions are the same, the investments made in the 2003 downturn provide an example of propitious timing. The six major investments acquired in 2003 were made at attractive prices and all have now been sold at an aggregate multiple of 2.7 times original cost of £6.4m. This generated realised profits of over £10.7m including interest and dividends received, even allowing for the disappointing multiple of 0.2 on cost realised from the investment in the Art Group.

MANAGING THROUGH RECESSIONS

The Board and Manager have experienced UK recessions both since our formation in 1998 and previously. Nonetheless there are always some surprises and on this occasion it has been the extent of the banking crisis in autumn 2008. The cash assets within Baronsmead VCT 2 are now held in Treasury Bills and Cash as it has never been the policy to take 'risk' with un-invested capital.

The nature of the credit crunch is such that we anticipate less banking finance being available for investees. This has been built into the Manager's plans for each unquoted investee for some time. We also wish to husband cash resources of Baronsmead VCT 2 for unexpected eventualities. There is a large pool of capital raised prior to April 2006 which can be invested in larger qualifying transactions and companies with gross assets of up to £15m pre investment. The current fund raising will supplement liquidity and also help us retain the high level of pre April 2006 capital.

Risk management

The Board manages all the risk dimensions associated with the Company through the framework established within the Combined Code for all fully listed public companies. At quarterly Board meeting all the key performance indicators

Chairman's Statement

are reviewed as well as wider topics which are spread annually across these meetings. In the current conditions we have paid particular attention to the diverse challenges facing the portfolio and to the security of the uninvested funds which have now been moved into Government securities.

OTHER ISSUES

VAT reclaim

It was announced in March 2008 that VAT is no longer to be charged on management fees from 1 July 2008. Subsequently HMRC confirmed that VAT paid by the Manager from a number of previous years could also be reclaimed and this is now being pursued. At this stage it is expected that a minimum of £740,000 will be recovered and is included in the NAV per share at 30 September 2008. These reclaims have resulted from the good work and representation by the Association of Investment Companies (AIC) that we joined as a member in October 2006.

Shareholder liquidity

An important risk that the Board monitors relates to share buy backs. Historically the repurchase price has represented an approximate discount to net asset value of 10 per cent and shareholders have been able to sell on this basis in normal market conditions. During the year, 3.0m shares were bought back. Another 0.6m shares were acquired under the Dividend Reinvestment Plan.

OUTLOOK

The availability of bank finance for investee companies has materially reduced and so these companies may have to be managed within their existing or shrinking credit lines. There is also increased economic risk that needs to be accommodated in the planning and financial control of investees. The Company has the cash resources to help in appropriate situations. However while the Manager is influential in its unquoted company relationships in this regard, it is less so with AiM-traded companies.

The priority for portfolio companies is to face any recessionary pressures in a controlled way and be strong enough not to be diverted from a growth path. In working with current and future investees the Manager will remain focused on these investment fundamentals.

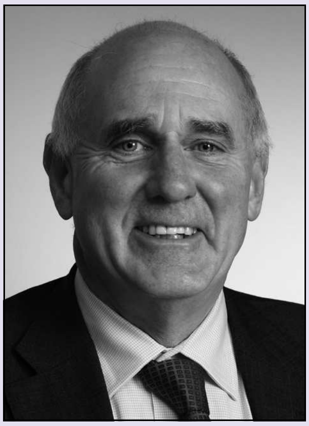
We can be selective in acquiring new investments at prices which are expected to be lower than in recent years. While the economic outlook is clearly difficult, the Board and the Manager both believe that attractive opportunities will arise to invest in businesses which have the resilience and flair to succeed. These prospective as well as existing investments provide the foundations on which we plan to both protect and then grow shareholder value in the years ahead.

Clive Parritt
Chairman

12 November 2008

Manager's Review

High levels of new investment and exits were achieved in the year under review. The priority in the coming year is to assist the existing portfolio companies to sustain profitable growth.



David Thorp
Investment Manager

Andrew Garside
Investment Manager

Het Marsh
Investment Manager

Prem Mohan Raj
Chief Financial Officer Funds

PORTFOLIO REVIEW

The total portfolio grew to 87 companies after 22 new investments, net of 14 realisations. All new investment and the exits are scheduled on page 9. £11.8m was invested in total, split £7.6m into nine unquoted investments and £4.2m into 21 AiM-traded investments.

The realisations are predominantly split between five successful unquoted exits and five AiM realisations for nominal amounts. The net realised profits from all these realisations totalled £3.4m.

Interest bearing securities and cash amounted to £18.1m at the start of the year and by 30 September 2008 totalled £13.6m. Shortly after the year end the holdings in money market OEICS were switched into Gilts and Treasury Bills leaving cash deposits of approximately £2m for immediate operational requirements. This structure will be reviewed regularly and some reversion back to higher yielding OEICs will be sought once financial markets are exhibiting more conventional behaviour.

The Portfolio companies are reviewed quarterly in terms of their financial health and while there has been a fall in those companies exhibiting steady or better trading progress from 83% to 71% at the year end most investees are still performing satisfactorily. In addition financial gearing is measured as a ratio of debt to current enterprise value as well as the debt divided by operating profits. These ratios are currently at prudent levels both historically and against industry standards.

The severe AiM market de-rating over the last year has dented the AiM record as over the year price/earnings multiples broadly halved for both the AiM All Share and the FTSE SmallCap indices (*source: Blue Oar Securities*). This de-rating was partially offset by earnings growth within the majority of portfolio companies although there was an impact from some specific trading issues with five negative trading statements from portfolio companies arising in the final quarter. 21 out of 66 AiM and listed investees were categorised as ''Down'' in terms of direction of travel, whilst 24 and 21 were categorised as up and steady respectively.

Pages 14 and 15 of the annual report depict four case studies of unquoted companies across a number of different market sectors within the portfolio.

HOW PRIVATE EQUITY CAN WORK IN A DOWN TURN

Selection, active management and exiting

The banking crisis has been driven by bad debts, over borrowing and now a shortage of capital. Moreover trading conditions for companies during an economic recession could be more volatile. These aspects will be designed into new investment opportunities by keeping borrowing levels low and allowing greater financial flexibility should the unforeseen happen.

Manager's Review

The appointment of an external chairman and one or more non-executives directors to investee companies can instil good standards of governance and key decision-making. This is normally reinforced by the alignment between all the shareholders including the executive directors who are incentivised to grow and then sell their company.

Investment process

The Manager constantly strives to achieve greater consistency through all the stages of investing in a niche market opportunity where the investee has a value strategy that can be sustained through economic cycles.

The sale of two investments last year illustrates how active management by ISIS resolved difficulties whether managerial or due to a rapidly changing market environment.

- New executive management introduced by ISIS joined Hawksmere in 2005 and were able to sell the business in early 2008 at a multiple of 2.5 times cost, which was a sharp change in fortunes as the investment had been valued at zero in June 2006.
- The investment in Kidsunlimited was held for over six years during which time the day care market sector for small children changed markedly caused by both regulatory and legislative change. Senior management had to change and evolve its skills over this time and judge when best to sell, which was achieved in April 2008 at a multiple of 4.75 times cost.

Continuous learning

Over the 10 year life of Baronsmead VCT 2, 143 investments have been made and about 40 per cent have been realised. These outcomes enable ISIS to learn continuously how to invest more skilfully. The increased consistency of unquoted exits is testimony to this.

AiM investing

The intent is to apply private equity disciplines when possible in AiM investees. These inputs range from use of sector knowledge, prior contact before float as an unquoted company, board appointment introductions and experience of exits for similar unquoted companies. 73% of the value of the AiM portion of the portfolio is within 20 stocks and this will be where the focus will be for growth while the tail of investments is slowly reduced as market conditions allow.

Getting ready for the upswing

Pricing of unquoted and AiM investments has begun to adjust and reduce so that the Manager is confident that the next year or so will be an advantageous time to invest. Debt availability will also be lower but the investment terms can be adjusted to accommodate lower gearing.

Deal flow

ISIS sustains an active origination programme of building a dialogue prior to investment and this effort will not be diminished during the recession. For example we first met the founder directors of Playforce, a new investment completed in January 2008, two years previously and identified this as an interesting opportunity.

OUTLOOK

The turbulence in financial markets will take some time to settle down but our role will be to stick to our investment principles during the current uncertainty. Prior experience of managing in the downturn is helpful both within incumbent investee management and ISIS as private equity managers, which can help ensure portfolio companies exercise sufficient control over costs and sales. We shall also be seeking out new opportunities where the economic 'drivers' behind sales growth are sound and at keener pricing than for some time.

ISIS EP LLP
Investment Managers
12 November 2008

Manager's Review

New Investments

The new investment (including further rounds of financing) is set out below and totalled £11.8 million including six sizeable unquoted investments and 14 smaller AiM subscriptions averaging £246,000. Further round financings are included within the total amount invested and were spread over nine other investees.

Company	Location	Sector	Activity	Investment cost (£'000)
Unquoted investments				
Active Assistance	Sevenoaks	Healthcare	Provision of live-in care to spinally injured clients	679
Carnell Contractors	Penkridge	Business Services	Support service provider in the highways sector	1,499
CSC (World) Limited	Pudsey	IT Support Services	Software for structural engineers	1,606
Kidsunlimited	Wilmslow	Business Services	Daycare provider	113
Nexus Vehicle Holdings Limited	Leeds	Business Services	Vehicle rental broker	1,368
Occam DM Limited*	Bath	Business Services	Integrated data services	4
Playforce Holdings Limited	Wiltshire	Business Services	Provider of playground equipment	1,033
TVC Group Limited	London	Media	Broadcast public relations firm	1,233
Xention Discovery*	Cambridge	Healthcare	Developer of ion channel modulating drugs	65
Total Unquoted investments				**7,600**
AiM-traded investments				
Advanced Computer Software plc	London	IT Support Services	Consolidation of Healthcare IT businesses focused on primary care, particularly focused on patient record data management	525
Appian Technology plc*	Buckinghamshire	IT Support Services	Number plate recognition products	52
Brulines Holdings plc*	Stockton-On-Tees	Business Services	Pub management systems	58
Character Group plc*	New Malden	Media	Design, development and international distribution of toys and games	144
Cohort	Henley-On-Thames	Business Services	Services to the defence industry	178
Concateno*	London	Healthcare	Drug testing	71
Electric Word plc	London	Media	Specialist information business serving the sport and education sectors	17
Essentially Group plc	Jersey	Media	Sports marketing	240
Ffastfill plc*	London	IT Support Services	Trading platform software provider	85
FishWorks plc*	Bath	Consumer	Fishmongers and fish restaurants	46
Independent Media Distribution plc	London	IT Support Services	Media logistics	15
IS Pharma plc	Chester	Healthcare	Specialist hospital medicines group	246
Mission Marketing Group	London	Media	Marketing services agency	247
Optimisa	London	Media	Marketing services and strategic consultancy	298
Plastics Capital plc	London	Business Services	Specialist plastics products buy & build	473
Praesepe plc	London	Consumer	Gaming	525
Relax Group plc	Chesterfield	Consumer	IVA and debt management group	263
Research Now plc	London	Media	Online market research provider	263
Silverdell plc	Barking	Business Services	Asbestos removal, asbestos abatement and asbestos management firm	14
STM Group plc	Gibraltar	Business Services	Offshore trust and company administration services for high net worth individuals	140
Tasty plc*	London	Consumer	Restaurant chain	290
Total AiM-traded investments				**4,190**
Total Investment in the period				**11,790**

*Follow on investment

Realisations in the year to 30 September 2008

	First Investment date	Original Cost £'000	Total Proceeds £'000	Multiple return*
Unquoted investments				
Boldon James	June 2005	562	1,713	3.1
Hawksmere Group Limited	December 2003	942	2,098	2.5
Kidsunlimited	June 2001	481	2,281	4.7
RLA Media	December 2002	1,438	2,398	3.7
SLR Group Limited	September 2002	494	2,485	6.0
The Art Group	October 2003	1,576	–	–
Total Unquoted realisations		**5,493**	**10,975**	
AiM-traded investments				
Cantono plc	April 2005	375	19	0.1
Capcon Holdings plc	October 2001	137	6	–
Oxford Biomedica	April 2003	250	65	0.3
SSP Holdings	July 2007	36	46	1.3
Xpertise Group plc	November 2002	296	222	0.8
Ardana	August 2003	481	–	–
Business Direct Group	August 2004	443	–	–
Charterhouse Communications plc	November 1999	355	–	–
Total AiM-traded investments		**2,373**	**358**	
Total Investments		**7,866**	**11,333**	

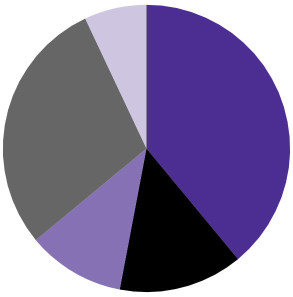
* Includes interest received and some earlier loan note redemptions.

Deferred proceeds were received for Domantis £174,000 and Oxxon Pharmaccines Ltd £3,900.

Investment Portfolio

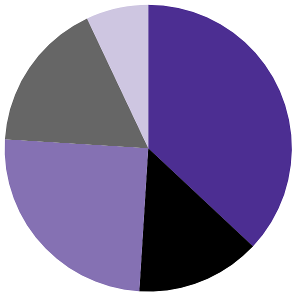
Investment Classification at 30 September 2008

By Sector



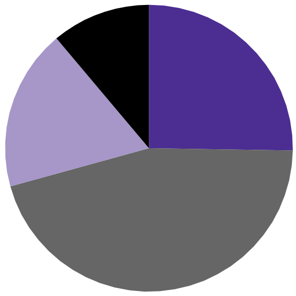
- Business services 39%
- Consumer markets 14%
- Healthcare 11%
- IT support services 29%
- Media 7%

Total Assets



- Unquoted – loan stock 36%
- Unquoted – ordinary and preference shares 13%
- AiM & Listed 25%
- Fixed interest 17%
- Net current assets 9%

Time Investments Held



- Less than 1 year 25%
- Between 1 and 3 years 46%
- Between 3 and 5 years 18%
- Greater than 5 years 11%

Deal name	Nature of business	Sum of book cost £'000	Sum of valuation £'000	Sum of % of net assets	Sum of % of equity held by legal entity	Sum of % of equity held by other funds*
Unquoted						
Scriptswitch	IT Support Services	1,167	2,718	5.0	7.2	25.4
Reed & Mackay	Business Services	1,211	2,557	4.7	9.3	29.9
Carnell Contractors	Business Services	1,499	1,878	3.4	8.3	29.3
Independent Living Services	Healthcare	801	1,861	3.4	14.4	46.1
CSC (World) Limited	IT Support Services	1,606	1,606	2.9	8.8	31.2
Kafevend Holdings Ltd	Consumer	1,247	1,602	2.9	15.4	49.6
CableCom Networking Holdings Ltd	IT Support Services	1,381	1,601	2.9	10.6	37.4
Fisher Outdoor Leisure Holdings Ltd	Consumer	1,423	1,461	2.7	10.5	33.6
Quantix Limited	IT Support Services	1,194	1,414	2.6	11.4	36.6
Crew Clothing Company Ltd	Consumer	933	1,398	2.6	5.9	19.1
Nexus Vehicle Holdings Ltd	Business Services	1,368	1,368	2.5	11.8	41.8
Credit Solutions	Business Services	1,031	1,323	2.4	8.6	28.4
TVC Group Limited	Media	1,233	1,233	2.2	6.4	22.6
Empire World Trade Limited	Business Services	1,297	1,126	2.1	7.1	22.9
Playforce Holdings Limited	Business Services	1,033	1,033	1.9	9.7	34.3
MLS	IT Support Services	781	965	1.8	5.3	17.2
Active Assistance	Healthcare	679	679	1.2	7.4	26.1
Occam DM Ltd	Business Services	465	575	1.0	5.4	13.8
Xention Discovery	Healthcare	277	277	0.5	1.0	4.0
Green Issues	Media	499	262	0.5	9.5	30.5
Kidsunlimited Group Ltd	Business Services	113	113	0.2	0.0	0.0
Total unquoted		**21,238**	**27,050**	**49.4**		
AiM						
Begbies Traynor Group plc	Business Services	263	1,071	2.0	0.7	2.2
Jelf Group plc	Business Services	551	996	1.8	1.3	3.9
IDOX plc	IT Support Services	920	960	1.8	2.8	4.8
Murgitroyd Group plc	Business Services	319	724	1.3	3.1	3.1
Staffline Recruitment Group plc	Business Services	249	594	1.1	4.5	4.5
Concateno plc	Healthcare	397	547	1.0	0.5	2.0
Praesepe plc	Consumer	525	477	0.9	1.4	6.7
Advanced Computer Software plc	IT Support Services	525	432	0.8	1.6	7.6
Driver Group plc	Business Services	438	426	0.8	2.4	8.7
Brulines Holdings plc	Business Services	348	404	0.7	1.2	5.2
Vero Software plc	IT Support Services	500	349	0.6	6.2	8.0
Mount Engineering plc	Business Services	385	341	0.6	2.3	10.6
Essentially Group Ltd	Media	495	330	0.6	1.5	7.8

Deal name	Nature of business	Sum of book cost £'000	Sum of valuation £'000	Sum of % of net assets	Sum of % of equity held by legal entity	Sum of % of equity held by other funds*
AiM (continued)						
Craneware plc	IT Support Services	179	321	0.6	0.6	2.3
Huveaux plc	Media	666	285	0.5	1.7	2.7
Plastics Capital plc	Business Services	473	284	0.5	1.8	8.3
InterQuest Group plc	Business Services	310	281	0.5	1.8	5.5
Research Now plc	Media	263	276	0.5	0.5	1.9
Stagecoach Theatre Arts plc	Consumer	419	270	0.5	4.6	4.6
Prologic plc	IT Support Services	310	228	0.4	4.1	10.9
Ffastfill plc	IT Support Services	216	227	0.4	0.8	3.5
Tasty plc	Consumer	356	225	0.4	1.7	11.3
Cohort plc	Business Services	179	214	0.4	0.3	1.1
IS Pharma plc	Healthcare	246	207	0.4	1.0	4.9
Sanderson Group plc	IT Support Services	387	194	0.4	1.8	5.3
Air Music & Media Group plc	Media	575	158	0.3	1.6	2.8
Appian Technology plc	IT Support Services	302	157	0.3	2.8	8.5
STM Group plc	Business Services	140	154	0.3	0.6	3.3
WIN plc	IT Support Services	263	150	0.3	1.3	3.6
Relax Group plc	Consumer	262	146	0.3	2.1	10.1
Quadnetics Group plc	Business Services	296	140	0.3	0.7	1.7
Proactis Holdings plc	IT Support Services	400	140	0.3	3.0	12.1
Adventis Group plc	Media	281	128	0.2	2.3	5.9
EG Solutions plc	IT Support Services	375	121	0.2	3.1	11.1
Colliers CRE plc	Business Services	470	114	0.2	0.9	1.8
Mission Marketing Group (The) plc	Media	247	113	0.2	0.6	0.9
RTC Group plc	Business Services	355	101	0.2	4.2	4.3
EBTM plc	Consumer	244	77	0.1	1.9	9.0
Claimar Care Group plc	Healthcare	569	73	0.1	1.4	5.5
Kiotech International plc	Healthcare	200	67	0.1	1.4	5.6
Character Group plc	Media	144	58	0.1	0.3	1.8
Brainjuicer Group plc	Media	50	57	0.1	0.4	1.5
Tangent Communications plc	Business Services	180	52	0.1	0.8	3.9
Autoclenz Holdings plc	Consumer	400	48	0.1	3.1	9.2
AorTech International plc	Healthcare	285	41	0.1	0.3	0.3
Optimisa plc	Media	298	41	0.1	1.5	7.3
FishWorks plc	Consumer	174	35	0.1	1.0	3.1
Universe Group plc	IT Support Services	195	27	0.1	0.7	1.4
IPT Holdings plc	Media	138	18	0.0	0.5	1.6
Payzone plc	Business Services	109	16	0.0	0.0	0.1
Landround plc	Business Services	467	16	0.0	1.7	1.7
INVU plc	IT Support Services	35	15	0.0	0.1	1.7
Real Good Food Company (The) plc	Consumer	620	14	0.0	0.7	1.6
Independent Media Distribution plc	IT Support Services	15	14	0.0	0.1	0.6
Electric Word plc	Media	17	11	0.0	0.2	1.2
Top Ten Holdings plc	Consumer	759	10	0.0	2.0	2.0
Cobra Biomanufacturing plc	Healthcare	210	10	0.0	0.6	0.0
MKM Group plc	Business Services	284	6	0.0	0.9	2.3
Zoo Digital Group plc	IT Support Services	438	5	0.0	0.3	0.8
Silverdell plc	Business Services	14	3	0.0	0.0	0.2
Higham Systems Services Group plc	IT Support Services	197	3	0.0	0.7	1.4
Loanmakers (Holdings) plc	Consumer	167	0	0.0	0.8	2.4
Conder Environmental plc	Business Services	607	0	0.0	7.4	7.4
Micap plc	Healthcare	372	0	0.0	0.3	0.4
Total AiM		**21,073**	**13,002**	**23.7**		
Listed						
Vectura Group plc	Healthcare	578	558	1.0	0.4	1.0
Total listed		**578**	**558**	**1.0**		
PLUS						
Chemistry Communications Group plc	Business Services	500	95	0.2	3.1	3.1
Total PLUS		**500**	**95**	**0.2**		
Interest bearing securities						
JP Morgan Cash Market OEIC		4,773	4,773	8.7		
BlackRock Cash Market OEIC		4,713	4,713	8.6		
Total interest bearing securities		**9,486**	**9,486**	**17.3**		
Total investments		**52,875**	**50,191**	**91.6**		
Net current assets less creditors falling due after 1 year			**4,631**	**8.4**		
Net assets			**54,822**	**100.0**		

*Other Funds managed by the same Investment Manager, ISIS EP LLP.

Ten Largest Investments

The top ten investments by current value at 30 September 2008 illustrate the diversity and size of investee companies within the portfolio. This financial information is taken from publicly available information, which has been audited by the auditors of the investee companies.

1 SCRIPTSWITCH LIMITED Coventry — Prescription software

First Investment: May 2007
Cost: £1,167,000
Valuation: £2,718,000
Valuation basis: Discounted price earnings
Percentage of equity held: 7.2%

ScriptSwitch Limited provides an innovative prescribing software product to Primary Care Trusts ('PCTs'), which is then employed by GPs in their surgeries. ScriptSwitch is a unique medicines management tool that provides decision support to GPs and enables PCTs to save millions of pounds from their drugs budgets.

In May 2007, funding was provided to complete a £4.7 million secondary buy-out of ScriptSwitch.

Year ended 30 June	2007 £ million	2006 £ million
Sales	**2.1**	0.3
Profit/(loss) before tax	**0.9**	(0.4)
Profit/(loss) after tax	**0.7**	(0.4)
Net assets/(liabilities)	**0.4**	(0.3)

(Source: ScriptSwitch Limited audited Annual Report and Accounts 2007)

www.scriptswitch.com

2 REED & MACKAY LIMITED London — High quality business travel

First Investment: November 2005
Cost: £1,211,000
Valuation: £2,557,000
Valuation Basis: Discounted price earnings
Percentage of equity held: 9.3%

Reed & Mackay Limited is a provider of business travel management services to professional services firms and corporates. £5.0 million was raised in November 2005 to fund a replacement capital deal.

*Net assets fell due to a capital reorganisation.

Year ended 31 March	2007 £ million	2006 £ million
Income	**10.8**	9.4
Profit before tax	**2.8**	2.6
Profit after tax	**2.3**	2.0
Net assets*	**3.4**	8.2

(Source: Reed & Mackay Limited audited Annual Report and Accounts 2007)

www.reedmac.com

3 CARNELL CONTRACTORS LIMITED Penkridge — Providing support to the highways sector

First Investment: March 2008
Cost: £1,499,000
Valuation: £1,878,000
Valuation Basis: Discounted price earnings
Percentage of equity held: 8.3%

Carnell Support Services is a provider of specialist support and technology maintenance services to the Highways Agency road network. £6 million was invested in March 2008 to fund a replacement capital deal. Carnell currently employs over 115 people.

Year ended 30 September	2007 £ million	2006 £ million
Sales	**12.7**	7.7
Profit before tax	**2.0**	0.5
Profit after tax	**1.4**	0.3
Net assets	**2.3**	0.9

(Source: Carnell Contractors Limited audited Annual Report and Accounts 2007)

www.carnellcontractors.com

4 INDEPENDENT LIVING SERVICES (ILS) LIMITED Alloa — Acute domiciliary care

First Investment: September 2005
Cost: £801,000
Valuation: £1,861,000
Valuation Basis: Discounted price earnings
Percentage of equity held: 14.4%

Independent Living Services Limited (ILS) is one of the leading providers of acute domiciliary care to its local authority customers, mainly based in east Scotland.

The first investment in ILS was made in September 2005 and, further funding was provided in November 2006 to support its first acquisition, giving the enlarged group a stronger presence in the west of Scotland.

Year ended 30 September	2007 £ million	2006 £ million
Sales	**8.1**	6.8
Profit before tax	**1.3**	0.9
Profit after tax	**0.9**	0.7
Net assets	**2.9**	2.0

(Source: Independent Living Services (ILS) Limited audited Annual Report and Accounts 2007)

www.ilsscotland.com

5 CSC (WORLD) LIMITED Pudsey — Structural engineering software

First Investment: January 2008
Cost: £1,606,000
Valuation: £1,606,000
Valuation Basis: Cost
Percentage of equity held: 8.8%

CSC (World) is a developer and seller of software aimed at the international structural engineering market. In January 2008, £6.5 million was raised for a replacement capital investment.

Year ended 31 March	2007 £ million	2006 £ million
Sales	**6.5**	5.1
Profit before tax	**1.7**	1.1
Profit after tax	**1.2**	0.8
Net assets	**3.6**	2.7

(Source: CSC (World) Limited audited Annual Report and Accounts 2007)

www.cscworld.com

6 KAFÉVEND GROUP LIMITED Crawley

SME drinks vending

First Investment:	October 2005
Cost:	£1,247,000
Valuation:	£1,602,000
Valuation Basis:	Discounted price earnings
Percentage of equity held:	15.4%

Kafévend Group Limited is a leading drinks vending machine service provider to the SME market. £5 million was invested in October 2005 to fund a management buyout.

Kafévend employs over 70 people and operates from seven sites across the UK.

Year ended 30 September	2007	2006
	£ million	£ million
Sales	**14.4**	12.1
Profit before tax	**0.7**	0.3
Profit after tax	**0.6**	0.2
Net assets	**2.1**	1.5

(Source: Kafévend Group Limited audited Annual Report and Accounts 2007)

www.kafevending.co.uk

7 CABLECOM NETWORKING HOLDINGS LIMITED Clevedon

Internet access solutions

First Investment:	May 2007
Cost:	£1,381,000
Valuation:	£1,601,000
Valuation Basis:	Discounted price earnings
Percentage of equity held:	10.6%

Cablecom Network Holdings Limited is a provider of networking solutions to corporate clients and since 2003 has evolved into providing IT and communication managed services to high density multi-tenanted accommodation in the student and key worker sectors. In May 2007, £5.6 million was raised for a management buy-out.

Year ended 30 September	2007	2006
	£ million	£ million
Sales	**4.9**	4.3
Profit before tax	**1.2**	1.0
Profit after tax	**0.9**	0.8
Net assets	**2.0**	1.2

(Source: Cablecom Networking Holdings Limited audited Annual Report and Accounts 2007)

www.cablecomnetworking.co.uk

8 FISHER OUTDOOR HOLDINGS LIMITED St. Albans

Supplying the cycling industry

First Investment:	June 2006
Cost:	£1,423,000
Valuation:	£1,461,000
Valuation Basis:	Discounted price earnings
Percentage of equity held:	10.5%

Fisher Outdoor Holdings Limited has grown to be the strongest name in the supply of cycle accessories and components to the UK cycle trade. £5.6 million was invested to fund the Management buyout in June 2006. Fisher employs 80 staff distributing key branded and own label products.

Year ended 31 January	2007	2006
	£ million	£ million
Sales	**18.1**	15.4
Profit before tax	**2.5**	2.0
Profit after tax	**2.1**	1.4
Net assets	**7.7**	5.3

(Source: Fisher Outdoor Holdings Limited audited Annual Report and Accounts 2007)

www.fisheroutdoor.co.uk

9 QUANTIX LIMITED Nottingham

Outsourced database maintenance

First Investment:	March 2007
Cost:	£1,194,000
Valuation:	£1,414,000
Valuation Basis:	Discounted price earnings
Percentage of equity held:	11.4%

Quantix Limited operates in the fast growing niche area of IT Managed Services – more specifically, the outsourced support and maintenance of databases, applications and security. It offers consultancy and product sales to clients for technology partners including Oracle, Microsoft, Juniper, Surfcontrol and Checkpoint.

ISIS invested £4.8 million in the management buy-out of Quantix Limited from Lynx Plc in March 2007.

Year ended 30 September	2007	2006
	£ million	£ million
Sales	**6.2**	5.9
Profit before tax	**1.2**	1.1
Profit after tax	**0.9**	0.7
Net assets	**1.0**	0.1

(Source: Quantix Limited audited Annual Report and Accounts 2007)

www.quantix-uk.com

10 CREW CLOTHING HOLDINGS LIMITED London

Multi-channel clothing retailer

First Investment:	November 2006
Cost:	£933,000
Valuation:	£1,398,000
Valuation Basis:	Discounted price earnings
Percentage of equity held:	5.9%

Crew Clothing Holdings Limited is a branded multi-channel retailer of men's and women's clothing headquartered in Wandsworth, London.

In November 2006 funding was provided to complete a £3.75 million investment for a 25 per cent stake in the company.

Year ended 28 October	2007	2006
	£ million	£ million
Sales	**15.9**	13.3
Profit/(loss) before tax	**0.6**	0.8
Profit/(loss) after tax	**0.4**	0.6
Net assets	**1.0**	2.4

(Source: Crew Clothing Holdings Limited audited Annual Report and Accounts 2007 and Crew Clothing Co. Limited audited Annual Report and Accounts 2006)

www.crewclothing.co.uk

HOW ISIS REALISES VALUE FOR THE SHAREHOLDERS OF BARONSMEAD VCT 2 PLC

Baronsmead VCT 2 plc invests in a diverse portfolio of UK growth businesses, whether unquoted or traded on AiM, run by entrepreneurial managers. It is the growth aspirations of these companies and their track record that make them above average and out of the ordinary.

The following four examples show how the Manager's approach can lead to growth in the investment value over time. The ISIS selection criteria include:

- Ability to become a market leader in their chosen niche
- Management teams who can deliver profitable and sustained growth
- Company can become a premium asset attractive to multiple bidders on exit

ISIS seeks selective opportunities from its four UK offices through a combination of corporate finance advisers and direct approaches to attractive targets.

For the unquoted investments the ISIS team are active Board participants ensuring that strategy is clear, the business plan well thought through and the management resources are in place to deliver profitable growth. The intention is to build on the initial platform and grow the business so that it can become an attractive target able to be either sold or floated in the medium term.

REED & MACKAY

Reed and Mackay is a leading strategic business travel management company. Utilising i-Q, its in-house developed bespoke technology, the business deals with professional services firms and corporates providing them with comprehensive corporate wide business travel services. Key clients include global legal firms and insurance companies, who demand precise high quality services.

Reed and Mackay's skill in managing diverse and demanding clientele has set them apart from their peers. The majority of customers have come through word of mouth recommendation and more than half of customers have traded with the business for more than 5 years.

Following the replacement capital investment by ISIS in 2005, the business has shown the ability and confidence to accelerate its growth over the last three years. Key to the double digit earnings growth in each of the last three years the business has achieved has been the building of an expanded management team.

> "I've dealt with many travel companies over the years before I came to Skandia and can honestly say I've never experienced expertise, help, knowledge or patience such as Reed and Mackay on every call".
>
> *Skandia UK*

www.reedmac.com

"Confidence to Grow"

PLAYFORCE, Wiltshire

Playforce provides playground equipment to local authorities, parish councils and park authorities. To date, Playforce has been commissioned to design and install over 2,000 school playgrounds.

Launched in 1998, Playforce has developed over the last ten years into a market leader within a fragmented market. The Company has turnover in excess of £6m and employs 38 staff from its Wiltshire offices.

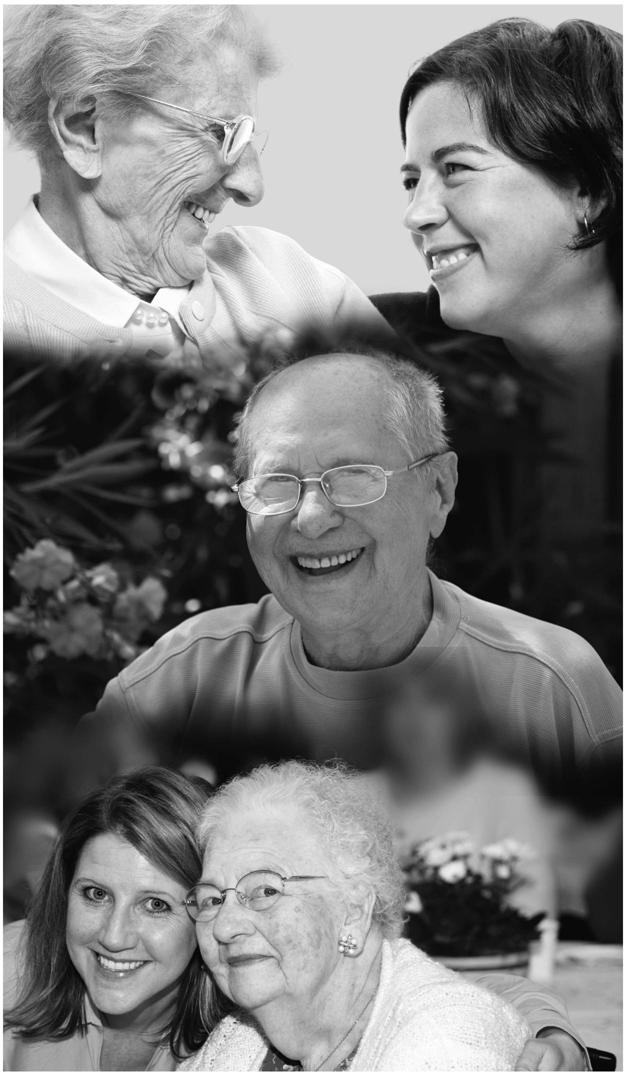
Growth has been recognised by several awards most notably by The Sunday Times Virgin Fast Track 100 which listed Playforce as the 61st fastest growing company in the UK with an annual compound growth rate of 77%.

Having identified the market opportunity, ISIS built up a two year relationship with the founders of Playforce before investing in January 2008. ISIS is working closely with the management team to invest to develop the company's capabilities and to support further growth.

www.playforce.co.uk

"Relationship and Opportunity"

Creating Shareholder Value



INDEPENDENT LIVING SERVICES

Independent Living Services is the leading independent provider of 'care at home' services in Scotland. Services are developed to support older and younger people living in the community with physical or learning disabilities. These services are delivered through partnership with local and health authorities, voluntary organisations and individuals.

ISIS was attracted to the care at home market in Scotland as it exhibits strong growth potential as provision of support is outsourced by local authorities and market supply remains relatively fragmented. ISIS completed its investment in September 2005. Since then ISIS has supported growth through a series of four acquisitions. This has resulted in an increased geographical presence in Scotland with the Company now working with eighteen local authorities in Scotland.

The combination of the 'buy and build' organic growth has resulted in the valuation rising to 2.3 times original cost of the investment.

www.ilsscotland.com

''Buy and Build''

SCRIPTSWITCH, Coventry

ScriptSwitch provides innovative prescribing software to healthcare organisations throughout the UK. The business was formed in 2003 and developed over a number of years by a team of skilled professionals (in conjunction with the NHS) from its University of Warwick base.

The ScriptSwitch software is a sophisticated medicines management tool that provides decision support to General Practitioners in prescribing medicines, whilst also quantifying and reporting on cost savings they are able to achieve.

Healthcare organisations are increasingly faced with budgetary challenges as the NHS is looking to reduce costs in prescribed pharmaceuticals. ScriptSwitch is well placed to support the NHS in achieving these objectives.

> ''In our area, the savings in our first year look set to be more than £100,000 from ScriptSwitch. As uptake improves and the database expands, this figure will rise''
>
> *Huntingdonshire Primary Care Trust*

Initially attracted by the market opportunity, ISIS have supported the business growth including the expansion of the management team, development of the product range and the move to new premises in Coventry. The valuation has risen to 2.3 times cost since investment in May 2007.

www.scriptswitch.com

''Investing in the business platform''

Board of Directors

as at 30 September 2008

Clive Parritt (Chairman)

Date of appointment 18 February 1998
(age 65) is a chartered accountant with over 30 years' experience of providing strategic, financial and commercial advice to medium sized businesses. Until February 2001 he was chairman of Baker Tilly having been its national managing partner for ten years until June 1996. He is a member of the Council and Board of the Institute of Chartered Accountants in England and Wales and chairman of BG Consulting Group Limited and DiGiCo Europe Limited. He is also a director of London & Associated Properties plc and F&C US Smaller Companies PLC. He specialises in corporate finance and was chief executive of a leading independent corporate finance house until July 2003. Previously he has chaired or been a director of a number of investment trusts, VCTs and media businesses. He is also a non-executive director of Baronsmead AIM VCT plc.

Godfrey Jillings
Date of appointment 18 February 1998
(age 68) is a non-executive chairman of Spring Studios and deputy chairman of Gladedale Holdings Ltd. He held a range of senior executive appointments at NatWest including responsibility for their retail stockbroking, unit trust and PEP operations. He was chief executive officer of FIMBRA, the regulatory body for IFAs and a deputy chief executive officer of its successor PIA (1990-1994). He was chairman of Ma Potter's until a successful trade sale last year and deputy chairman of DBS plc (1996-2002), the leading IFA network prior to its take-over and is also a director of Baronsmead VCT plc.

Gillian Nott (OBE)
Date of appointment 18 February 1998
(age 63) has led the Board of Baronsmead VCT and helped pioneer the investor relations activities with the Shareholders of Baronsmead VCT. Gill has in-depth experience of private investors as chief executive of ProShare (1994–1999). Previously she was responsible for the private equity portfolio at BP and has been on the board of the FSA. She is currently a non-executive director of investment trusts at Black Rock and Martin Currie and is chairman of Witan Pacific Investment Trust plc. She is also on the board of Liverpool Victoria Friendly Society, and a deputy chairman of the Association of Investment Companies. Gill is a non executive Director of Baronsmead VCT 2 and Baronsmead VCT 3.

Nicholas Timpson
Date of appointment 18 February 1998
(age 67) was the founder, chairman and managing director of Furnitureland Holdings plc. He is also a director of The Vestey Group Ltd. He brings to the Board long experience in the development of private companies. Before founding Furnitureland Holdings plc in 1973, he worked as a management consultant for McKinsey & Co.

As a fully listed Company, Baronsmead VCT 2 plc is required to comply with the Financial Reporting Council's Combined Code on Corporate Governance. This Code requires the Company to be headed by an effective Board of Directors who lead and control the Company's affairs.

The directors of a VCT and investment managers are required under the listing and continuing obligations of the London Stock Exchange to have sufficient and satisfactory experience in the management of a portfolio of unquoted investments of the size and type in which the VCT proposes to invest.

Report of the Directors

Results and Dividends

The Directors present the Eleventh Report and audited financial statements of the Company for the year ended 30 September 2008.

Ordinary Shares	£'000
Loss on ordinary activities after taxation	(8,533)
First interim dividend of 3p per ordinary share paid on 20 June 2008	(1,837)
Second interim dividend of 4p per ordinary share paid on 30 September 2008	(2,408)
Total dividends paid in year	(4,245)

Principal Activity and Status

The Company is registered as a Public Limited Company under the Companies Acts 1985 and 2006. The Directors have managed, and intend to continue to manage, the Company's affairs in such a manner as to comply with Section 274 of the Income Tax Act 2007 and the Company has received full approval as a Venture Capital Trust (VCT) from HM Revenue & Customs for the year to 30 September 2007. A review of the Company's business during the period is contained in the Chairman's Statement and Manager's Review.

Business Review

The purpose of this review is to provide shareholders with a summary setting out the business objectives of the Company, the Board's strategy to achieve those objectives, the risks faced, the regulatory environment and the key performance indicators (KPIs) used to measure performance.

Strategy for achieving objectives

Baronsmead VCT 2 plc is a tax efficient company listed on the London Stock Exchange's main market for listed securities.

Investment Objective

The investment objective of the Company is to achieve long-term capital growth and generate tax-free dividends and capital distributions for private investors.

Investment Policy

The Company's investment policy is to invest primarily in a diverse portfolio of UK growth businesses, whether unquoted or traded on AiM.

Investments are made selectively across a range of sectors in companies that have the potential to grow and enhance their value.

Investment securities

The Company invests in a range of securities including, but not limited to, ordinary and preference shares, loan stocks, convertible securities, and fixed-interest securities as well as cash. Unquoted investments are usually structured as a combination of ordinary shares and loan stocks, while AiM investments are primarily held in ordinary shares. Pending investment in unquoted and AiM-traded securities, cash is primarily held in an interest bearing money market open ended investment company (OEIC) and UK gilts.

UK companies

Investments are primarily made in companies which are substantially based in the UK, although many of these investees will trade overseas. The companies in which investments are made must have no more than £15 million of gross assets at the time of investment (or £7 million if the funds being invested were raised after 5 April 2006) to be classed as a VCT qualifying holding.

VCT regulation

The investment policy is designed to ensure that the Company continues to qualify and is approved as a VCT by HM Revenue and Customs. Amongst other conditions, the Company may not invest more than 15 per cent of its investments in a single company and must have at least 70 per cent by value of its investments throughout the period in shares or securities comprised in qualifying holdings, of which 30 per cent by value must be ordinary shares which carry no preferential rights. In addition, it must have at least 10 per cent by value of its total investments in any qualifying company in ordinary shares which carry no preferential rights.

Asset mix

The Company aims to be at least 90 per cent invested in growth businesses subject always to the quality of investment opportunities and the timing of realisations. Any un-invested funds are held in cash and interest bearing securities. It is intended that at least 75 per cent of any funds raised by the Company will be invested in VCT qualifying investments.

Risk diversification and maximum exposures

Risk is spread by investing in a number of different businesses within different industry sectors using a mixture of securities. The maximum amount invested in any one company is limited to £1 million in a fiscal year and generally no more than £2.5 million at cost is invested in the same company. The value of an individual investment is expected to increase over time as a result of trading progress and a continuous assessment is made of its suitability for sale.

Investment style

Investments are selected in the expectation that the application of private equity disciplines including an active management style for unquoted companies will enhance value and enable profits to be realised from planned exits.

Co-investment

The Company aims to invest in larger more mature unquoted and AiM companies and to achieve this it invests alongside the other Baronsmead VCTs. As such, at the time of initial investment, the combined investment can currently total up to a maximum of £6.5 million for unquoted and £4.4 million for AiM investees. Currently, ISIS EP LLP ('the Manager') and its executive members are mandated to invest in unquoteds alongside the Company on terms which align the interests of shareholders and the Manager.

Borrowing powers

The Company's Articles permit borrowing to give a degree of investment flexibility. The Company's policy is to use borrowing for short term liquidity purposes only.

Management

The Board has delegated the management of the investment portfolio to the Manager. The Manager also provides or procures the provision of company secretarial, administrative and custodian services to the Company.

The Manager has adopted a 'top-down, sector-driven' approach to identifying and evaluating potential investment opportunities, by assessing a forward view of firstly the business environment, then the sector and finally the specific potential investment opportunity. Based on its research, the Manager has selected a number of sectors that it believes will offer attractive growth prospects and investment opportunities. Diversification is also achieved by spreading investments across different asset classes and making investments for a variety of different periods.

The Manager's Review on pages 7 to 9 provides a review of the investment portfolio and of market conditions during the year.

Principal risks, risk management and regulatory environment

The Board believes that the principal risks faced by the Company are:

- Economic risk – events such as an economic recession and movement in interest rates could affect smaller companies valuations.
- Loss of approval as a Venture Capital Trust – the Company must comply with Section 274 of the Income Tax Act 2007 which allows it to be exempted from capital gains tax on investment gains. Any breach of these rules may lead to the Company losing its approval as a VCT, qualifying shareholders who have not held their shares for the designated holding period having to repay the income tax relief they obtained and future dividends paid by the Company becoming subject to tax. The Company would also lose its exemption from corporation tax on capital gains.
- Investment and strategic – inappropriate strategy, poor asset allocation or consistent weak stock selection might lead to under performance and poor returns to shareholders.
- Regulatory – the Company is required to comply with the Companies Acts, the rules of the UK Listing Authority and United Kingdom Accounting Standards. Breach of any of these might lead to suspension of the Company's Stock Exchange listing, financial penalties or a qualified audit report.
- Reputational – inadequate or failed controls might result in breaches of regulations or loss of shareholder trust.
- Operational – failure of the Manager's and administrator's accounting systems or disruption to its business might lead to an inability to provide accurate reporting and monitoring.
- Financial – inadequate controls might lead to misappropriation of assets. Inappropriate accounting policies might lead to misreporting or breaches of regulations.
- Market risk – investment in AiM traded, PLUS traded and unquoted companies by nature involve a higher degree of risk than investment in companies traded on the main market. In particular, smaller companies often have limited product lines, markets or financial resources and may be dependent for their management on a smaller number of key individuals. In addition, the market for stock in smaller companies is often less liquid than that for stock in larger companies, bringing with it potential difficulties in acquiring, valuing and disposing of such stock.
- Liquidity risk –The Company's investments may be difficult to realise. The fact that a share is traded on AiM does not guarantee its liquidity. The spread between the buying and selling price of such shares may be wide and thus the price used for valuation may not be achievable.
- Competitive risk –Retention of key personnel is vital to the success of the Company. Incentives to the Manager's key staff were recently strengthened.

The Board seeks to mitigate the internal risks by setting policy, regular review of performance, enforcement of contractual obligations and monitoring progress and compliance. In the mitigation and management of these risks, the Board applies rigorously the principles detailed in the Turnbull guidance. Details of the Company's internal controls are contained in the Corporate Governance and Internal Control sections on pages 19 to 21.

Performance and key performance indicators (KPIs)

The Board expects the Manager to deliver a performance which meets the twin objectives of achieving long term capital growth and generating tax-free dividends.

Performance, measured by dividends paid to shareholders and the change in NAV per share, is also measured against the FTSE All-Share Total Return Index. This index, as the widest measure of UK quoted equities, has been adopted as an informal benchmark. Investment performance, cash returned to shareholders and share price are also measured against the Company's peer group of six other generalist venture capital trusts. A review of the Company's performance during the financial period, the position of the Company at the period end and the outlook for the coming year is contained within the Chairman's statement on pages 4 to 6.

The Board assesses the performance of the Manager in meeting the Company's objective against the primary KPIs highlighted on pages 1 to 3 of this Report and Accounts.

Issue and Buy-Back of Shares

During the period the Company issued 1,539,377 ordinary shares of 10p each and raised net proceeds of £1,785,677.

During the period the Company bought back 3,021,770 ordinary shares to be held in Treasury, at a cost of £2,849,145.

Report of the Directors

These shares will not be sold at a discount wider than the discount prevailing at the time the shares were initially bought back by the Company. The Company holds 5,241,770 ordinary shares in Treasury representing 8.8 per cent of the issued share capital as at 12 November 2008.

Directors

Biographies of the Directors are shown on page 16.

As explained in more detail under Corporate Governance on pages 19 and 20, the Board has agreed that Directors who have held office for more than nine years will retire annually.

Accordingly, as all the Company's Directors have held office for a period of more than nine years, all Directors will retire by rotation at the forthcoming Annual General Meeting of the Company and, being eligible, offer themselves for re-election.

In accordance with Listing Rule (LR) 15.2.13, the Company should have no more than one Director who is also a Director of another company managed by the Manager (ISIS EP LLP). Transitional provisions are in place for Venture Capital Trusts and the Company must comply with LR 15.2.13 by 28 September 2010. Notwithstanding this, the Board has decided that Mrs G Nott who is a director of Baronsmead VCT plc and Baronsmead VCT 3 plc, Mr G Jillings who is a director of Baronsmead VCT plc, Mr Clive Parritt who is a director of Baronsmead AIM VCT plc and Mr N Timpson will seek annual re-election. As explained above, these Directors already seek annual re-election under the Combined Code.

The Board confirms that, following formal performance evaluations, the performance of each of the Directors continues to be effective and demonstrates commitment to the role; the Board believes that it is therefore in the best interests of shareholders that these Directors be re-elected.

The Directors who held office during the period, and their interests in the shares of the Company were:

	30 September 2008	30 September 2007
	Ordinary 10p shares	Ordinary 10p shares
Clive Parritt*	59,545	57,758
Godfrey Jillings	189,224	170,687
Gillian Nott	11,799	11,799
Nicholas Timpson	331,114	300,219
Total shares held	591,682	540,463

*Beneficial and family.

There have been no changes in the holdings of the Directors between 30 September 2008 and 12 November 2008.

No Director has a service contract with the Company.

All Directors are members of the Audit, Remuneration and Nomination Committees.

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditors are unaware; and each Director has taken all the steps that they ought to have taken as a Director to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Corporate Governance

Arrangements in respect of corporate governance, appropriate to a venture capital trust, have been made by the Board. The Board has considered the principles and recommendations of the Association of Investment Companies' Code of Corporate Governance issued in May 2007 ('AIC Code') by reference to the AIC Corporate Governance Guide for Investment Companies ('AIC Guide'). The AIC Code, as explained by the AIC Guide, addresses all the principles set out in Section 1 of the Combined Code on Corporate Governance issued by the Financial Reporting Council in July 2003 and revised in June 2006 ('the Combined Code'), as well as setting out additional principles and recommendations on issues which are of specific relevance to the Company.

The Board considers that reporting against the principles and recommendations of the AIC Code, and by reference to the AIC Guide (which incorporates the Combined Code) will provide better information to shareholders.

Except as disclosed below, the Company complied throughout the period with the recommendations of the AIC Code and the relevant provisions of Section 1 of the Combined Code. Since all the Directors are non-executive the provisions of the Combined Code in respect of the role of the chief executive are not relevant to the Company and, likewise, the provisions of the Combined Code relating to Directors' remuneration are not relevant except in so far as they relate specifically to non-executive Directors. For the reasons set out in the AIC Guide, and in the preamble to the Combined Code, the Board considers that these provisions are not relevant to the Company, being an externally managed venture capital trust. The Company has therefore not reported further in respect of these provisions.

In view of the requirement in the Articles of Association that all Directors retire by rotation, the Board considers that it is not appropriate for the Directors to be appointed for a specified term as recommended by principle 3 of the AIC Code and provision A.7.2 of the Combined Code. However, the Board has agreed that each Director will retire and, if appropriate, seek re-election after each three years' service, and annually after serving on the Board for more than nine years.

The Board consists solely of non-executive Directors of which Mr Parritt is Chairman and Mr Timpson is Senior Independent Director. All Directors are considered by the Board to be independent of the Company's Manager. Directors received an induction from the Manager on joining the Board, and all Directors receive other relevant training as necessary.

As explained earlier, Mr G Jillings and Mrs G Nott are directors of Baronsmead VCT plc, Mrs G Nott is also a Director of Baronsmead VCT 3 plc and Mr C Parritt is a Director of Baronsmead AIM VCT plc which are all managed by ISIS EP LLP. The Board does not consider that a Director's tenure reduces their ability to act independently. The Board believes that, as a whole, it comprises an appropriate balance of skills, experience and knowledge. It also

Report of the Directors

believes that each Director is independent in character and judgement and that there are no relationships or circumstances which are likely to affect the judgement of any Director.

The Company has no executive Directors or employees.

A management agreement between the Company and its Manager, ISIS EP LLP, sets out the matters over which the Manager has authority and the limits above which Board approval must be sought. All other matters, including strategy, investment and dividend policies, gearing, and corporate governance procedures, are reserved for the approval of the Board of Directors. The Board meets at least quarterly and receives full information about the Company's investment performance, assets, liabilities and other relevant information in advance of Board meetings. The Manager, in the absence of explicit instructions from the Board, is empowered to exercise discretion in the use of the Company's voting rights. All shareholdings are voted, where practicable, in accordance with the Manager's own corporate governance policy, which is to seek to maximise shareholder value by constructive use of votes at company meetings and by endeavouring to use its influence as an investor with a principled approach to corporate governance.

Throughout the period a number of committees have been in operation. The committees are the Audit Committee, the Management Engagement and Remuneration Committee and the Nomination Committee.

The Audit Committee, chaired by Mr Parritt, operates within clearly defined terms of reference and comprises the full Board. The Board has concluded that Mr Parritt, as the only qualified chartered accountant on the Board, is best suited for the role of chairman of the Audit Committee. The duties of the Audit Committee include reviewing the annual and interim accounts, the system of internal controls, the terms of appointment of the auditors together with their remuneration, and ensuring that auditor objectivity and independence is safeguarded in the provision of non audit services by the auditors. It also provides a forum through which the auditors may report to the Board of Directors and meets at least twice yearly.

The Management Engagement and Remuneration Committee, chaired by Mrs Nott, comprises the full Board and reviews the appropriateness of the Manager's appointment together with the terms and conditions thereof on a regular basis.

The Nomination Committee, chaired by Mr Jillings, comprises the full Board and is convened for the purpose of considering the appointment of additional Directors as and when considered appropriate. In considering appointments to the Board, the Nomination Committee takes into account the ongoing requirements of the Company and the need to have a balance of skills and experience within the Board.

During the period the performance of the Board, committees and individual Directors was evaluated through an assessment process, led by the Chairman. The performance of the Chairman was evaluated by the other Directors under the leadership of the Senior Independent Director.

The following table sets out the number of Board and Committee meetings held for the year to 12 November 2008 and the number of meetings attended by each Director.

	Board of Directors Held Attended	Audit Committee Held Attended	Management Engagement and Remuneration Committee Held Attended	Nomination Committee Held Attended
Clive Parritt	5	2	1	1
Godfrey Jillings	5	2	1	1
Gillian Nott	4	2	1	1
Nicholas Timpson	4	2	1	1

Individual Directors may, at the expense of the Company, seek independent professional advice on any matter that concerns them in the furtherance of their duties. The Company maintains appropriate Directors' and Officers' liability insurance.

After making enquiries, and bearing in mind the nature of the Company's business and assets, the Directors consider that the Company has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Whistleblowing

The Board has considered the Combined Code's recommendations in respect of arrangements by which staff of the Manager or Secretary of the Company may, in confidence, raise concerns within their respective organisations about possible improprieties in matters of financial reporting or other matters. It has concluded that adequate arrangements are in place for the proportionate and independent investigation of such matters and, where necessary, for appropriate follow-up action to be taken within their respective organisations.

Relations with Shareholders

The Company welcomes the views of shareholders and places great importance on communication with its shareholders. The Chairman and other Directors are available to meet shareholders if required. The Annual General Meetings of the Company provides a forum both formal and informal, for shareholders to meet and discuss issues with the Directors and Manager of the Company. Details of the resolutions to be proposed at the forthcoming Annual General Meeting on 15 December 2008 can be found in the Notice of Meeting on page 40.

Internal Control

The Board is responsible for the Company's system of internal control and for reviewing its effectiveness. The Board has therefore established an ongoing process designed to meet the particular needs of the Company in managing the risks to which it is exposed, consistent with the Association of Investment Companies Corporate Governance Guide for Investment Companies. The process is based principally on the Manager's existing risk-based approach to internal control whereby a test matrix is created that identifies the key functions carried out by the Manager and other service providers, the individual activities undertaken within those functions, the risks associated with each activity and the controls employed to minimise those risks.

Report of the Directors

A residual risk rating is then applied. The test matrix is regularly updated and the Board is provided with regular reports highlighting all material changes to the risk ratings and confirming the action which has been, or is being, taken. A formal annual review of these procedures is carried out by the Audit Committee and includes consideration of internal control reports and similar reports issued by the Manager and other service providers.

Such review procedures have been in place throughout the financial period and up to the date of approval of the full Report and accounts and the Board is satisfied with their effectiveness. These procedures are designed to manage, rather than eliminate, risk and by their nature can provide reasonable, but not absolute, assurance against material misstatement or loss. The Board monitors the investment performance of the Company in comparison to a benchmark index and to comparable venture capital trusts at each Board meeting. The Board also reviews the Company's activities since the previous Board meeting to ensure that the Manager adheres to the agreed investment policy and approved investment guidelines and, if necessary, approve changes to such policy and guidelines.

The Board has reviewed the need for an internal audit function. The Board has concluded that the systems and procedures employed by the Manager, provide sufficient assurance that a sound system of 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.

Management

ISIS EP LLP manages the investments for the Company. From 1 January 2007, the liquid assets within the portfolio (being cash, gilts and other assets, which are not categorised as venture capital investments for the purpose of the FSA's rules) have been managed by FPPE LLP. This was a new limited partnership, which is authorised and regulated by the FSA and which has the same controlling members as the Manager. The Manager has continued to act as the manager of the Company and as the Investment Manager of the Company's illiquid assets (being all AiM-traded and other venture capital investments).

The personnel involved in providing management and investment management services to the Company has not changed as a result of the implementation of these arrangements.

The Manager will also provide or procure the provision of secretarial, administrative and custodian services to the Company. The management agreement may be terminated at any date by either party giving twelve months' notice of termination. Under the management agreement, the Manager receives a fee of 2.0 per cent per annum of the net assets of the Company.

In addition, the Manager receives an annual secretarial and accounting fee of £35,540, adjusted annually for movements in the UK Retail Price Index, plus a variable fee of 0.125 per cent of the net assets of the Company which exceed £5 million, subject to annual review. The annual secretarial and accounting fee is subject to a maximum of £106,000 per annum, excluding VAT adjusted annually for movements in the UK Retail Price Index.

Annual running costs are capped at 3.5 per cent of the net assets of the Company (excluding any performance fee payable to the Manager and irrecoverable VAT), any excess being refunded by the Manager by way of an adjustment to its management fee.

It is the Board's opinion that the continuing appointment of ISIS EP LLP on the terms agreed is in the best interests of shareholders as a whole.

Co-investment Scheme

The Co-investment Scheme requires that executive members of the Manager invest their own personal capital into twelve per cent of the ordinary shares of each and every unquoted investment excepting those life science transactions where ISIS EP LLP is not the lead investor. By 30 September 2008, a total of £483,127 had been invested in ordinary shares of 19 unquoted investments by 36 executives.

Shares held under the Scheme cannot be sold unless and until each investment held by the four Baronsmead VCTs is sold contemporaneously. Gains for the executives will only be achieved if the Baronsmead VCTs make gains from the underlying investment. If the executive leaves before the sale of the investment, they may miss out on much of the potential value inherent in their Co-investment shares. The Scheme is intended to help attract, recruit, retain and incentivise executive members of the Manager.

Procedures are in place whereby the Board receives quarterly updates from the Manager regarding the amounts committed by ISIS EP LLP under the terms of the Co-investment Scheme for each new unquoted investment. The Board also reviews the Co-investment Scheme arrangements at each quarterly valuation meeting. An open dialogue is maintained between the Board and the Manager regarding the operation of the Scheme.

Performance Incentive

A performance fee will not be payable to the Manager until the total return on shareholders' funds exceeds an annual threshold of base rate plus 2% calculated on a compound basis. To the extent that the total return exceeds the threshold of base rate plus 2% on shareholders' funds compounded over the relevant period then a performance fee (plus VAT) will be paid to the Manager of 20% of such excess to 31 March 2007, 16.66% to 31 March 2008, 13.33% to 31 March 2009 and 10% thereafter. The amount of any performance fee which is paid in an accounting period shall be capped at 5% of shareholders' funds for that period.

ISIS Equity Partners – Arrangement Fees

During the period to 30 September 2008, ISIS EP LLP received income of £203,298 (2007: £169,528) from investee companies in connection with arrangement fees, net of abort costs for six investee companies. This amount was paid by the investee companies.

Report of the Directors

VCT Status Adviser

The Company has retained PricewaterhouseCoopers LLP (PwC) as their VCT Tax Status Advisers to advise it on compliance with VCT requirements. PwC review new investment opportunities, as appropriate, and review regularly the investment portfolio of the Company. PwC work closely with the Manager but report directly to the Board.

Creditor Payment Policy

The Company's payment policy is to settle investment transactions in accordance with market practice and to ensure settlement of supplier invoices in accordance with stated terms.

The Company did not have any trade creditors at the period end.

Environment

The Company seeks to conduct its affairs responsibly and environmental factors are, where appropriate, taken into consideration with regard to investment decisions.

Auditors

KPMG Audit Plc have expressed their willingness to continue in office as auditors and a resolution proposing their appointment will be submitted at the forthcoming Annual General Meeting.

Substantial Interests in Share Capital

At 12 November 2008 the Company was not aware of any beneficial interests exceeding 3 per cent of the issued Ordinary Share capital.

Directors' Authority to Allot Shares, to Disapply Pre-emption Rights and to re-issue Treasury Shares

Shareholders gave authority at its Extraordinary General Meeting held on 31 July 2008 for Directors to offer existing shareholders the opportunity to add to their investment or to offer to potential shareholders an opportunity to invest in the Company in a tax efficient manner without the Company having to incur substantial costs and may be used, in part, to purchase ordinary shares in the market.

Treasury Shares

The Company currently holds 5,241,770 ordinary shares in Treasury. On 31 July 2008 the Board received authority from shareholders to re-issue ordinary shares out of Treasury at a discount to the prevailing NAV per ordinary share if the Board considers it in the best interest of the Company to do so. However, ordinary shares will never be re-issued out of Treasury at a discount wider than the discount prevailing at the time the shares were initially bought back by the Company.

The Company's brokers, currently provide a two way secondary market in the Company's shares. It is the Board's intention only to use the mechanism of re-issuing Treasury shares when demand for the Company's shares is greater than the supply available in the market place. Although shares re-issued from Treasury will not attract the 30 per cent initial income tax relief, all further dividends will be tax-free and if these shares are subsequently sold no capital gains tax will be payable by qualifying shareholders.

Directors' Authority to Purchase Shares

Shareholders gave authority at the Extraordinary General Meeting held on 31 July 2008 for the Company to make purchases of up to approximately 14.99 per cent of its issued share capital expiring at the end of the 2009 Annual General Meeting. The price paid for shares will not be less than the nominal value nor more than the maximum amount permitted by the rules of the UK Listing Authority in force at the time of purchase. This power will be exercised only if, in the opinion of the Directors, a repurchase would be in the best interests of shareholders as a whole. Any shares repurchased under this authority will either be cancelled or held in Treasury for future re-sale in appropriate market conditions.

Extension to the life of the Company

One of the main changes brought about by the Finance Act 2006 is that the holding period for investments moves from 3 years to 5 years from 6 April 2006. This means that in order for initial income tax relief not to be withdrawn, shareholders who subscribed after that date must hold their shares for 5 years from the date of investment. Shareholders gave approval at the Extraordinary General Meeting held on 31 July 2008 to extend the life of the Company to the annual general meeting falling after the fifth anniversary of the last allotment (from time to time) of shares by the Company.

Annual General Meeting

A notice for the Annual General Meeting of the Company to be held at 11.00 am on 15 December 2008 at the London Stock Exchange, 10 Paternoster Square, London EC4M 7LS is set out on the page 40. In addition to the ordinary business (all of which will be proposed as ordinary resolutions requiring the approval of more than 50% of the votes cast at the meeting) the following special business will be proposed.

By Order of the Board,

P M Forster

100 Wood Street
London EC2V 7AN

12 November 2008

Directors' Remuneration Report

The Board has prepared this report, in accordance with the requirements of Schedule 7A to the Companies Act 1985. An ordinary resolution for the approval of this report will be put to the members at the forthcoming Annual General Meeting.

The law requires the Company's auditors, KPMG Audit Plc, to audit certain of the disclosures provided. Where disclosures have been audited, they are indicated as such. The auditors' opinion is included in the 'Independent Auditors' Report'.

Board of Directors and their Fees

The Board which is profiled on page 16 consists solely of independent non-executive Directors and considers at least annually the level of the Board's fees, in accordance with the Combined Code on Corporate Governance. The Company Secretary provides information on comparative levels of Directors' fees to the Board in advance of each review.

The Board concluded following a review of the level of Directors' fees for the forthcoming year that the Chairman's and Directors' fees should remain the same.

The Remuneration Committee comprises C Parritt, G Jillings, G Nott and N Timpson. As the Company has no executive Directors, the Remuneration Committee meets, at least annually, to review the remuneration and terms of appointment of the Investment Manager.

Policy on Directors' Fees

The Board's policy is that the remuneration of non-executive Directors should reflect the experience of the Board as a whole, be fair and comparable to that of other relevant venture capital trusts that are similar in size and have similar investment objectives and structures. Furthermore the level of remuneration should be sufficient to attract and retain the Directors needed to oversee properly the Company and to reflect the specific circumstances of the Company, the duties and responsibilities of the Directors and the value and amount of time committed to the Company's affairs. It is intended that this policy will continue for the year ended 30 September 2009 and subsequent years.

Directors' service contracts

It is the Board's policy that Directors do not have service contracts, but new Directors are provided with a letter of appointment.

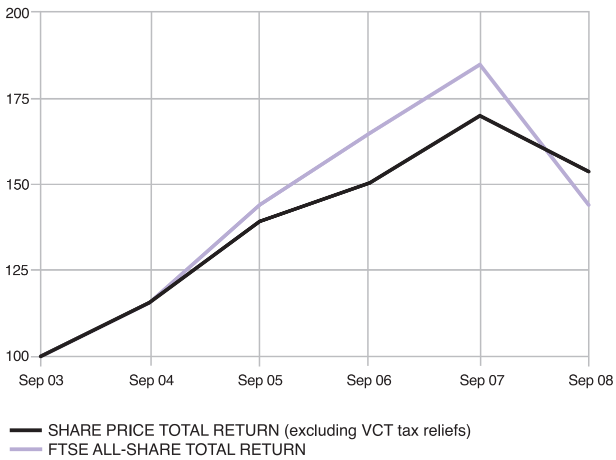
Director	Date of Original appointment	Due date for Re-election
C Parritt	18 February 1998	AGM 2008
G Jillings	18 February 1998	AGM 2008
G Nott	18 February 1998	AGM 2008
N Timpson	18 February 1998	AGM 2008

The terms of Directors' appointments provide that Directors should retire and be subject to re-election at the first Annual General Meeting after their appointment. Directors are thereafter obliged to retire by rotation, and to offer themselves for re-election by shareholders at least every three years after that. In accordance with the Combined Code on Corporate Governance, Directors who have served on the Board for more than 9 years must offer themselves for re-election on an annual basis. There is no notice period and no provision for compensation upon early termination of appointment.

Company performance

The Board is responsible for the Company's investment strategy and performance, although the management of the Company's investment portfolio is delegated to the Investment Manager through the investment management agreement, as referred to in the 'Report of the Directors'. The graph below compares for the five years ending 30 September 2008, the percentage change over each period in the total return (assuming all dividends are reinvested) to ordinary shareholders compared to the percentage change over each period in total shareholder return on a notional investment made up of shares of the same kind and number as those by reference to which the FTSE All-Share Index is calculated. This index was chosen for comparison purposes, as it represents a widely understood broad equity market index against which investors can measure the relative performance of the Company. An explanation of the performance of the Company is given in the Chairman's Statement and Manager's Review.

Ordinary Share price total return and the FTSE All-Share Index total return performance graph



Directors' emoluments for the Period (audited)

The Directors who served in the period received the following emoluments in the form of fees:

	Fees 2008 £	Fees* 2007 £
C Parritt	**21,000**	31,500
G Jillings	**14,000**	21,000
G Nott	**14,000**	21,000
N Timpson	**14,000**	21,000
Total	**63,000**	94,500

*18 month period.

Gillian Nott
Chairman of the Management Engagement and Remuneration Committee
12 November 2008

Statement of Directors' Responsibilities

Statement of Directors' Responsibilities in respect of the Annual Report and the Financial Statements

The Directors are responsible for preparing the Annual Report and the Financial Statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards (UK GAAP).

The financial statements are required by law to give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards (UK GAAP) 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 responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' Report (including Business Review), Directors' Remuneration Report and Corporate Governance Statement that comply with that law and those regulations.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Visitors to the website should be aware that legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Responsibility statement of the Directors in respect of the annual financial report

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company; and
- the Directors' Report includes a fair review of the development and performance of the business and the position of the issuer together with a description of the principal risks and uncertainties that they face.

On behalf of the Board,

Clive A Parritt
Chairman
12 November 2008

Independent Auditors' Report

Independent Auditors' report to the members of Baronsmead VCT 2 plc

We have audited the financial statements of Baronsmead VCT 2 plc for the year ended 30 September 2008 which comprise the Income Statement, the Balance Sheet, the Reconciliation of Movements in Shareholders' Funds and the Cash Flow Statement and the related notes. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. 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 Auditors

The Directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the financial statements in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities on page 24.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion, the information given in the Directors' Report (including the Business Review) is consistent with the financial statements. The information given in the Directors' Report includes that specific information presented in the Business Review. We also report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We review whether the Corporate Governance Statement reflects the company's compliance with the nine provisions of the 2006 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the company's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of Audit Opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Directors' Remuneration Report to be audited.

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of the company's affairs as at 30 September 2008 and of its loss for the period then ended;
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

KPMG Audit Plc
Chartered Accountants
Registered Auditor
Edinburgh
12 November 2008

Balance Sheet

As at 30 September 2008

	Notes	2008 £'000	2007 £'000
Fixed assets			
Investments	9	**50,191**	67,440
Current assets			
Debtors	10	**1,378**	690
Cash at bank and on deposit		**4,123**	1,167
		5,501	1,857
Creditors (amounts falling due within one year)	11	**(846)**	(505)
Net current assets		**4,655**	1,352
Total assets less current liabilities		**54,846**	68,792
Creditors (amounts falling due after one year)	12	**(24)**	(47)
Net assets		**54,822**	68,745
Capital and reserves			
Called-up share capital	13	**6,504**	6,350
Share premium account	14	**5,135**	3,563
Capital redemption reserve	14	**9,254**	9,254
Revaluation reserve	14	**(2,684)**	11,240
Profit and loss account	14	**36,613**	38,338
Equity shareholders' funds	15	**54,822**	68,745
Net asset value per share			
– Basic (59,794,245 shares)	15	**91.68p**	112.19p
– Treasury	15	**91.10p**	111.80p

The financial statements on pages 26 to 39 were approved by the Board of Directors on 12 November 2008 and were signed on its behalf by:

CLIVE A PARRITT FCA (Chairman)

The accompanying notes are an integral part of this balance sheet.

Income Statement

For the year ended 30 September 2008

	Notes	2008 Revenue £'000	2008 Capital £'000	2008 Total £'000	2007* Revenue £'000	2007* Capital £'000	2007* Total £'000
Unrealised (losses)/gains on investments		–	(10,241)	(10,241)	–	6,288	6,288
Realised (losses)/gains on investments		–	(105)	(105)	–	1,820	1,820
Income	2	2,834	–	2,834	3,474	–	3,474
Recoverable VAT	3	85	655	740	–	–	–
Investment management fee	4	(350)	(1,054)	(1,404)	(624)	(2,380)	(3,004)
Other expenses	5	(357)	–	(357)	(624)	–	(624)
Profit/(loss) on ordinary activities before taxation		2,212	(10,745)	(8,533)	2,226	5,729	7,954
Taxation on ordinary activities	6	(544)	544	–	(459)	459	–
Profit/(loss) on ordinary activities after taxation		1,668	(10,201)	(8,533)	1,767	6,187	7,954
Return per ordinary share							
Basic	8	2.73p	(16.68p)	(13.95p)	2.86p	10.02p	12.88p

The 'Total' column of this statement is the profit and loss account of the Company.

All revenue and capital items in this statement derive from continuing operations.

No operations were acquired or discontinued in the year.

Reconciliation of Movements in Shareholders' Funds

For the year ended 30 September 2008

	Notes	2008 Ordinary shares £'000	2007* Ordinary shares £'000	2007* C shares £'000	2007* Total £'000
Opening shareholders' funds at 30 September 2007		68,745	46,897	22,677	69,574
(Loss)/profit for period		(8,533)	5,513	2,441	7,954
Conversion of C shares		–	24,760	(24,760)	–
Purchase of shares for treasury		(2,850)	(1,159)	–	(1,159)
Issue of shares		1,786	–	–	–
Expenses for share issue/buybacks		(81)	(23)	(2)	(25)
Dividends paid	7	(4,245)	(7,243)	(356)	(7,599)
Closing shareholders' funds at 30 September 2008		54,822	68,745	–	68,745

* Comparative information represents an eighteen month accounting period.

The accompanying notes are an integral part of these statements.

Cash Flow Statement

As at 30 September 2008

	Notes	2008 £'000	2007* £'000
Operating activities			
Investment income received		**2,949**	2,746
Deposit interest received		**152**	237
Investment management fees		**(1,531)**	(3,784)
Other cash payments		**(358)**	(582)
Net cash inflow/(outflow) from operating activities	17	**1,212**	(1,383)
Capital expenditure and financial investment			
Purchases of investments		**(32,122)**	(31,030)
Disposals of investments		**38,917**	37,531
Net cash inflow from capital expenditure and financial investment		**6,795**	6,501
Dividends			
Equity dividends paid		**(4,251)**	(7,603)
Net cash inflow/(outflow) before financing		**3,756**	(2,485)
Financing			
Issue of shares		**1,786**	–
Expenses of the issue of shares		**(60)**	(25)
Buy-back of ordinary shares		**(2,526)**	(1,285)
Net cash outflow from financing		**(800)**	(1,310)
Increase/(decrease) in cash in the year/period		**2,956**	(3,795)
Opening cash position		**1,167**	4,962
Closing cash position		**4,123**	1,167

* Comparative information represents an eighteen month accounting period.

The accompanying notes are an integral part of this statement.

Notes to the Accounts

1. Accounting policies

(a) Basis of accounting

These financial statements have been prepared under UK Generally Accepted Accounting Practice (UK GAAP) and on the assumption that the Company maintains VCT status.

The Company is no longer an investment Company as defined by Section 266 of the Companies Act 1985, as investment Company status was revoked on 10 March 2003 in order to permit the distribution of capital profits.

The principal accounting policies adopted are set out below. Where presentational guidance set out in the Statement of Recommended Practice (''SORP'') for investment trusts issued by the Association of Investment Companies (''AIC'') in January 2003, revised December 2005, is consistent with the requirements of UK GAAP, the Directors have sought to prepare the financial statements on a basis compliant with the recommendations of the SORP.

Presentation of the Income Statement

In order to better reflect the activities of a VCT and in accordance with the SORP, supplementary information which analyses the income statement between items of a revenue and capital nature has been presented alongside the income statement. Net Revenue is the measure the Directors believe appropriate in assessing the Company's compliance with certain requirements set out in Section 274 of the Income Tax Act 2007.

(b) Valuation of investments

Purchases or sales of investments are recognised at the date of transaction.

Investments are valued at fair value. For quoted securities this is either bid price or the last traded price, depending on the convention of the exchange on which the investment is quoted.

In respect of unquoted investments, these are fair valued by the Directors in accordance with the following rules, which are consistent with the International Private Equity and Venture Capital (IPEVC) guidelines:

1. Investments are to be held at cost for a limited period only and not necessarily for a full 12 month period. The Company generally values new investments on an earnings basis when financial statements are available within the first 12 months of the investment being made.

2. Investments outwith the initial limited holding period are valued using an earnings multiple (at a discount to an appropriate stock market or comparable transaction multiple) in the absence of overriding factors. Where such factors apply, alternative methods of valuation will include application of an arm's length third party valuation, a provision on cost or a net asset basis.

Gains and losses arising from changes in the fair value of the investments are included in the Income Statement for the period as a capital item. Transaction costs on acquisition are included within the initial recognition and the profit or loss on disposal is calculated net of transaction costs on disposal.

(c) Income

Interest income on loan stock and dividends on preference shares are accrued on a daily basis. Provision is made against this income where recovery is doubtful. Where the terms of unquoted loan stocks only require interest to be paid on redemption, the interest is recognised as income once redemption is reasonably certain. Until such date interest is accrued daily and included within the valuation of the investment.

Income from fixed interest securities and deposit interest is included on an effective interest rate basis.

Dividends on quoted shares are recognised as income on the date that the related investments are marked ex dividend and where no dividend date is quoted, when the Company's right to receive payment is established.

(d) Expenses

All expenses are recorded on an accruals basis.

(e) Revenue/capital

The revenue column of the income statement includes all income and expenses. The capital column accounts for the realised and unrealised profit and loss on investments and the proportion of management fee charged to capital.

(f) Issue costs

Issue costs are deducted from the share premium account.

(g) Deferred taxation

Deferred taxation is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more, or the right to pay less, tax in future have occurred at the balance sheet date. This is subject to deferred tax assets only being recognised if it is considered more likely than not that there will be suitable profits from which the future reversal of the underlying timing differences can be deducted. Timing differences are differences arising between the Company's taxable profits and its results as stated in the financial statements which are capable of reversal in one or more subsequent periods.

Notes to the Accounts

2. Income

	2008 £'000	2007* £'000
Income from investments†		
UK franked	334	697
UK unfranked	1,987	2,461
Redemption premium	358	95
	2,679	3,253
Other income‡		
Deposit interest	155	221
Total income	2,834	3,474
Total income comprises:		
Dividends	334	697
Interest	2,500	2,777
	2,834	3,474
Income from investments:		
Listed and AiM securities	1,050	978
Unquoted securities	1,629	2,275
	2,679	3,253

* Comparative information represents an eighteen month accounting period.

†All investments have been designated fair value through profit or loss on initial recognition, therefore all investment income arises on investments at fair value through profit or loss.

‡Other income on financial assets not designated fair value through profit or loss.

3. Recoverable VAT

HM Revenue and Customs (HMRC) confirmed in October 2007, following the European Court of Justice decision in the JPMorgan Claverhouse case, that the provision of management services to investment trusts is exempt from VAT. Accordingly ISIS EP LLP ceased to charge VAT on management fees payable by the Company with effect from 30 June 2008.

On the basis of information supplied by ISIS EP LLP and discussions with the Company's professional advisors, the Directors consider it reasonably certain that the Company will in the foreseeable future obtain a repayment of VAT of not less than £740,000. This amount has been recognised as a separate item in the income statement, allocated between revenue and capital return in the same proportion as that in which the irrecoverable VAT was originally charged. It is possible that additional amounts of VAT will be recoverable in due course but the Directors are unable at this stage to quantify the sums involved.

Notes to the Accounts

4. Investment management fee

	2008 £'000	2007* £'000
Investment management fee	**1,404**	2,496
Performance fee	**–**	508
	1,404	3,004

For the purposes of the revenue and capital columns in the income statement, the management fee (including VAT) has been allocated 25 per cent to revenue and 75 per cent to capital, in line with the Board's expected long term return in the form of income and capital gains respectively from the Company's investment portfolio.

The management agreement may be terminated by either party giving 12 months' notice of termination. The Manager, ISIS EP LLP, receives a fee of 2 per cent per annum of the net assets of the Company, calculated and payable on a quarterly basis.

The Manager is entitled to a performance fee if at the end of any calculation period, the total return on shareholders' funds, calculated on a compound basis, exceeds the threshold of UK base rate plus 2 per cent on shareholders' funds. The Manager was entitled to 20 per cent of the excess prior to 31 March 2007 and will be entitled to 16.66 per cent to 31 March 2008, 13.33 per cent to 31 March 2009, and 10 per cent thereafter. The amount of any performance fee which is paid in respect of a calculation period shall be capped at 5 per cent of shareholders' funds at the end of the period.

ISIS EP LLP receives an annual secretarial and accounting fee (plus VAT) of £35,540 (uplifted annually for movements in the Retail Prices Index) and a variable fee of 0.125% on net assets over £5,000,000 subject to annual review. The secretarial and accounting fee is up to a maximum of £106,000 per annum, excluding VAT (uplifted annually for movements in the UK Retail Prices Index). It is chargeable 100 per cent to revenue.

Amounts payable to the Manager at the period end are disclosed in note 11.

5. Other expenses

	2008 £'000	2007* £'000
Directors' fees	**63**	95
Secretarial and accounting fee	**126**	176
Remuneration of the auditors and their associates:		
– audit	**20**	16
– other services supplied pursuant to legislation (interim review)	**4**	7
– other services supplied relating to taxation	**6**	5
Trail Commission	**–**	93
Other	**138**	232
	357	624

* Comparative information represents an eighteen month accounting period.

The Chairman receives £21,000 per annum (2007: £21,000). Each of the other Directors receives £14,000 per annum (2007: £14,000).

The Audit Committee reviews the nature and extent of non-audit services to ensure that independence is maintained. The Directors consider that the auditors were best placed to provide such services.

All figures include irrecoverable VAT, where applicable. The Company is not registered for VAT.

Notes to the Accounts

6a. Tax on ordinary activities

	2008 £'000	2007* £'000
UK corporation tax	–	–

The income statement shows the tax charge allocated between revenue and capital.

6b. Factors affecting tax charge for the year

The tax charge for the period is lower than the standard rate of corporation tax in the UK for a company (blended rate 29 per cent). The differences are explained below:

	2008			2007*		
	Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
(Loss)/profit on ordinary activities before taxation	2,212	(10,745)	(8,533)	2,226	5,728	7,954
Corporation tax at blended rate of 29%	641	(3,116)	(2,475)	668	1,718	2,386
Effect of:						
Non-taxable dividend income	(97)	–	(97)	(209)	–	(209)
Non-taxable (gains)/losses	–	3,000	3,000	–	(2,432)	(2,432)
Losses carried forward/(utilised)	–	(428)	(428)	–	255	255
Tax charge/(credit) for the period/year	544	(544)	–	459	(459)	–

At 30 September 2008 the Company had surplus management expenses of £1,358,000 (30 September 2007: £2,837,000) which have not been recognised as a deferred tax asset. This is because the Company is not expected to generate taxable income in a future period in excess of the deductible expenses of that future period and, accordingly, the Company is unlikely to be able to reduce future tax liabilities through the use of existing surplus expenses. Due to the Company's status as a VCT, and the intention to continue meeting the conditions required to obtain approval in the foreseeable future, the Company has not provided deferred tax on any capital gains and losses arising on the revaluation or disposal of investments.

7. Dividends

	2008			2007*		
	Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
Amounts recognised as distributions to equity holders in the year/period:						
For the year ended 30 September 2008						
– First interim dividend of 3.0p per ordinary share paid on 20 June 2008	1,102	735	1,837	–	–	–
– Second interim dividend of 4.0p per ordinary share paid on 30 September 2008	602	1,806	2,408	–	–	–
For the period ended 30 September 2007						
– First interim dividend of 5.0p per ordinary share paid on 20 December 2006	–	–	–	282	1,730	2,012
– First interim dividend of 1.6p per C share paid on 20 December 2006	–	–	–	178	178	356
– Second interim dividend of 5.0p per ordinary share paid on 30 March 2007	–	–	–	–	3,086	3,086
– Third interim dividend of 3.5p per ordinary share paid on 28 September 2007	–	–	–	1,287	858	2,145
	1,704	2,541	4,245	1,747	5,852	7,599

* Comparative information represents an eighteen month accounting period.

Notes to the Accounts

8. Returns per share

The (13.95)p return per ordinary share (2007: 12.88p return per ordinary share) is based on the net loss from ordinary activities after tax of (£8,533,000) (2007: £7,954,000 profit for the ordinary shares) and on 61,138,930 ordinary shares (2007: 61,762,131), being the weighted average number of shares in issue during the period.

9. Investments

All investments are designated fair value through profit or loss at initial recognition, therefore all gains and losses arise on investments designated at fair value through profit or loss. Given the nature of the Company's investments the fair value gains recognised in these financial statements are not considered to be readily convertible to cash in full at the balance sheet date and therefore the movement in these fair values are treated as unrealised.

	2008 £'000	2007 £'000
Listed Investments	**558**	1,274
Interest bearing securities	**9,486**	16,929
Investments traded on AiM	**13,002**	18,433
Investments traded on PLUS	**95**	65
Unquoted investments	**27,050**	30,739
	50,191	67,440
Equity shares	**20,541**	32,796
Preference shares	**59**	891
Loan notes	**20,105**	16,824
Fixed income securities	**9,486**	16,929
	50,191	67,440

	Listed £'000	Interest bearing securities £'000	Traded on AiM £'000	Traded on PLUS £'000	Unquoted £'000	Total £'000
Opening book cost	1,310	16,918	18,546	500	18,926	56,200
Opening unrealised appreciation/(depreciation)	(36)	11	(113)	(435)	11,813	11,240
Opening valuation	1,274	16,929	18,433	65	30,739	67,440
Movements in the year:						
Purchases at cost	–	20,088	4,190	–	7,960	32,238
Sales – proceeds	(65)	(27,546)	(378)	–	(11,152)	(39,141)
– realised gains/(losses) on sales	(518)	14	43	–	356	(105)
Unrealised (losses)/gains realised during the year	(148)	11	(1,328)	–	5,148	3,683
Increase/(decrease) in unrealised appreciation	15	(10)	(7,958)	30	(6,001)	(13,924)
Closing valuation	558	9,486	13,002	95	27,050	50,191
Closing book cost	578	9,486	21,073	500	21,238	52,875
Closing unrealised appreciation/(depreciation)	(20)	–	(8,071)	(405)	5,812	(2,684)
	558	9,486	13,002	95	27,050	50,191

During the period the Company incurred brokerage costs on sales of £5,720 (2007: £6,890).

An analysis of material sales during the period is disclosed in the Manager's Review on page 9.

Notes to the Accounts

10. Debtors

	2008 £'000	2007 £'000
Amounts due from brokers	**222**	–
Prepayments and accrued income	**416**	690
Other debtors	**740**	–
	1,378	690

11. Creditors (amounts falling due within one year)

	2008 £'000	2007 £'000
Amounts due to brokers	**454**	–
Management and secretarial and accounting fees due to the Manager	**306**	433
Other creditors	**86**	72
	846	505

12. Creditors (amounts falling due after one year)

	2008 £'000	2007 £'000
Trail commission payable	**24**	47
	24	47

Notes to the Accounts

13. Called-up share capital

	£'000
Authorised:	
191,238,250 ordinary shares of 10p each	19,124
2,752,350 C shares of 50p each	1,376
	20,500
Allotted, called-up and fully paid:	
Ordinary shares	
63,496,638 ordinary shares of 10p each listed at 30 September 2007	6,350
1,539,377 ordinary shares of 10p issued during the period	154
65,036,015 ordinary shares of 10p each listed at 30 September 2008	6,504
2,220,000 ordinary shares of 10p each held in treasury at 30 September 2007	(222)
3,021,770 ordinary shares of 10p each repurchased during the period and held in treasury	(302)
5,241,770 ordinary shares of 10p each held in treasury at 30 September 2008	(524)
59,794,245 ordinary shares of 10p each in issue at 30 September 2008	5,980

Treasury shares

The Companies (Acquisition of Own Shares) (Treasury Shares) Regulations 2003 came into force on 1 December 2003 and allowed the Company to hold shares acquired by way of market purchase as treasury shares, rather than having to cancel them. Up to five per cent of each class of a Company's shares may be held in this way. Shareholders have previously approved a resolution permitting the Company to issue shares from treasury at a discount to the prevailing NAV if the Board considers it in the best interests of the Company to do so. However, treasury shares will not be sold at a discount wider than the discount prevailing at the time the shares were initially bought back by the Company. It is the Board's intention only to use the mechanism of re-issuing treasury shares when demand for the Company's shares is greater than the supply available in the market place. Such issues would be captured under the terms of the Prospectus Directive and subject to the annual cap of Euro 2.5 million on funds raised before requiring a full prospectus, although they would not be considered by HM Revenue & Customs to be new shares entitling the purchaser to initial income tax relief, and therefore shares are unlikely to be issued from treasury in the same year as a ''top up'' offer for subscription.

14. Reserves

	Share premium account* £'000	Capital redemption reserve* £'000	Revaluation reserve* £'000	Profit and loss account £'000
At 30 September 2007	3,563	9,254	11,240	38,338
Issue of shares	1,632	–	–	–
Repurchase of shares to be held in treasury	–	–	–	(2,850)
Expenses of share issue and buybacks	(60)	–	–	(15)
Reallocation of prior year unrealised gains	–	–	(3,683)	3,683
Net decrease in value of investments	–	–	(10,241)	10,241
Equity dividends paid	–	–	–	(4,251)
Retained profit for the period	–	–	–	(8,533)
At 30 September 2008	**5,135**	**9,254**	**(2,684)**	**36,613**

When the Company revalues its investments during the period, any gains or losses arising are credited/charged to the revaluation reserve unless any diminution in value is considered to be permanent, in which case it is charged to the profit and loss account. When an investment is sold any balance held on the revaluation reserve is transferred to the profit and loss account as a movement in reserves.

* These reserves are non-distributable.

Notes to the Accounts

15. Net asset value per share

The net asset value per share and the net asset values attributable to the ordinary shares at the period end are calculated in accordance with their entitlements in the Articles of Association and were as follows:

	Number of shares		Net asset value per share attributable		Net asset value attributable	
	2008 number	2007 number	2008 pence	2007 pence	2008 £'000	2007 £'000
Ordinary shares (basic)	**59,794,245**	61,276,638	**91.68p**	112.19p	**54,822**	68,745
Ordinary shares (treasury)	**65,036,015**	63,496,638	**91.10p**	111.80p	**58,918**	70,987

Basic net asset value per share is based on net assets at the period end, and on 59,794,245 (2007: 61,276,638) ordinary shares, being the respective number of shares in issue at the period end.

At the Extraordinary General Meeting held on 31 July 2008, shareholders renewed the existing authority to disapply pre-emption rights in relation to the allotment for sale from treasury of up to 10 per cent of the listed share capital. The Board is now permitted to sell treasury shares at a discount to the prevailing NAV. Therefore the Treasury net asset value per share as at 30 September 2008 is based on net assets at the period end, inclusive of the 5,241,770 ordinary shares held in treasury valued at middle market price (84.5p), and on 59,794,245 ordinary shares, being the number of ordinary shares listed at the period end.

The Treasury net asset value per share as at 30 September 2008 included ordinary shares held in treasury valued at the prevailing Net Asset Value.

16. Analysis of changes in cash

	2008 £'000	2007* £'000
Beginning of year	1,167	4,962
Net cash inflow/(outflow)	2,956	(3,795)
End of period	**4,123**	**1,167**

17. Reconciliation of net revenue before taxation to net cash inflow/(outflow) from operating activities

	2008 £'000	2007* £'000
(Loss)/profit on ordinary activities before taxation	**(8,533)**	7,954
Losses/(gains) in investments	**10,346**	(8,108)
(Increase)/decrease in debtors	**(465)**	(506)
(Decrease)/increase in creditors	**(136)**	(723)
Net cash inflow/(outflow) from operating activities	**1,212**	(1,383)

* Comparative information represents an eighteen month accounting period.

18. Contingencies, guarantees and financial commitments

There were no contingencies, guarantees or financial commitments of the Company as at 30 September 2008 (30 September 2007: nil).

Notes to the Accounts

19. Significant interests

There are no interests of 20% or more of any class of share capital.

Further information on the significant interests is disclosed on pages 10 and 11.

20. Financial instruments and associated risks

The Company's financial instruments comprise equity and fixed interest investments, cash balances and liquid resources. The Company holds financial assets in accordance with its investment policy to invest in a diverse portfolio of established and profitable UK unquoted companies and companies raising new share capital on AiM.

Fixed asset investments held (see note 9) are valued at fair value. For quoted securities this is either bid price or the last traded price, depending on the convention of the exchange on which the investment is quoted. In respect of unquoted investments, these are fair valued by the Directors (using rules consistent with IPEVC guidelines). The fair value of all other financial assets and liabilities is represented by their carrying value in the Balance sheet.

The Company's investing activities expose it to various types of risk that are associated with financial instruments and markets in which it invests. The most important types of financial risk to which the Company is exposed are market risk, credit risk and liquidity risk. The nature and extent of the financial instruments outstanding at the balance sheet date and the risk management policies employed by the Company are discussed overleaf.

21. Market risk

Market risk embodies the potential for both loss and gains and includes interest rate risk and price risk.

The Company's strategy on the management of investment risk is driven by the Company's investment objective as outlined in note 20. The management of market risk is part of the investment management process and is typical of private equity investment. The portfolio is managed in accordance with policies and procedures in place as described in more detail in the Report of the Directors on page 17 to 22, with an awareness of the effects of adverse price movements through detailed and continuing analysis, with an objective of maximising overall returns to shareholders. Investments in unquoted stocks and AiM traded companies, by their nature, involve a higher degree of risk than investments in the main market. Some of that risk can be mitigated by diversifying the portfolio across business sectors and asset classes. The Company's overall market positions are monitored by the Board on a quarterly basis.

Details of the Company's investment portfolio at the balance sheet date are disclosed in the schedule of investments set out on pages 10 and 11. An analysis of investments between debt and equity instruments is disclosed in note 9.

25 per cent (2007: 29 per cent) of the Company's investments are listed on the London Stock Exchange or traded on AiM. A 5 per cent increase in stock prices as at 30 September 2008 would have increased the net assets attributable to the Company's shareholders and the total profit for the year by £683,000 (2007: £989,000); an equal change in the opposite direction would have decreased the net assets attributable to the Company's shareholders and the total profit for the year by an equal amount.

49 per cent (2007: 45 per cent) of the Company's investments are in unquoted companies held at fair value. Valuation methodology includes the application of earnings multiples derived from listed companies with similar characteristics. Therefore the value of the unquoted element of the portfolio is also indirectly affected by price movements on the listed exchanges. A 5 per cent increase in the valuations of unquoted investments at 30 September 2008 would have increased the net assets attributable to the Company's shareholders and the total profit for the year by £1,353,000 (2007: £1,537,000); an equal change in the opposite direction would have decreased the net assets attributable to the Company's shareholders and the total profit for the year by an equal amount.

Notes to the Accounts

22. Interest rate risk

At 30 September 2008 no fixed rate (2007: £8,360,000) securities were held by the Company. As a result, the Company is not subject to exposure to fair value interest rate risk due to fluctuations in the prevailing levels of market interest rates.

The table below summarises weighted average effective interest rates for the fixed interest-bearing financial instruments:

	2008			2007		
	Total fixed rate portfolio £'000	Weighted average interest rate %	Weighted average time for which rate is fixed days	Total fixed rate portfolio £'000	Weighted average interest rate %	Weighted average time for which rate is fixed days
Fixed rate						
Fixed interest securities	–	–	–	8,360	5.0	159

Floating rate

When the Company retains cash balances, the majority of cash is ordinarily held on interest bearing deposit accounts and, where appropriate, within an interest bearing money market open ended investment company (OEIC). The benchmark rate with determines the interest payments received on interest bearing cash balances is the bank base rate which was 5.00 per cent as at 30 September 2008 (2007: 5.75 per cent).

	2008 £'000	2007 £'000
Floating rate		
OEIC	**9,486**	8,558
Cash on deposit	**4,123**	1,167

23. Credit 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 Investment Manager has in place a monitoring procedure in respect of counterparty risk which is reviewed on an ongoing basis. The carrying amounts of financial assets best represents the maximum credit risk exposure at the balance sheet date.

At the reporting date, the Company's financial assets exposed to credit risk amounted to the following:

	2008 £'000	2007 £'000
Investments in floating rate instruments	**9,486**	8,558
Cash and cash equivalents	**4,123**	1,167
Interest, dividends and other receivables	**416**	690
	14,025	10,415

23. Credit risk (continued)

Credit risk arising on fixed interest instruments is mitigated by investing in UK Government Stock.

Credit risk arising on floating rate instruments is mitigated by investing in a money market open ended investment company managed by Blackrock and JP Morgan. Credit risk on unquoted loan stock held within unlisted investments is considered to be part of market risk as disclosed in note 21.

Credit risk arising on transactions with brokers relates to transactions awaiting settlement. Risk relating to unsettled transactions is considered to be small due to the short settlement period involved and the high credit quality of the brokers used. The Board monitors the quality of service provided by the brokers used to further mitigate this risk.

All assets of the Company which are traded on a recognised exchange are held by JPMorgan Chase (JPM), the Company's custodian. The Board monitors the Company's risk by reviewing the custodian's internal control reports as described in the Report of the Directors on pages 20 and 21.

Substantially all of the cash held by the Company is held by JPM. The Board monitors the Company's risk by reviewing regularly JPM's internal control reports as previously described. Should the credit quality or the financial position of JPM deteriorate significantly the Investment Manager will move the cash holdings to another bank.

There were no significant concentrations of credit risk to counterparties at 30 September 2008 or 30 September 2007. No individual investment exceeded 8.7 per cent of the net assets attributable to the Company's shareholders at 30 September 2008 (2007: 12.4 per cent).

24. Liquidity risk

The Company's financial instruments include investments in unquoted companies which are not traded in an organised public market as well as AiM traded equity investments both of which generally may be illiquid. As a result, the Company may not be able to liquidate quickly some of its investments in these instruments at an amount close to their fair value in order to meet its liquidity requirements, or to respond to specific events such as deterioration in the creditworthiness of any particular issuer.

The Company's liquidity risk is managed on an ongoing basis by the Investment Manager in accordance with policies and procedures as described in the Report of the Directors on page 18. The Company's overall liquidity risks are monitored on a quarterly basis by the Board.

The Company maintains sufficient investments in cash and readily realisable securities to pay accounts payable and accrued expenses. At 30 September 2008 these investments were valued at £13,608,628 (2007: £18,095,898).

25. Related parties

Related party transactions include Management, Secretarial, Accounting and Performance fees payable to the Manager, ISIS EP LLP, as disclosed in notes 4 and 11, and fees paid to the Directors as disclosed in note 5. In addition, the Manager operates a Co-Investment Scheme, detailed in the Report of the Directors on page 21, whereby employees of the Manager are entitled to participate in certain unquoted investments alongside the Company.

Notice of Annual General Meeting

Notice is hereby given that the eleventh Annual General Meeting of Baronsmead VCT 2 plc (''the Company'') will be held at the London Stock Exchange, 10 Paternoster Square, London EC4M 7LS, on 15 December 2008 at 11.00 am for the purposes of considering and, if thought fit, passing the following resolutions which will be proposed as ordinary resolutions.

Ordinary business

1. That the Report and Accounts for the year ended 30 September 2008 be received.
2. That the Directors' Remuneration Report for the year ended 30 September 2008 be approved.
3. To re-elect Mr C A Parritt as a Director.
4. To re-elect Mr G Jillings as a Director.
5. To re-elect Mrs G Nott as a Director.
6. To re-elect Mr N G L Timpson as a Director.
7. To re-appoint KPMG Audit Plc, Chartered Accountants, as auditors and that the Directors be authorised to determine their remuneration.

By Order of the Board

P M Forster
Secretary
100 Wood Street
London EC2V 7AN
12 November 2008

1. No Director has a service contract with the Company.
2. To be entitled to attend and vote at the meeting (and for the purposes of the determination by the Company of the votes they may cast), Members must be registered in the Register of Members of the Company at 11.00 am on 13 December 2008 (or, in the event of any adjournment, 11.00 am on the date which is two days before the time of the adjourned meeting). Changes to the Register of Members of the Company after the relevant deadline shall be disregarded in determining the rights of any person to attend and vote at the meeting.
3. A member entitled to attend and vote at the meeting is entitled to appoint a proxy or proxies to attend, speak and vote on his or her behalf. A proxy need not also be a member, but must attend the meeting to represent you. Details of how to appoint the Chairman of the meeting or another person as your proxy using the proxy form are set out in the notes to the proxy form. If you wish your proxy to speak on your behalf at the meeting you will need to appoint your own choice of proxy (not the Chairman) and give your instructions directly to them.
4. To appoint more than one proxy, an additional proxy form(s) may be obtained by contacting the Company's registrars, Computershare Investor Services PLC, helpline on 0870 703 0137 or you may photocopy the proxy form. Please indicate in the box next to the proxy holder's name, the number of shares in relation to which they are authorised to act as your proxy. Please also indicate by ticking the box provided, if the proxy instruction is one of multiple instructions being given. All forms must be signed and should be returned together in the same envelope.
5. A reply paid form of proxy is enclosed with Shareholders' copies of this document. To be valid, it should be lodged with the Company's registrars, Computershare Investor Services PLC, The Pavilions, Bridgwater Road, Bristol BS99 6ZY so as to be received not later than 48 hours before the time appointed for the meeting or any adjourned meeting or, in the case of a poll taken subsequent to the date of the meeting or adjourned meeting, so as to be received no later than 24 hours before the time appointed for taking the poll.
6. In order to facilitate voting by corporate representatives at the meeting, arrangements will be put in place at the meeting so that (i) if a corporate shareholder has appointed the Chairman of the meeting as its corporate representative with instructions to vote on a poll in accordance with the directions of all of the other corporate representatives for that shareholder at the meeting, then on a poll those corporate representatives will give voting directions to the Chairman and the Chairman will vote (or withhold a vote) as corporate representative in accordance with those directions; and (ii) if more than one corporate representative for the same corporate shareholder has not appointed the Chairman of the meeting as its corporate representative, a designated corporate representative will be nominated, from those corporate representatives who attend, who will vote on a poll and the other corporate representatives will give voting directions to that designated corporate representative. Corporate shareholders are referred to the guidance issued by the Institute of Chartered Secretaries and Administrators on proxies and corporate representatives – www.icsa.org.uk – for further details of this procedure. The guidance includes a sample form of representation letter if the Chairman is being appointed as described in (i) above.
7. Appointment of a proxy will not preclude a member from subsequently attending and voting at the meeting should he or she subsequently decide to do so. You can only appoint a proxy using the procedures set out in these notes and the notes to the proxy form.

Shareholder Information and Contact Details

Enquiries

Shareholders should contact the following regarding queries:

Basic contact details, ie change of address, joining the DRIP, queries regarding share and tax certificates and bank mandate forms:

Computershare (Company Registrar)

www-uk.computershare.com/investor

Investors who hold ordinary shares in their own name can check their holdings on our Registrar's website www-uk.computershare.com. Please note that to access this facility investors will need to quote the reference number shown on their share certificate.

Alternatively, by registering for the Investors' Centre facility on Computershare's website, investors can view details of all their holdings for which Computershare is Registrar, as well as access additional facilities and documentation. Please see www.investorcentre.co.uk for further information.

Shareholder helpline

Tel: 0870 703 0137 (Calls charged at national rate).

The Shareholder Helpline is available on UK business days between Monday and Friday, 8.30 am to 5 pm. The helpline contains automated self-service functionality which is available 24 hours a day, 7 days a week. Using your Shareholder Reference Number which is available on your share certificate or dividend tax voucher, our self-service functionality will let you do the following things:

Automated functions

– confirm the latest share price

– confirm your current share holding balance

– confirm payment history

– order a change of address, dividend bank mandate or stock transfer form

e-mail: web.queries@computershare.co.uk

For information on asset allocations, dividend policies, investment process, DRIP mechanism, share price movements, the share price discount and selling shares:

ISIS EP LLP (the Investment Manager) at www.isisep.com

e-mail: michael.probin@isisep.com; paul.forster@isisep.com; margaret.barff@isisep.com

Tel: Michael Probin 020 7506 5796; Paul Forster 020 7506 5652; Margaret Barff 020 7506 5630.

The Baronsmead website (www.baronsmeadvcts.co.uk) links to helpful sites, contains details of the team and some case studies of investments.

Shareholder communication

The Board has a policy of regular and open communication with shareholders based around quarterly statutory reporting.

Electronic communication has been introduced following new legislation in the 2006 Companies Act and the Baronsmead VCT2 website is available at www.baronsmeadvct2.co.uk.

Shareholder Information and Contact Details

Share Price

The Company's ordinary shares are listed on the London Stock Exchange. The mid-price of the Company's ordinary shares is given daily in the *Financial Times* in the Investment Companies section of the London Share Service. Share price information can also be obtained from many financial websites.

Trading Shares

The Company's shares can be bought and sold in the same way as any other quoted company on the London Stock Exchange through a stockbroker.

Please call Michael Probin (020 7506 5796) or Paul Forster (020 7506 5652) if you or your adviser have any questions about this process.

Financial Calendar

15 December 2008	Eleventh Annual General Meeting
May 2009	Announcement and posting of interim report for the six months to 31 March 2009
November 2009	Announcement and posting of final results for year to 30 September 2009

There were 3,250 holders of Ordinary Shares as at 30 September 2008. Their shareholdings (including shares held in Treasury) are analysed as follows:

	Ordinary Shares			
Size of shareholding	Number of shareholders	Percentage of total number of shareholders	Number of shares	Percentage of shares
1–2,000	100	3.08	123,864	0.19
2,001–5,000	822	25.29	3,182,005	4.89
5,001–10,000	835	25.69	6,452,206	9.92
10,001–25,000	887	27.29	14,896,019	22.90
25,001–50,000	397	12.22	14,505,974	22.30
50,001–100,000	158	4.86	11,129,143	17.12
Over 100,000	51	1.57	14,746,804	22.68
Total	3,250	100.0	65,036,015	100.0

Additional Information

The information provided in this report has been produced in order for shareholders to be informed of the activities of the Company during the period it covers. ISIS EP LLP does not give investment advice and the naming of companies in this report is not a recommendation to deal in them.

Baronsmead VCT 2 plc is managed by ISIS EP LLP which is Authorised and regulated by the FSA. Past performance is not necessarily a guide to future performance. Stockmarkets and currency movements may cause the value of investments and the income from them to fall as well as rise and investors may not get back the amount they originally invested. Where investments are made in unquoted securities and smaller companies, their potential volatility may increase the risk to the value of, and the income from, the investment.

Corporate Information

Directors
Clive Anthony Parritt (Chairman)*
Godfrey Frank Jillings†
Gillian Nott OBE‡
Nicholas George Lawrence Timpson¶

Secretary
Paul Forster, FCIS

Registered Office
100 Wood Street
London EC2V 7AN

Investment Manager
ISIS EP LLP
100 Wood Street
London EC2V 7AN

Investor Relations
Michael Probin
Tel: 020 7506 5796

Registered Number
03504214

Website
www.baronsmeadvct2.co.uk

Registrars and Transfer Office
Computershare Investor Services PLC
PO Box 82
The Pavilions
Bridgwater Road
Bristol BS99 6ZZ
Tel: 0870 703 0137

VCT Status Adviser
PricewaterhouseCoopers LLP
1 Embankment Place
London WC2N 6RH

Auditors
KPMG Audit Plc
Chartered Accountants
Saltire Court
20 Castle Terrace
Edinburgh EH1 2EG

Solicitors
Martineau
No 1 Colmore Square
Birmingham B4 6AA

*Chairman of the Audit Committee
†Chairman of Nomination Committee
‡Chairman of Management Engagement and Remuneration Committee
¶Senior Independent Director

Summerhall Corporate 48380