

Annual report

Early Fund II

Beginning of the financial year: 1 January 2016

End of the financial year: 31 December 2016

Fund Management Company: AS SmartCap

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Auditor: AS PricewaterhouseCoopers

Main area of activity: Venture capital fund investing into Estonian small and medium-sized businesses, which focus on innovation, create and use modern technologies as well as develop new products and services, or into investment funds, the assets of which can be invested into businesses described above.

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MANAGEMENT REPORT

Early Fund II (hereinafter the “Fund”) is a closed-ended common investment fund formed on 20.02.2012. The Fund is a venture capital fund as set out in the § 254¹ of the Investment Funds Act (hereinafter “IFA”). The terms of the Early Fund II were registered by the Financial Supervision Authority on 1.08.2012.

The Fund is managed by AS SmartCap, registry code 12071991 (hereinafter the “SmartCap”), which operated until 10.03.2017 as a fund management company under the supervision of the Financial Supervision Authority and since 10.03.2017 continues operating as a small fund manager set out in the clause (5) 5) of § 306 of the Investment Fund Act. SmartCap is a 100% subsidiary of Estonian Development Fund (in liquidation) (hereinafter “EDF”).

The Fund is established for an undetermined period. The Fund invests into Estonian small and medium-sized businesses, which focus on innovation, create and use modern technologies as well as develop new products and services, or into investment funds, the assets of which can be invested into businesses described above. The purpose of the Fund is to earn income for the investors of the fund and simultaneously contribute to changes in the Estonian economy, which help modernize the economy, ensure export growth and create new highly skilled jobs.

In 2016, the Fund made one new investment into the Estonian software company Scoro Software OÜ, which enables companies to manage all important data and processes in a single system. The rest of the investments were follow-up investments into current portfolio companies. Total investments of the Fund were 4 347 thousand euros (in 2015, 2 773 thousand euros). In 2016, the Fund divested one investment, when it sold its stake in VitalFields (WeatherMe OÜ), an internationally active Estonian developer of agricultural software, to Climate Corporation, a US agricultural company.

As at 31.12.2016, the net value of the Fund’s assets was 29 119 thousand euros (31.12.2015: 25 170 thousand euros), the net asset value per unit was 11,395.6240 euros (31.12.2015: 9,850.2121 euros) and the ratio between the Fund’s net asset value and paid in capital shall be (TVPI) 1.14 (2015: 1.00).

OUTLOOK FOR 2017

The reorganization of the investment activities of the EDF and the SmartCap and the process for selecting a private fund management company that started in 2016 is scheduled to be completed in 2017. For the purpose of independence and impartiality, the process was consulted by the European Investment Bank, which also declared on 25.08.2016 the call for finding the private fund management company. Six teams submitted their expression of interest, among which four were chosen for the final round, and after the final offer, the Committee of Experts nominated by the European Investment Bank, chose Tera Ventures as the winner. Tera Ventures is a venture capital fund management company that begins operating in the Estonian market, consisting existing investment managers of SmartCap - Andrus Oks, Stanislav Ivanov and adviser James Patrick McDougall. The direct investment portfolio is expected to be transferred to the fund established by the winning team and its management in the first half of 2017.

As part of the reorganization of the EDF and the SmartCap's investment activities, the Supervisory Board of the EDF approved on 27.01.2016 a new investment strategy, according to which the Fund invests the received funds returned from earlier direct investments into accelerator funds. In addition to investments, the accelerator funds offer portfolio companies also a wide range of business development services, which are funded by Startup Estonia instruments, which means that suitable accelerator fund selection process will be implemented in the form of a competitive dialogue on the basis of the Public Procurement Act, where the Management Company and Fund KredEx act as joint contracting authorities.

Accelerator fund selection process was announced in May 2016, but the first public procurement¹ failed due to the discord that occurred in the time-limit published in application documents and the tender notice published in the register of public procurements. Therefore, in October of the same year, a new public procurement² was announced, and by the deadline for submission of applications in November, seven contenders had submitted primary statements of interest to participate in the process. Four applicants out of the seven applicants met the qualification requirements, and in January 2017 these four were proposed to participate in the dialogue. The Management Company expects to reach the conclusion of agreements with suitable accelerator funds already in the second half of 2017.

Until the reorganization of the direct investment management, the Fund's direct investments will continue to be managed in accordance with the terms and conditions of the Fund.

In the spring of 2016, the Economic Affairs Committee of Estonian Parliament concluded a principal decision to terminate the activities of the Development Fund, to transfer monitoring activities to a new Foresight Centre to be created, and investment activities to Fund KredEx. On 29.06.2016 Estonian Parliament adopted the Foresight Act that terminates the activities of the Development Fund from 29.06.2017. Transfer of investment activities of the EDF (including the activities of the former Management Company) into Fund KredEx organization composition takes place after conclusion of the contract with the winning private foundation manager, during the first half of 2017 at the latest. As resulting from the restructuring, in 2017 the Management Company will become a subsidiary of Fund KredEx, which will continue implementation of the current investment strategy.

¹ <https://riigihanked.riik.ee/register/hange/171705>

² <https://riigihanked.riik.ee/register/hange/178587>

THE SIGNATURES OF THE MANAGEMENT BOARD OF THE FUND MANAGEMENT COMPANY TO THE EARLY FUND II FINANCIAL STATEMENTS OF 2016

Management Board of the Fund Management Company AS SmartCap has prepared the Early Fund II Annual Report 2016 that contains a management report, financial statements (including notes), an investment statement and a report of an independent certified auditor.

/signed/

Ms Sille Pettai

AS SmartCap

Fund Manager, Management Board Member

/signed/

Ms Mari Vavulski

AS SmartCap

Management Board Member

Tallinn, 21.04.2017

FINANCIAL STATEMENTS

STATEMENT OF FINANCIAL POSITION

(in euros)

	Note no.	31.12.2016	31.12.2015
ASSETS			
Fixed Assets			
Financial investments at fair value through profit or loss	8	16,532,293	9,702,422
Long-term receivables	9	360,045	219,930
Total fixed assets		16,892,338	9,922,352
Current assets			
Cash and cash equivalents	5	7,789,442	8,301,567
Term deposits	6	4,500,000	7,000,000
Trade receivables and prepayments	7	1,199	23,519
Total current assets		12,290,641	15,325,086
TOTAL ASSETS		29,182,979	25,247,438
Current liabilities			
Trade payables and other current liabilities	10	63,513	76,994
Total current liabilities		63,513	76,994
TOTAL LIABILITIES		63,513	76,994
Fund's assets owned by the unit-holder in net asset value	12	29,119,466	25,170,444

Notes provided on pp. 10–30 form integral parts of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME

(in euros)

	Note no.	2016	2015
Financial income and expenses		192,843	286,410
Interest incomes		205,072	286,410
Foreign exchange losses		-12,229	0
Operating costs	11	-802,649	-791,556
Management fees	11, 13	-757,842	-757,842
Other expenses		-33,698	-10,940
Expert Committee fees	11	-11,109	-22,774
Realised profit from the sale of financial assets measured at fair value		1,093,805	373,641
Net profit/loss from financial assets at fair value through profit or loss	8	3,465,022	908,363
Net result of the Fund		3,949,022	776,858

Notes provided on pp. 10–30 form integral parts of these financial statements.

STATEMENT OF CASH FLOWS

(in euros)

	Note no.	2016	2015
Cash flows from Fund's operating activities			
Operating expenses paid		-800,137	-787,571
Loans granted	8	-2,041,510	-986,254
Paid upon acquisition of financial investments		-2,305,185	-1,786,651
Received from sales of financial investments		2,112,676	791,221
Interests received		22,032	101,763
Total cash flows from Fund's operating activities		-3,012,125	-2,667,492
Cash flows from Fund's investing activities			
Payments to/repayments from term deposits	6	2,500,000	9,000,000
Total cash flows from Fund's financial activities		2,500,000	9,000,000
Total cash flows		-512,125	-6,332,508
Cash and cash equivalents at beginning of period	5	8,301,567	1,969,059
Change in cash and cash equivalents		-512,125	6,332,508
Cash and cash equivalents at end of period	5	7,789,442	8,301,567

Notes provided on pp. 10–30 form integral parts of these financial statements.

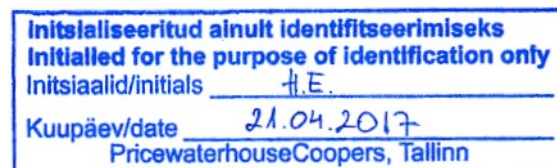
STATEMENT OF CHANGES IN FUND'S NET ASSET VALUE

(in euros)

	2016	2015
Net asset value of Fund's assets at the beginning of reporting period	25,170,444	24,393,586
Change in the net asset value of the Fund's assets owned by the unit-holder	3,949,022	776,858
Net asset value of the Fund's assets at the end of the period	29,119,466	25,170,444
Number of units outstanding at the end of the period	2,555.320	2,555.320
Net Asset Value per share at the end of reporting period	11,395.6240	9,850.2121

More specific information on Fund units is indicated in Note 12.

Notes provided on pp. 10–30 form integral parts of these financial statements.



NOTES TO THE FINANCIAL STATEMENTS

Note 1 General information

Early Fund II (the Fund) is a closed-ended common investment fund (venture capital fund) formed on 20.02.2012. The Fund is comprised of money raised through issue of units and other assets received from investing such money, owned collectively by investors and managed by the SmartCap. The Estonian Financial Supervision Authority is exercising financial supervision over the Fund.

The Fund is managed by AS SmartCap. The sole shareholder of AS SmartCap is Estonian Development Fund (in liquidation) that is a legal entity governed by public law established on the basis of the Estonian Development Fund Act.

The registered address of the Fund is Hobujaama 4, Tallinn 10151, Republic of Estonia. The financial year of the Fund starts on 1 January and ends on 31 December.

The management board of the SmartCap approved the annual report of the Fund on 21.04.2017.

Note 2 Overview of key accounting and reporting policies

An overview of the key accounting and reporting policies applied to the preparation of the financial statements is presented below. These accounting and reporting policies have been used consistently in all reporting periods, other than the cases for which information has been disclosed separately.

2.1. Basis of accounting

The financial statements of the Fund have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS EU). Financial reporting principles of investment funds are set out by the Investment Funds Act, Accounting Act and Regulation no 21 of the Minister of Finance of 13 April 2011 "Requirements for investment fund reports subject to disclosure". The financial statements have been prepared taking into account the procedure for determining the net asset value of the Fund, adopted pursuant to § 142 2) and § 204 1) of the Investment Funds Act.

The financial statements of the Fund have been prepared in accordance with IFRS to the extent that complies with the requirements of the Investment Funds Act and Regulation no 21 of the Minister of Finance. In the event of any inconsistency, the Fund has taken into account the requirements provided for in the Investment Funds Act and in the Regulation no 21 of the Minister of Finance "Requirements for investment fund reports subject to disclosure".

A new Investment Fund Act entered into force after the end of reporting period but before preparation of these financial statements. These financial statements have been prepared in accordance with the Investment Fund Act valid during reporting period, guided by the principle set in § 522 of the new Investment Fund Act.

The financial statements have been prepared under the historical cost convention, except for financial assets at fair value through profit or loss (long-term financial investments). Preparation of financial statements in conformance with financial reporting standards requires use of specific accounting estimates. The management is also required to exercise its judgment in the process of applying the reporting and accounting principles. The areas involving a higher degree of judgment

or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 4.

2.2 New or revised standards and their interpretations

“Disclosure Initiative” - Amendments to IAS 1 (Effective for annual periods beginning on or after 1 January 2016; not yet adopted by the European Union). The amendments clarify guidance in IAS 1 on materiality and aggregation, the presentation of subtotals, the structure of financial statements and the disclosure of accounting policies.

There are no other new or revised standards or interpretations that are effective for the first time for the financial year beginning on 1.1.2016 that would be expected to have a material impact to the Fund.

New or revised standards and interpretations

The following new or amended standards and interpretations released as of the date of approval of this report but that have not taken effect yet:

IFRS 9 "Financial Instruments": Classification and measurement (effective for annual periods beginning on or after 1 January 2018). The key features of the new standard are as follows:

- Financial assets are required to be classified into three measurement categories: those to be measured subsequently at amortised cost, those to be measured subsequently at fair value through other comprehensive income (FVOCI) and those to be measured subsequently at fair value through profit or loss (FVPL).
- Classification for debt instruments is driven by the entity’s business model for managing the financial assets and whether the contractual cash flows represent solely payments of principal and interest (SPPI). If a debt instrument is held to collect, it may be carried at amortised cost if it also meets the SPPI requirement. Debt instruments that meet the SPPI requirement that are held in a portfolio where an entity both holds to collect assets’ cash flows and sells assets may be classified as FVOCI. Financial assets that do not contain cash flows that are SPPI, must be measured at FVPL (for example, derivatives). Embedded derivatives are no longer separated from financial assets but will be included in assessing the SPPI condition.
- Investments in equity instruments are always measured at fair value. However, management can make an irrevocable election to present changes in fair value in other comprehensive income, provided the instrument is not held for trading. If the equity instrument is held for trading, changes in fair value are presented in profit or loss.
- Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated at fair value through profit or loss in other comprehensive income.
- IFRS 9 introduces a new model for the recognition of impairment losses - the expected credit losses (ECL) model. There is a ‘three stage’ approach which is based on the change in credit

quality of financial assets since initial recognition. In practice, the new rules mean that entities will have to record an immediate loss equal to the 12-month ECL on initial recognition of financial assets that are not credit impaired (or lifetime ECL for trade receivables). Where there has been a significant increase in credit risk, impairment is measured using lifetime ECL rather than 12-month ECL. The model includes operational simplifications for lease and trade receivables.

- Hedge accounting requirements were amended to align accounting more closely with risk management. The standard provides entities with an accounting policy choice between applying the hedge accounting requirements of IFRS 9 and continuing to apply IAS 39 to all hedges because the standard currently does not address accounting for macro hedging.

The fund manager estimates that the implementation of IFRS 9 standard does not significantly change classification of debt securities and equity instruments, as:

- a) the Fund's debt securities have been historically subsequently measured at fair value through profit or loss, into which category the financial assets also will be placed after assessment of business model when implementing IFRS 9;
- b) equity instruments have been historically subsequently measured at fair value through profit or loss.

According to fund manager's estimation, the implementation of the expected credit loss model has no material impact to existing incurred credit loss model, as significant part of Fund's assets are measured at fair value through profit or loss or have a very low credit risk (cash and cash equivalents in banks).

There are no other new or revised standards or interpretations that are not yet effective that would be expected to have a material impact on the Fund.

2.3 Classification of assets and liabilities into current and non-current

Assets and liabilities are classified as current and non-current in the statement of financial position. Current assets include the assets which are expected to be disposed of in the next financial year or during the normal operating cycle of the Fund. Current liabilities include liabilities which payment date is in the next financial year or which are expected to be paid in the next financial year or during the normal operating cycle of the Fund. All remaining assets and liabilities are considered as non-current.

2.4 Financial assets

2.4.1 Classification

The Financial assets of the Fund are classified into the following categories:

- 1) Financial assets at fair through profit or loss, and
- 2) Loans and receivables.

Financial assets are classified depending on the purpose for which the financial assets were acquired. The Fund manager classifies the financial assets at the initial recognition of the financial asset.

(a) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are included in current assets, except for maturities greater than 12 months as at period end date. In that case they are classified as non-current assets. The following financial assets are included in the category of loans and receivables: “Cash and cash equivalents”, “Maturing deposits” and “Other current receivables”.

(b) Financial investments

The Fund recognises the venture capital investments in early-phase companies (hereinafter financial investments) at fair value through profit or loss. Venture capital investments in financial assets are initially recognized at fair value through profit or loss if the fair value of financial assets are evaluated in accordance with documented risk management policies and investment strategies and reporting to the unit-holders is based on the same principles.

The granted convertible loans, which likelihood of conversion Fund manager has evaluated as high in accordance with documented risk management policies and investment strategies are initially recognized financial assets at fair value through profit or loss. Other loans are recognised at amortised cost.

2.4.2 Recognition and measurement

Sales and purchases of financial assets under ordinary market terms are recognised or their recognition is ended by using the value date based calculation. The Fund recognises a financial asset when the contractual rights to the cash flows generated by the financial assets have expired or have been transferred and substantial part of risks and rewards bound to the financial asset have been transferred.

(a) Loans and receivables

Loans and receivables are initially recognised at their fair value plus transactions costs. After initial recognition loans and receivables are subsequently measured at amortised cost using the effective interest rate method. Interest income is recognised in the statement of comprehensive income on line “Interest income”.

(b) Financial investments

Financial assets that are recognised at fair value through profit or loss are initially recognized at fair value and acquisition-related transaction costs are recognized as an expense in the statement of profit or loss. Financial assets that are recognised at fair value through profit or loss are after initial recognition recognised at fair value. Changes in fair value are recognised in statement of comprehensive income under "Profit / loss from financial assets at fair value through profit or loss" in period in which they incurred.

For investees, the Fund will assess whether the Fund would have a significant influence on the investee. In general, significant influence is presumed to exist when the Fund owns 20% to 50% of the voting rights.

In exceptional cases it may also be presumed as a significant influence on holding less than a 20% of the shares. Significant influence is usually characterised by the following circumstances:

- (a) Representation in the management or in a higher supervisory body of the investee;
- (b) Participation in business-political decision-making of investee;
- (c) Material transactions between the investor and the investee;
- (d) Partial overlaps of the managements of the investor and the investee;
- (e) Exchange of technical information between the investor and the investee.

Investments in associates are recognised similarly to other investees at fair value through profit or loss according to an exception in IAS 28 “Investments in Associates” for venture capital company financial statements for recognition of associates. An investment in an associate is initially recognized at fair value and transaction costs related to acquisition are recognized as expenses in the income statement.

2.5 Cash and cash equivalents

For the purpose of the statement of financial position and cash flow statement, cash and cash equivalents include bank account balances (except bank overdraft), term deposits with maturities of 3 months or less at the time of acquisition and investments in money market funds and other highly liquid funds, assuming that the fund invests in financial assets that meet the definition of cash and cash equivalents.

2.6 Trade receivables and prepayments

Loans granted and other short and long-term receivables are recognised at amortised cost. The amortised cost of current receivables generally equals to their nominal value (minus repayments or given discounts), for which reason current receivables are recognised in the balance sheet at the likely received sum. Long-term receivables are initially recognised at fair value of the consideration receivable and subsequently interest income is calculated on the receivable using the effective interest rate method.

It will be evaluated at each balance sheet date whether there are signs of impairment of financial assets or a group of financial assets measured at amortized cost. In case there are signs of impairment, the financial assets measured at amortised cost are discounted to the expected net present value of future cash payments (discounted at the initial recognition of the financial asset with original effective interest rate) and financial assets recognised at first cost are discounted to the amount that is reasonably estimated to be the selling price at the balance sheet date. Impairment losses are recognised as an expense in the statement of comprehensive income.

2.7 Impairment of financial assets

If the Fund has financial assets that are not recognized in their fair value through profit and loss, at each reporting date, it assessed whether there is objective evidence that a financial asset has actually impaired compared to the book value of these assets. Factors that may indicate to the impairment of financial assets include:

- Financial problems of the security’s issuer, signs of possible bankruptcy of the issuer;
- Defaulting or overdue payment of interest or principals of the security;

- Loss of active market of the financial asset;
- Other significant events that may indicate impairment.

In impairment of assets recognized at amortised cost, the impairment loss is calculated as the difference between the carrying amount of the asset and the present value of the estimated future cash flows, discounted using the original effective interest rate. The carrying amount of the asset is reduced by this amount and the loss is recognized in the statement of profit or loss. In case of impairment of financial assets recognized in amortized cost, the calculation of interest income of the assets is not amended. Impairment loss on financial assets carried at amortized cost is reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

2.8 Financial liabilities

All financial liabilities (supplier payables, accrued expenses and other short and long-term payables) are initially recorded at amortised cost. The amortised cost of the current financial liabilities normally equals their nominal value; therefore current financial liabilities are stated in the balance sheet in their redemption value. To calculate the amortised cost of non-current financial liabilities, they are initially recognised at fair value of the proceeds received (net of transaction costs incurred) and an interest expense is calculated on the liability in subsequent periods using the effective interest rate method.

Financial liabilities are classified as current when they are due to be settled within twelve months after the balance sheet date; or the Fund does not have an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date or when the borrower has the right to recall the loan at the balance sheet date, due to breach of the loan contract terms.

2.9 Recognition of foreign currency transactions

Functional currency of the Fund is euro. Presentation currency of the financial statements of the Fund is also euro.

When recognising transactions performed in foreign currency, the exchange rates of the European Central Bank officially valid on transaction day are taken as the basis for the transactions. Financial assets and obligations fixed in foreign currency are revaluated on the balance sheet date into functional currency using the official exchange rates quoted by the European Central Bank. Exchange gains and losses resulting from the revaluation are recognized in the income statement of the reporting period. Non-monetary assets and liabilities fixed in foreign currency measured at fair value are revaluated to the functional currency taking the exchange rates of the European Central Bank valid on the day of designation of fair value as the basis.

2.10 Transactions with related parties

Preparation of the financial statements deems the associates, the AS SmartCap and its executive and senior management and other persons and entrepreneurs who can control and significantly influence the financial and business decisions as related parties. Since the units of Early Fund II are 100% owned by the Republic of Estonia, the related parties include also all entities under control or significant influence of the Republic of Estonia.

2.11 Revenues

- (a) Interest income

Interest income is recognised when the receipt of revenue is certain and the amount of revenue can be measured reliably. Interest income is recognised using the asset's effective interest rate unless the receipt of interest is uncertain. In such cases, interest income is reported on a cash basis.

(b) Dividend income

Dividend income is recognised when the right to receive payment is established.

2.12 Fund units

The Fund has issued one class of units that give the unit-holder the right to a pro rata share of the Fund's net assets in liquidation of the Fund upon maturity (see note 2.13 of Fund's rules). Fund units are not associated with any other contractual obligations except their redemption in case of fund liquidation. Fund units are recognised as equity instruments as following IAS 32 criteria are met;

- Units provide owners with a right to receive a pro-rata share of the Fund's net assets (or net asset value) upon the Fund's liquidation. The Fund's net asset value is determined by subtracting the Fund's liabilities from the market value of the Fund's assets. A pro-rata share is calculated as follows: the Fund's net asset value is divided by the number of units issued and the result is multiplied by the number of units owned by each unit-holder.

- Units are subordinate to all other debt and other instruments issued by the Fund;

- The rights arising from all units (to receive payment in accordance with a pro-rata share in net assets) are identical;

- The Fund has no other financial instruments or contracts whose cash flows are largely based on profit, changes in net assets or fair value change in net assets accounted for on the balance sheet/off-balance sheet, as a result of which the income of unit-holders would be substantially limited or fixed.

If the terms related to units change so as to cause the criteria listed above to be no longer met, the units shall be classified as financial liabilities from the date that such conditions are no longer met. A financial liability is recognised at the fair value of the transaction date. In the event of a difference arising between the carrying amount of an equity instrument and the fair value of a liability, the difference is recognised in net assets.

Direct expenses related to the issuance of new units are recognised in net assets as a reduction of the amount paid-in for units. If the Fund repurchases its own units, the equity attributable to unit-holder is reduced by the payment received, less costs to sell.

2.13 Fund rules

Fund rules regulate the relations with the Fund unit-holders and with the management company.

Fund units

Fund units are issued by the SmartCap. Issuance of the units is not public. SmartCap will conduct the issuance of units targeting professional investors as set out in § 6 2) of the Securities Market Act. Unit represents the investor's share of the Fund's assets. The Fund has one class of units. Units

are held in registered form and ownership documents will not be issued for the unit. Units acquired by the investor will be recorded in the investor's securities account. Units are not redeemed at investor's request. Units are redeemed upon liquidation of the Fund. The nominal value of one unit is EUR 10,000 (ten thousand). SmartCap will issue the units at issue price, that is the latest NAV by the time the purchase order came in. Number of units issued to the investor will be calculated by dividing amount paid by the investor by the unit issue price. When issuing units the SmartCap does not take subscription fee from the investors. Units are divisible. When dividing units, fractions are rounded to three decimal places.

Rights arising from ownership of units

Rights and obligations arising from units will rise as unit is issued and will be terminated as unit is redeemed. The unit is issued from the moment of registration and redeemed from the moment of removal from the register. Ownership of a unit is certified by an entry in the register. Investors are participating in the management of the Fund through general meetings. The investor does not have the right to request termination of the common ownership or separation of its unit from the assets of the Fund. Investors are entitled under the ownership of the units, including, but not limited to the following:

- Units may be disposed to professional investors in the stock market;
- Get in case of payments made from the Fund their share (accordingly to units owned) of the profit according to the Fund's rules;
- In case of funds liquidation receive according to the Fund's rules its share of fund's assets remained accordingly to units owned;
- Convene a general meeting and to attend and vote at general meetings;
- Require that the management company compensates the damage caused by breaching of its obligations.

Investor is not personally liable for the obligations of the Fund, the SmartCap has taken account of the Fund, as well as the responsibilities that SmartCap has the right to require from the Fund, according to funds rules. Investor responsibility for the performance of such obligations is limited to his share of the Fund's assets.

Fees and expenses paid from Fund's accounts

The SmartCap is paid management fees on behalf of the Fund in exchange for management of the Fund, comprised of two components: a fixed fee and a success fee. Fixed fee is paid on a monthly basis and is amounted 3% of fund's assets (initial investment capital). If the Fund's net income is (amount received for the exit from the investments, minus the initial investment capital) positive, success fee amounted 20% of fund's net profit is paid to the SmartCap.

In addition to the management fee expenses directly related to the management of the Fund are paid from fund's accounts, which include, for example:

- All expenses related to investments and the costs corresponding to market practice (at market prices);
- All expenses related to purchase, sales or management of the Fund's assets;
- Expenses related to valuation of Fund's assets;
- Expenses associated with formation and liquidation of the Fund;

- Registrar fees;
- Expenses of convening and conducting the Shareholders' meeting;
- Expert Committee fees;
- Expenses of preparing fund's reports (incl. the annual report) and auditing fees of the annual report;
- Other charges relating to the Fund, such as transaction fees, bank charges, commissions, security account management fees, stamp duties, fees for legal services, legal costs.

Fees (fixed fee paid to the Fund's management company for managing the Fund) and expenses paid in a one year from Fund's accounts cannot be more than 6% from fund's assets.

Note 3 Financial risk management

The SmartCap has established rules for identification, measurement, management, monitoring and reporting of risks. The objective of such rules is to regulate the procedures related to risk management on the level of the SmartCap and the Fund. The general risk management policies are approved by the Supervisory Board of the SmartCap. The management board of the SmartCap submits reports and overviews on a regular basis to the Supervisory Board regarding the risks associated with the SmartCap's business and loss events arising from the materialisation of such risks. The management board is responsible for the implementation of risk management policies approved by the Supervisory Board. The SmartCap undertakes to immediately communicate any material unusual risks associated with the investment of the Fund's assets or other activities related to management of the Fund. The Fund manager observes that the Fund is managed according to the provisions of the legislation and the Terms of the Fund.

Risk management, including decision process and role of different persons (including investment managers) and bodies (including Expert Committee), are additionally regulated in the document "Principle for performance and management of direct investments" established by the SmartCap upon making and managing investments from the Fund and divestments.

Risks related to the activities of the SmartCap are divided into Fund-related risks and other risks related to the activities of the SmartCap. Operational risk is also monitored on the level of risks associated with the operations of the SmartCap which may arise from inadequacy or failure to function in an expected manner of processes, actions by people or systems or external events. Operational risk involves legal, regulative, information technology, model, procedural, personnel, control and management risk.

3.1 Financial risks

The Fund that is managed by the SmartCap is an early seed and start-up stage venture capital investment fund and the investments that it makes are inherently of a high risk level. Investment risks arise from the following attributes:

- Early stage of development of investees, therefore their business models and revenue generation capacity have not yet been proved and thus several investees could experience failure;
- Concentration of investments of a similarly high risk level in the Fund;

- Low level of liquidity of long-term non-marketable securities, therefore the divestment may significantly impact the return on investment and the return of the whole fund.

The primary risks involved in the Fund from the standpoint of the SmartCap's operations include failure to achieve a critical level of assets under management, rendering it unreasonably expensive to manage the Fund, and/or a lower than expected return on invested capital, causing unit-holders in the Fund to not receive the return that they expected on their invested capital or, worse, fail to even achieve the return of the capital that they invested.

With the aim of hedging, the possible investees are analysed (including analysis of legal and business activities of investment projects, technical expert assessments and background screening) thoroughly before investing. A multi-tiered structure has been established for the management of risks associated with the selection of investments for the Fund and lack of management quality whereby an independent expert committee will also participate in giving an investment recommendation in addition to the management board of the SmartCap.

In addition, involvement of independent co-investors of private sector helps the Fund to manage the investment-related risks on the direct investment level (the Fund has the right to invest to entrepreneurs only with legal persons in private law (with involvement of private equity) and under the same conditions).

With the aim to spread risks, the terms of the Fund have established the limits for Fund's volume to avoid the significant negative impact that might occur with realisation of a single investment on the one hand and existence of sufficient amount of investees in the Fund to earn required income on the other hand.

The SmartCap and its employees consider the following specific risks related to Fund investments upon making and managing Fund's investments:

- Market risk - market of the fund's investee may rise or fall and impact hence the value of Fund assets. The overall condition of the economy as well as the developments in a relevant sector can influence the value of the Fund's investments.
- Credit risk - issuer of the security in the Fund assets or counterparty of the transaction carried out with the Fund assets fails partly or fully perform its obligations (e.g. the acquirer of the investee does not perform its payment obligation upon divestment). For hedging, the free funds of the Fund are invested to the low risk instruments and the counterparties with low credit risk are preferred. The risk of non-performance of the investee upon divestment is managed contractually (e.g. using appropriate collaterals or prepayments).
- Liquidity risk - financial risk that an open positions cannot be liquidated or the Fund's assets cannot be traded quickly enough for the foreseen fair price. Since the Fund invests to non-traded low liquidity instruments, the Fund investments might not have market if the Fund wishes to divest. To enable divestment, the divestment is usually planned approximately 3 years before divestment. Management of liquidity risk follows the procedure of management of a assets of the SmartCap.
- Issuer risk - the price of a security may be subject to adverse changes upon discovery of unfavourable circumstances dependent on the issuer. The businesses of the issuers are analysed and monitored in order to manage issuer risk. Employees of the SmartCap participate in the Supervisory Board of an issuer in order to manage issuer risk.

- Interest risk arises from a change in interest rates. As the Fund may grant loans to companies in addition to investing in the equity of the company, the Fund is exposed to interest rate risk. However, convertible loans granted typically carry a fixed rate of interest.
- Concentration risk is related to concentration of assets. To hedge the concentration risk, the SmartCap follows the risk management requirements provided for in the Terms of the Fund upon asset investments.
- Legal risk - the risk that legislation that the Fund is subject to may change, including legislation governing the tax system. The SmartCap monitors changes in the legal environment in order to manage legal risk and adapts the operations of the Fund in accordance with any changes in legislation.

The SmartCap views the levels of market risk, credit risk, liquidity risk and issuer risk as relatively high due to the characteristics of the Fund's investments. The SmartCap does not aim to avoid those risks but rather to manage them appropriately and proactively. The Fund has maintained a sufficient level of liquid assets in the form of cash and cash equivalents in order to mitigate liquidity risk and perform obligations on a timely basis and as at 31.12.2016, the liquid funds exceed the Fund's liabilities. The Fund also has adequate liquid funds to meet financial obligations that will be incurred in the year 2017 and to make new investments. (Also see Note 5 - cash and cash equivalents and Note 10 - liabilities as at 31.12.2016). No custody risk arises in association with the Fund's operations because the Fund does not have a depositary. Also, no significant currency risk arises in association with the Fund's investments, because the investments made from the Fund's accounts are primarily into the equity capital of Estonian companies.

Financial assets of the Fund indicated in Notes 5, 6, 7 and 8 are exposed to credit risk. Regarding cash at bank and in hand, subsidiaries/branches of Scandinavian banks that are strong and recognized in Estonian market and with a Moody's rating of at least Aa3 have been chosen to hedge the credit risk. Credit risk of investments recognized at fair value is high due to the early development phase of these investees.

3.2 Capital risk management

Shares subscribed for by investors of the Fund constitute capital. Units are not redeemed at investor's request. The redemption of shares only occurs upon liquidation of the Fund. Shareholders may resolve to liquidate the Fund.

All shares of the Early Fund II belong to the Republic of Estonia. Decisions concerning the distribution of dividends and subscription or redemption of shares are made by the Republic of Estonia (via the Ministry of Economic Affairs and Communications). The equity of the Fund is not subject to regulation by the Commercial Code and there are no other requirements arising from law.

Liquidation of the Fund must consider that the Fund's assets are highly illiquid and this factor causes a high risk to maintaining the fair value of assets in the course of the liquidation process. The Fund does not employ financial leverage.

3.3 Fair value

According to the judgment of the Fund manager, the fair value of financial assets and liabilities measured at amortised cost are not significantly different than the carrying amounts presented in the balance sheet as at 31 December 2016. The financial assets measured at amortised cost are short-term in duration and bear interest at rates that have not substantially changed in the market between the dates of recognition of the financial assets and the balance sheet date, therefore the carrying amount is estimated to approximate the fair value. As financial liabilities are short-term and are not interest-bearing and have been repaid by the date of approval of the financial statements, their carrying amount is estimated to approximate the fair value.

The Fund classifies financial investments in three levels according to revaluation:

Level 1: Financial investments measured at unadjusted stock exchange quotations or quoted prices in other active regulated markets;

Level 2: Financial instruments measured using methods that are based on observable inputs. This category includes for example financial instruments that are measured using prices of similar instruments in an active regulated market or financial instruments for which quoted prices from regulated markets are used but where market liquidity is low.

Level 3: Financial instruments where the methods used for revaluation are based on unobservable inputs.

The following is determined in accordance with the Fund's rules for determining net asset value as adopted by the Supervisory Board of the SmartCap:

- The value of cash in hand and deposits at their nominal value;
- The value of interest that is accrued but unpaid is accounted for as accrued income;
- Determination of fair value of non-marketable securities is primarily based on the valuation methods stipulated by IFRS and valuation methods provided in the valuation guidance issued by the Invest Europe (former EVCA), which may be:
 - Price of the most recent investment transaction;
 - Discounted cash flow method;
 - Net assets method;
 - Determination of value on the basis of a profit multiplier.

All investments of the Fund measured at fair value as classified as Level 3.

Fair value of the Fund's financial investments as of 31.12.2016 is calculated as follows:

- GOLIATH Wind OÜ, Lingvist Inc., Jobbatical OÜ, Realeyes (Holdings) Limited, IOT Holding OÜ, Scorio Software OÜ, Monese Ltd: price of the most recent investment transaction. The most recent transaction price of investees is used as the price of the most recent investment transaction within the framework of which existing or new investors have invested to the investee. If the aforementioned transaction did not occur close to the balance sheet date (i.e. more than 3 months prior to or after the balance sheet date), the fair value at the balance sheet date has been determined based on the operations of the investee during the interim period and the rate at which actual operations correspond to initial targets on the basis of which the transaction price and value of the investee were determined by investors. Regarding the investments provided above, no significant adjustments during the period between the transaction date and the balance sheet date have been made due to changes;

- Thinnect OÜ: price/acquisition cost of the last investment transaction. The Fund's initial transaction involving the investee has been used as the price of the most recent investment transaction /cost with the investee because it is estimated that the transaction occurred close to the balance sheet date (i.e. 3 months prior to or after the balance sheet date) or no incremental investments by new external investors have been made to the investee after the initial purchase. The fair value at the balance sheet date has been determined using the operations of the investee during the interim period and the rate at which actual operations correspond to initial targets on the basis of which the transaction price and value of the investee were determined by investors. Regarding the investments provided above, no significant adjustments during the period between the transaction date and the balance sheet date have been made due to changes;
- CX Cloud Services OÜ and Sportlyzer OÜ: price of the most recent investment transaction /cost adjusted with the investee's activity result compared to the forecasts based on the last transaction price. The Fund's initial transaction involving the investee has been used as the price of the most recent investment transaction /cost with the investee because it is estimated that the transaction occurred close to the balance sheet date (i.e. 3 months prior to or after the balance sheet date) or no incremental investments by new external investors have been made to the investee after the initial purchase. The fair value at the balance sheet date has been determined using the operations of the investee during the interim period and the rate at which actual operations correspond to initial targets on the basis of which the transaction price and value of the investee were determined by investors. Significant adjustments have been made towards the above specified investment due to the changes in the interim period of the moment of transaction and the balance day.

Fair value of the Fund's financial investments as of 31.12.2015 is calculated as follows:

- GOLIATH Wind OÜ, WeatherMe OÜ, Lingvist Inc., Jobbatical OÜ, Realeyes (Holdings) Limited and IOT Holding OÜ: price of the most recent investment transaction. The most recent transaction price of investees is used as the price of the most recent investment transaction within the framework of which existing or new investors have invested to the investee. If the aforementioned transaction did not occur close to the balance sheet date (i.e. more than 3 months prior to or after the balance sheet date), the fair value at the balance sheet date has been determined based on the operations of the investee during the interim period and the rate at which actual operations correspond to initial targets on the basis of which the transaction price and value of the investee were determined by investors. Regarding the investments provided above, no significant adjustments during the period between the transaction date and the balance sheet date have been made due to changes;
- Thinnect OÜ and Monese Ltd: price/acquisition cost of the last investment transaction. The Fund's initial transaction involving the investee has been used as the price of the most recent investment transaction /cost with the investee because it is estimated that the transaction occurred close to the balance sheet date (i.e. 3 months prior to or after the balance sheet date) or no incremental investments by new external investors have been made to the investee after the initial purchase. The fair value at the balance sheet date has been determined using the operations of the investee during the interim period and the rate at which actual operations correspond to initial targets on the basis of which the transaction price and value of the investee were determined by investors. Regarding the investments provided above, no significant

adjustments during the period between the transaction date and the balance sheet date have been made due to changes;

- CX Cloud Services OÜ and Sportlyzer OÜ: price of the most recent investment transaction /cost adjusted with the investee's activity result compared to the forecasts based on the last transaction price. The Fund's initial transaction involving the investee has been used as the price of the most recent investment transaction /cost with the investee because it is estimated that the transaction occurred close to the balance sheet date (i.e. 3 months prior to or after the balance sheet date) or no incremental investments by new external investors have been made to the investee after the initial purchase. The fair value at the balance sheet date has been determined using the operations of the investee during the interim period and the rate at which actual operations correspond to initial targets on the basis of which the transaction price and value of the investee were determined by investors. Significant adjustments have been made towards the above specified investment due to the changes in the interim period of the moment of transaction and the balance day.

More detailed quantitative information concerning investments measured at fair value is presented in Note 8. In accordance with the circumstances disclosed in Note 4, sensitivity analysis has not been performed for investments classified as Level 3 in these financial statements.

Note 4 Significant accounting estimates

Several accounting estimates and assumptions which have an impact on the assets and liabilities as well as off-balance sheet assets and contingent liabilities disclosed in the notes have been used in preparing the financial statements. Although these estimates are based on the management's best knowledge of current events and actions, actual results may differ ultimately from those estimates. Changes in management estimates are recognised in the statement of comprehensive income of the period of the change.

Estimates concerning the fair value of financial investments have the greatest impact on the financial information presented in the annual account. At the same time, long-term financial investments account for 56.65 % of the Fund's assets at the balance sheet date (31.12.2015: 38.43 % of the Fund's assets).

The basis for the value of financial investments measured at fair value is a valuation conducted as at 31.12.2016. In accordance with the disclosure in Note 3.3, the price of the most recent investment transaction/cost has been used as the method.

Note 5 Cash and cash equivalents

(in euros)

	31.12.2016	31.12.2015
Current accounts	7,789,442	8,301,567
Total cash and cash equivalents	7,789,442	8,301,567

Note 6 Term deposits

(in euros)

	31.12.2016	Currency	Starting date	Maturity date	Interest rate
Term deposit LHV	4,500,000	EUR	12.08.2016	12.02.2017	0.07 %
Total term deposits	4,500,000	EUR			

	31.12.2015	Currency	Starting date	Maturity date	Interest rate
Term deposit Nordea	3,000,000	EUR	17.07.2015	18.01.2016	0.30%
Term deposit Nordea	4,000,000	EUR	20.10.2015	20.10.2016	0.23%
Total term deposits	7,000,000	EUR			

Note 7 Trade receivables and prepayments

(in euros)

	31.12.2016	31.12.2015
Current trade receivables and prepayments		
Other current receivables		
Interest receivables	1,199	6,065
Other receivables	0	17,454
Total current trade receivables and prepayments	1,199	23,519

As at 31.12.2015 and 31.12.2016, interest receivable includes accrued interest on term deposits. Interests are collected at the end of the term of the deposit.

As at 31.12.2015, the line item "Other receivables" includes receivables from sale of Fits.me Holding Ltd shares.

The fair value of receivables does not materially differ from its carrying amount. The collection of receivables and the receipt of services and goods for prepayments are not secured by collateral. All of the receivables and prepayments of the Fund are denominated in euros.

Note 8 Financial investments at fair value through profit or loss

(in euros)

	31.12.2016	31.12.2015
The carrying value of the holdings at the beginning of the year	7,836,525	3,881,277
Fair value of the convertible loans granted at the beginning of the year	1,865,897	2,406,870
Total investments to associates at fair value at the beginning of the year	9,702,422	6,288,147
Cost of acquired share holdings	2,303,417	1,964,641
Convertible loans granted	2,041,510	986,254
Calculated interests	187,920	209,981
Fair value revaluation of holdings/loans	3,465,022	908,363
Sales of holdings	-1,167,997	-654,964
Convertible loans converted to share capital	3,368,846	1,490,716
Fair value of holdings at the end of the year	15,805,812	7,836,525
Fair value of the convertible loans granted at the end of the year	726,481	1,865,897
Total investments to associates at fair value at the end of the year	16,532,293	9,702,422

Associate	Area of activity	Holding as at 01.01.2016 (%)	Acquired holding %	Holding as at 31.12.2016 (%) ³
GOLIATH Wind OÜ	Manufacturing of electric motors, power generators and transformers	15.71 %	0.11 %	15.82 %
IOT Holding OÜ (Defendec OÜ)	Holding companies	20.35%	0%	20.35%

³ In recording the contribution to the investments of associates at the balance sheet date option programs approved and issued by investees have been taken into account that have a solvent effect on valuing the contributions.

Sportlyzer OÜ	Programming	6.75%	-2.47%	4.28%
Realeyes (Holdings) Limited (Realeyes OÜ)	Data processing, web hosting and related activities	20.40%	1.88%	22.28%
WeatherMe OÜ	Information-related activities not classified elsewhere	16.72%	-16.72%	0%
Jobbatical OÜ	Information-related activities not classified elsewhere	16.50%	-0.10%	16.40%
Lingvist Inc. (Keel 24 OÜ)	Programming	8.79%	0%	8.79%
CX Cloud Services OÜ	Data processing, web hosting and related activities	0%	0%	0%
Thinnect OÜ	Other IT and computer-specific activities	0%	0%	0%
Monese Ltd	Holding companies	0%	12.83%	12.83%
Scoro Software OÜ	Publishing of other software	0%	9.10%	9.10%

Associate	Area of activity	Holding as at 01.01.2015 (%)	Acquired holding %	Holding as at 31.12.2015 (%) ⁴
GOLIATH Wind OÜ	Manufacturing of electric motors, power generators and transformers	12.62%	5.12%	15.71%
Fits.me Holdings Ltd	Other professional, scientific and technical activities n.e.c.	7.49%	-7.49%	0.00%
IOT Holding OÜ (Defendec OÜ)	Holding companies	20.35%	0%	20.35%
Sportlyzer OÜ	Programming	6.75%	0%	6.75%
Realeyes (Holdings) Limited (Realeyes OÜ)	Data processing, web hosting and related activities	18.60%	1.8%	20.40%
WeatherMe OÜ	Information-related activities not classified elsewhere	0%	16.72%	16.72%
Jobbatical OÜ	Information-related activities not classified elsewhere	16.50%	0%	16.50%
Lingvist Inc. (Keel 24 OÜ)	Programming	0%	8.79%	8.79%
CX Cloud Services OÜ	Data processing, web hosting and related activities	0%	0%	0%
Thinnect OÜ	Other IT and computer-specific activities	0%	0%	0%
Monese Ltd	Holding companies	0%	0%	0%

In table above, associates with 0% holding as at 31.12.2015 or 31.12.2016, the Fund has correspondingly not made any investments or has made an investment only as a convertible loan.

The Fund invests in the shares of early-stage knowledge-intensive and technology-intensive Estonian companies. Investments are made in conjunction with co-investors from the private sector on equal terms and on the basis of commercial considerations. The Fund has not invested in situations where they would have acquired the shares of other shareholders or investors. As a result of the investment, the Fund's ownership interest in the company is typically within the range of 10% to 49% of the voting rights.

The Fund may grant loans to the investees for improved structuring of equity investments. Loans granted to investees bear interest at rates of 8%, 10%, 15% and 20% depending on the terms of the loan agreement. The loans are convertible into equity.

⁴ In recording the contribution to the investments of associates at the balance sheet date option programs approved and issued by investees have been taken into account that have a solvent effect on valuing the contributions.

The Fund has not received any dividend income during 2015 and 2016.

The methodology for the estimation of fair value of investees and the fair value of convertible loans is presented in Note 3.3. According to terms of the shareholder agreements and loan agreements, the Fund has significant influence over, IOT Holding OÜ, Realeyes (Holdings) Limited, GOLIATH Wind OÜ, Lingvist Inc., Sportlyzer OÜ, Jobbatical OÜ, Monese Ltd, CX Cloud Services OÜ, Thinnect OÜ and Scoro Software OÜ. As at 31.12.2016, the Fund had agreed to unfunded investment commitments in the amount of 400 thousand euros (the Fund paid out the outstanding investment commitment in the amount of 400 thousand euros in February 2017) (31.12.2015: 570 thousand euros)

Note 9 Long-term receivables

(in euros)

	31.12.2016	31.12.2015
Long-term receivable	360,045	219,930
Total	360,045	219,930

As at 31.12.2015, the receivable of the Fund amounted to EUR 219,930 in accordance with the sale contract of portfolio shares concluded on 15.05.2015. The claim is based on a conditional time deposit (*escrow*) opened on 24.05.2015. The deposit period is 18 months.

As at 31.12.2016, the receivable of the Fund amounted to EUR 360,045 in accordance with the sale contract of portfolio shares concluded on 18.11.2016. The claim is based on a conditional time deposit (*escrow*) opened on 18.11.2016. The deposit period is 18 months.

Note 10 Trade payables and other current liabilities

(in euros)

	31.12.2016	31.12.2015
Current trade and other payables		
Trade payables	63,513	76,994
Other accruals	0	0
Total current trade and other payables	63,513	76,994

Note 11 Miscellaneous operating expenses

	2016	2015
Fund management fee (<i>Note 13</i>)	757,842	757,842
Shares' registrar fee	2,000	2,000
Services purchased	15,720	8,939
Fund's management fees (Expert Committee)	11,109	22,774
Total miscellaneous operating expenses	786,671	791,555

Note 12 Fund units and statement of comparison of the Fund's net asset value

With its decision dated 01.08.2012, the SmartCap approved the issuance of fund shares, specifying 1,247.908 shares as the size of the offering. The nominal value of one unit is EUR 10,000.

Acting on the basis of order number 171 of the Government of the Republic dated 12.04.2012 and the contract between the EDF and the Ministry of Economic Affairs and Communications dated 06.12.2011, the EDF on 02.08.2012 on behalf of the Ministry of Economic Affairs and Communications subscribed for the entire offering of 1247.908 fund shares and paid the issue price totalling EUR 12,479,080. After the Fund's terms and conditions were approved on 01.08.2012, the Fund acquired an unconditional claim and the EDF assumed an unconditional obligation to subscribe for units in the Fund.

With a decision adopted at its session of 06.12.2012 (item number 15 on the agenda) the Government of the Republic authorised the Ministry of Economic Affairs and Communications to acquire additional shares in the Fund paid for in full with a cash contribution of EUR 6,391,165.

AS SmartCap issued to the Ministry of Economic Affairs and Communications an additional 645.561 shares in the Fund. Nominal value of one unit is EUR 10,000. Shares were issued at their issue price, which was the most recent net asset value per share by the time that the purchase order from the Ministry of Economic Affairs and Communications was received as at 30.11.2012, which was EUR 9,900.1661. The Ministry of Economic Affairs and Communications subscribed for EUR 6,391,165 worth of shares and paid for them.

With a decision adopted at its session of 05.12.2013 (item number 21 on the agenda) the Government of the Republic authorised the Ministry of Economic Affairs and Communications to acquire additional shares in the Fund paid for in full with a cash contribution of EUR 6,391,165.

AS SmartCap issued to the Ministry of Economic Affairs and Communications an additional 661.851 shares in the Fund. Nominal value of one unit is EUR 10,000. Units were issued at their issue price, which was the most recent net asset value per share by the time that the purchase order from the Ministry of Economic Affairs and Communications was received as at 30.11.2013, which

was EUR 9,656.4968. The Ministry of Economic Affairs and Communications subscribed for EUR 6,391,165 worth of shares and paid for them.

Year	Fund's NAV (in euros)	Net Asset Value of the Fund unit
31.12.2016	29,119,466	11,395.6240
31.12.2015	25,170,444	9,850.2121

Note 13 Transactions with related parties

Related parties of the Fund are:

- Investee companies over which the Fund has significant influence;
- AS SmartCap and its management and senior management;
- Close family members of the aforementioned persons and companies controlled by them or under their significant influence;
- The sole unit-holder of the Fund, the Republic of Estonia, and the entities under state control or significant influence.

Excluding investment transactions, the Fund has not entered into any transactions with investee companies in 2016. Transactions involving investee companies are disclosed in Note 8. The SmartCap is paid management fees on behalf of the Fund in exchange for management of the Fund, comprised of two components: a fixed fee and a success fee. During the reporting period, management fees totaled to EUR 757,842 (2015: EUR 757,842). As at 31.12.2016, the Fund had a balance of management fees payable to the SmartCap of EUR 63,154 (31.12.2015: EUR 63,154) and other liabilities to the SmartCap of EUR 0 (31.12.2015: EUR 13,490).

Transactions involving the unit-holder, the Republic of Estonia, are disclosed in Note 12.

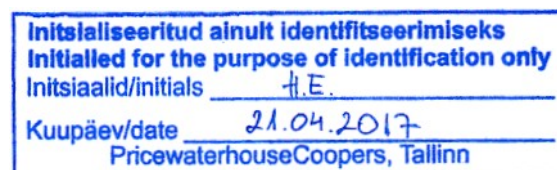
Note 14 Events after the balance sheet day and going concern

On 27.01.2016, the Supervisory Board of the EDF approved a renewed investment strategy, according to which returned capital by the EDF will be invested in accelerator funds. In 2016 accelerators selection process was started, to be completed in 2017 in the form of a competitive dialogue⁵ on the basis of the Public Procurement Act, where AS SmartCap and Fund KredEx act as joint contracting authorities.

At the beginning of 2017, SmartCap and the EDF started negotiations with representatives of Tera Ventures on the technical details of reorganization. The investment portfolio is expected to be transferred to a private fund management company in the first half of 2017, as resulting from the negotiations. Until the reorganization of the direct investment management, the Fund's direct investments will continue to be managed in accordance with the terms and conditions of the Early Fund II terms.

In the spring of 2016, the Economic Affairs Committee of Estonian Parliament concluded a principal decision to terminate the activities of the EDF, to transfer monitoring activities to a new

⁵ <https://riigihanked.riik.ee/register/hange/178587>



Foresight Centre to be created, and investment activities to composition of Fund KredEx. On 29.06.2016 Estonian Parliament adopted the Foresight Act that terminates the activities of the EDF from 29.06.2017. Transfer of investment activities of EDF (including AS SmartCap) into Fund KredEx composition takes place after conclusion of the contract with the private foundation manager, during the first half of 2017 at the latest. As resulting from the restructuring, AS SmartCap will become a subsidiary of Fund KredEx, which will continue implementation of the current investment strategy.

Regardless of the reorganization of the activities of EDF, including the transfer of AS SmartCap into Fund KredEx organization, the management of the SmartCap estimates the Fund as a continuously operating organization.

INVESTMENT STATEMENT

According to regulation of the Minister of Finance no 21 "Requirements for investment fund reports subject to disclosure" the following information of fund's investments as at 31.12.2016 has been disclosed (in euros):

Name	ISIN code (commercial registry code)	Country	Nominal value	Currency	Quantity	Average acquisition cost per unit	Total average acquisition cost	Market value per unit	Total market value	Percentage of Fund's NAV
Equity investments										
GOLIATH Wind OÜ	11441701	EE	2,188	EUR	1	-	-	-	-	-
Sportlyzer OÜ	11671051	EE	576	EUR	1	-	-	-	-	-
Realeyes (Holdings) Ltd	8922462	GB	0.001	EUR	2,571,611	-	-	-	-	-
Jobbatical OÜ	12671900	EE	1,208	EUR	1	-	-	-	-	-
Monese Ltd	08720992	UK	0.01	GBP	8,630	-	-	-	-	-
IOT Holding OÜ	12580341	EE	3,727	EUR	1	-	-	-	-	-
Lingvist Inc.	-	US	0.0001	USD	49,488	-	-	-	-	-
Scoro Software OÜ	10806081	EE	1,071	GBP	1	-	-	-	-	-
Total equity investments						10,666,090	10,666,090	-	15,805,812	54.16%
Convertible loans										
CX Cloud Services OÜ	12394106	EE	-	EUR	1	-	-	-	-	-
IOT Holding OÜ	12580341	EE	-	EUR	2	-	-	-	-	-
Thinnect OÜ	12925756	EE	-	EUR	2	-	-	-	-	-
Total convertible loans						870,000	870,000	-	726,481	2.49 %
Interest receivable										
CX Cloud Services OÜ						-	-	-	-	-
Thinnect OÜ						-	-	-	-	-
IOT Holding OÜ						-	-	-	-	-
Total interest receivable						-	-		66,481	0.23%

Cash at bank and in hand	Moody's rating	Country	Nominal value	Currency				Total market value	Percentage from market value of Fund's assets on 31.12.2016
Nordea Bank AB Estonian branch	Aa3	EE	4,015,259	EUR				4,015,259	13.76 %
Swedbank Eesti AS	Aa3	EE	3,454,173	EUR				3,454,173	11.84 %
Total cash and bank and in hand			7,469,432					7,469,432	25.60 %

Deposits	Moody's rating	Country	Nominal value	Currency	Starting Date	Maturity date	Interest rate	Total average acquisition cost	Total market value	Percentage from market value of Fund's assets on 31.12.2016
Term deposit LHV		EE	4,500,000	EUR	15.08.2016	12.02.2016	0.07%	4,500,000	4,500,000	15.42%
Total deposits			4,500,000					4,500,000	4,500,000	15.42%

Overnight deposit SEB Pank AS	A1	EE	320,010	EUR			0.01%	320,010	320,010	1.10%
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Other current receivables

Interest receivable LHV		EE	1,199	EUR				1,199	0.0041%
Total other current receivables			1,199					1,199	0.0041%

Long-term receivables		Country	Nominal value					Total market value	Percentage from market value of Fund's assets on 31.12.2016
Sale of Weather Me		EE	360,045					360,045	1.2337%
Total long-term receivables			360,045					360,045	

Total fund's assets								29,182,979	100.22%
Fund's liabilities								-63,513	-0.22%
Fund's NAV								29,119,466	100.00%

As the aforementioned equity investments and convertible loans do not constitute marketable securities, the fair value of such investments has been determined through the use of alternative information based on estimates. As the disclosure of information concerning the fair value of such investments is restricted due to confidentiality agreements in place and as it would undermine the Fund's position in exiting the investments, the average acquisition cost and the total market value or fair value of such investments is disclosed in aggregate.

As at 31.12.2015, the following information is disclosed as follows:

Name	ISIN code (commercial registry code)	Country	Nominal value	Currency	Quantity	Average acquisition cost per unit	Total average acquisition cost	Market value per unit	Total market value	Percentage of Fund's NAV
Equity investments										
GOLIATH Wind OÜ	11441701	EE	1,888	EUR	1	-	-	-	-	-
Sportlyzer OÜ	11671051	EE	576	EUR	1	-	-	-	-	-
WeatherMe OÜ	12247361	EE	864	EUR	1	-	-	-	-	-
Realeyes (Holdings) Ltd	8922462	GB	0.001	EUR	1,516,108	-	-	-	-	-
Jobbatical OÜ	12671900	EE	769	EUR	1	-	-	-	-	-
IOT Holding OÜ	12580341	EE	3727	EUR	1	-	-	-	-	-
Lingvist Inc.		US	0.0001	USD	49,488	-	-	-	-	-
Total equity investments					7	6,127,145	6,127,145	7,836,525	7,836,525	31.04%
Convertible loans										
Realeyes (Holdings) Ltd	8922462	GB	-	EUR	2	-	-	-	-	-
Monese Ltd	08720992	GB	-	EUR	2	-	-	-	-	-
Jobbatical OÜ	12671900	EE	-	EUR	1	-	-	-	-	-
Thinnect OÜ	12925756	EE	-	EUR	1	-	-	-	-	-
IOT Holding OÜ	12580341	EE	-	EUR	1	-	-	-	-	-

CX Cloud Services OÜ	12394106	EE	-	EUR	1	-	-	-	-	-
Total convertible loans					8	1,931,250	1,931,250	1,865,897	1,865,897	6.86%

Long-term receivables		Country	Nominal value						Total market value	Percentage from market value of Fund's assets on 31.12.2015
Fits.me sales (J SHAW SLCTR LTD)		EE	219,930						219,930	0.87%
Total long-term receivables			219,930						219,930	0.87%

Cash at bank and in hand	Moody's rating	Country	Nominal value	Currency					Total market value	Percentage from market value of Fund's assets on 31.12.2015
Nordea Bank AB Estonian branch	Aa3	EE	1,197	EUR					1,197	0.005%
Swedbank Eesti AS	Aa3	EE	7,901,706	EUR					7,901,706	31.30%
Total cash and bank and in hand			7,902,903						7,902,903	31.30%

Term deposits	Moody's rating	Country	Nominal value	Currency	Starting Date	Maturity date	Interest rate	Total average acquisition cost	Total market value	Percentage from market value of Fund's assets on 31.12.2015
Fixed term deposit Nordea Bank AB Estonian branch	Aa3	EE	3,000,000	EUR	17.07.2015	18.01.2016	0.30%	3,000,000	3,000,000	11.88%
Fixed term deposit Nordea Bank AB Estonian branch	Aa3	EE	4,000,000	EUR	20.10.2015	20.10.2016	0.23%	4,000,000	4,000,000	15.84%
Total term deposits			7,000,000					7,000,000	7,000,000	27.73%

Overnight deposit SEB Pank AS	A1	EE	398,664	EUR			0.01%	398,664	398,664	1.58%
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Other current receivables

J Shaw SLCTR LTD (Fits.me sales)		EE	17,454	EUR					17,454	0.07%
Interest receivable Nordea		EE	1,866	EUR					1,866	0.0074%
Interest receivable Nordea		EE	4,200	EUR					4,200	0.0166%
Total other current receivables			23,520						23,520	0.09%

Total fund's assets									25,247,438	100.31%
Fund's liabilities									-76,994	-0.30%
Fund's NAV									25,170,444	100.00%

As the aforementioned equity investments and convertible loans do not constitute marketable securities, the fair value of such investments has been determined through the use of alternative information based on estimates. As the disclosure of information concerning the fair value of such investments is restricted due to confidentiality agreements in place and as it would undermine the Fund's position in exiting the investments, the average acquisition cost and the total market value or fair value of such investments is disclosed in aggregate.



INDEPENDENT AUDITOR'S REPORT

(Translation of the Estonian original)*

To the Shareholder of Early Fund II

Our opinion

In our opinion, the annual statements present fairly, in all material respects, the financial position of Early Fund II (the Fund) managed by AS SmartCap (the Management Company) as at 31 December 2016, and its financial performance and its cash flows for the year then ended in accordance with the Investment Funds Act.

We audited the Fund's annual statements that comprise:

- the financial statements that comprise:
 - the statement of financial position as at 31 December 2016;
 - the statement of comprehensive income for the year then ended;
 - the statement of cash flows for the year then ended;
 - the statement of changes in the Fund's net asset value for the year then ended; and
 - the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information; and
- the statement of investments.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Fund's annual statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the ethical requirements of the Auditors Activities Act of the Republic of Estonia. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code and the ethical requirements of the Auditors Activities Act of the Republic of Estonia.



Other information

The Management Company's Management Board is responsible for the other information contained in the Fund's annual report in addition to the Fund's annual statements and our auditor's report thereon.

Our opinion on the Fund's annual statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the Fund's annual statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the Fund's annual statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Management Company's Management Board and those charged with governance for the Fund's annual statements

The Fund's Management Company's Management Board is responsible for the preparation and fair presentation of the Fund's annual statements in accordance with the Investment Funds Act and for such internal control as the Management Company's Management Board determines is necessary to enable the preparation of the Fund's annual statements that are free from material misstatement, whether due to fraud or error.

In preparing the Fund's annual statements, the Fund's Management Company's Management Board is responsible for assessing the Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Fund's Management Company's Management Board either intends to liquidate the Fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Fund's financial reporting process.

Auditor's responsibilities for the audit of the Fund's annual statements

Our objectives are to obtain reasonable assurance about whether the Fund's annual statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this annual statements of the Fund.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the Fund's annual statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.



- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management Company's Management Board.
- Conclude on the appropriateness of the Management Company's Management Board's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the Fund's annual statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the Fund's annual statements, including the disclosures, and whether the Fund's annual statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

AS PricewaterhouseCoopers

/signed/

Tiit Raimla
Auditor's certificate no.287

/signed/

Verner Uiibo
Auditor's certificate no.568

21 April 2017

** This version of our report is a translation from the original, which was prepared in Estonian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.*