

HERALD INVESTMENT TRUST plc

REPORT & ACCOUNTS

31 December 2000

# CONTENTS

1	Company Summary
2	Year's Summary
3	Long Term Performance Summary
4	Directors, Manager and Advisers
5	Chairman's Statement
6	Investment Manager's Report
10	Top Twenty Holdings
12	Classification of Investments
12	Geographical Spread of Investments
13	Detailed List of Investments
17	Long Term Record
18	Directors' Report
20	Statement of Directors' Responsibilities
21	Corporate Governance
23	Auditors' Report
24	Statement of Total Return
25	Balance Sheet
26	Cash Flow Statement
27	Notes to the Accounts
35	Notice of Annual General Meeting
36	Further Shareholder Information

# COMPANY SUMMARY

## COMPANY DATA AT 31 DECEMBER 2000

Total assets less current liabilities	Shareholders' funds	Market capitalisation
£379m	£375m	£427m

**Policy and Objective** Herald's objective is to achieve capital appreciation through investments in smaller quoted companies, principally in the UK but also in the rest of the world, in the areas of communications and multi-media. The business activities of investee companies will include information technology, broadcasting, printing and publishing and the supply of equipment and services to these companies.

**Benchmark** The portfolio benchmark against which performance is measured is  $\frac{2}{3}$  Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies) and  $\frac{1}{3}$  Russell 2000 (small cap) Technology Index (in sterling terms).

**Management Details** Herald Investment Management Limited ('HIML') are appointed investment managers to the Company. The management contract can be terminated at twelve months' notice. Administration of the Company and its investments is contracted by HIML to Baillie Gifford & Co., who also act as company secretary.

**Capital Structure** The Company's share capital consists of 83,873,599 ordinary shares of 25p each which are issued and fully paid.  
There are also 3,933,750 Warrants which are exercisable at 100p on 30 April in any of the remaining years 2001 to 2003.

**Management Fee** Herald Investment Management Limited's annual remuneration is 1.0% of the Company's net asset value, calculated on a monthly basis.

**Wind-Up** The Company's Articles of Association require the Directors to propose an ordinary resolution at the Annual General Meeting of the Company in 2004 (and at every third subsequent Annual General Meeting) proposing that the Company will continue to operate as an investment trust company.

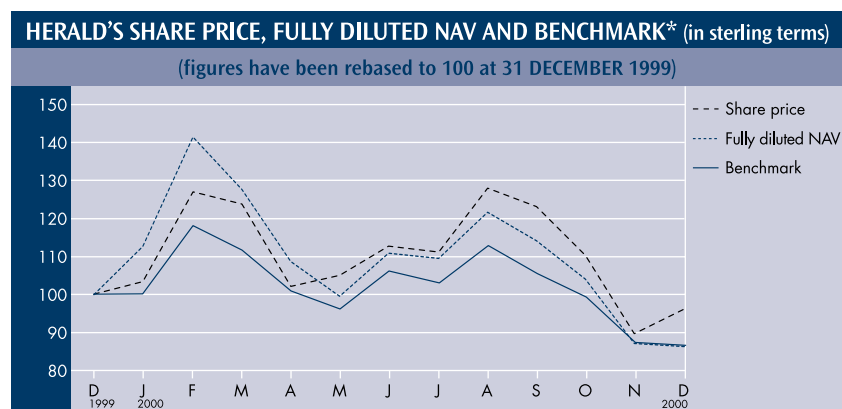
**AITC** The Company is a member of the Association of Investment Trust Companies.

## YEAR'S SUMMARY

	31 December 2000	31 December 1999	% change
Total assets (before deduction of bank loan)	£378.6m	£432.6m	(12.5)
Bank loan	£3.2m	£3.3m	3.0
Equity shareholders' funds	£375.4m	£429.3m	(12.6)
Net asset value per ordinary share	447.5p	517.4p	(13.5)
Diluted net asset value per ordinary share (FRS 14)	431.4p	494.2p	(12.7)
Fully diluted net asset value per ordinary share	432.0p	494.4p	(12.6)
Share price	491.0p	511.0p	(3.9)
Warrant price	382.5p	411.0p	(6.9)
FTSE 100	6,222.5	6,930.2	(10.2)
FTSE All-Share	2,983.8	3,242.1	(8.0)
FTSE Small Cap	3,183.3	3,097.8	2.8
Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies)	2,702.2	2,762.9	(2.2)
Russell 2000 (small cap) Technology Index (in sterling terms)	128.3	199.8	(35.8)
Benchmark composite index			(12.3)
Dividend per ordinary share	0.85p	0.85p	-
Earnings per ordinary share (basic)	0.93p	0.86p	8.1
Expense ratio	1.40%	0.95%	47.4
Premium/(discount) (to basic net asset value)	9.7%	(1.2%)	
Premium/(discount) (to diluted net asset value (FRS14))	13.8%	3.4%	

Year's high and low (on month end values)	Year to 31 December 2000		Year to 31 December 1999	
	High	Low	High	Low
Share price	652.5p	458.0p	511.0p	190.0p
Warrant price	551.5p	361.5p	411.0p	98.0p
Net asset value	732.6p	447.3p	517.4p	218.6p
Fully diluted net asset value	697.7p	431.7p	494.4p	212.0p
Premium/(discount) (to fully diluted net asset value)	13.8%	(7.2%)	3.4%	(11.1%)

	31 December 2000	31 December 1999
<b>Total return per ordinary share (basic)</b>		
Revenue	0.93p	0.86p
Capital	(65.67p)	311.33p
Total	(64.74p)	312.19p



Source: Primark Datastream.

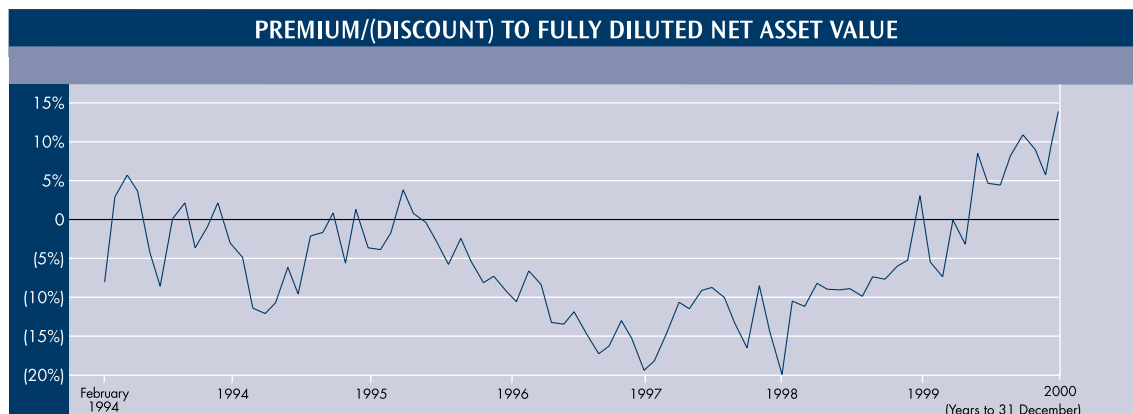
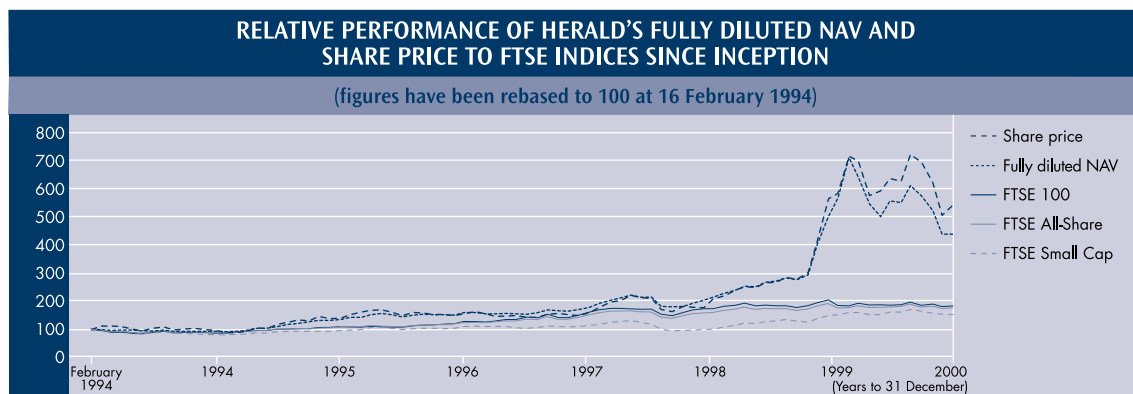
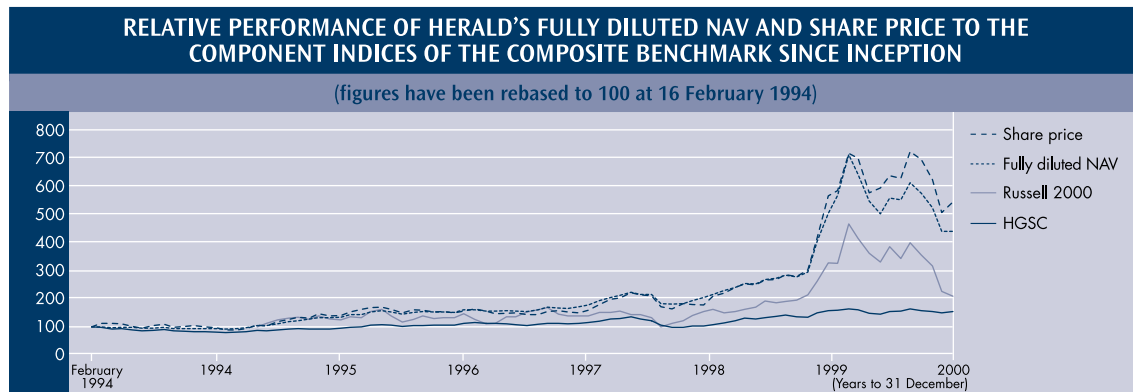
\*2/3 Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies) and 1/3 Russell 2000 (small cap) Technology Index (in sterling terms).

## LONG TERM PERFORMANCE SUMMARY

The following charts indicate how an investment in Herald has performed relative to its comparative indices (applied retrospectively) and its underlying fully diluted net asset value over the period since inception of the Company.

	31 December 2000	Inception 16 February 1994	% change
Fully diluted net asset value per ordinary share	432.0p	98.7p	337.7
Share price	491.0p	90.9p	440.2
Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies)	2,702.2	1,750.0	54.4
Russell 2000 (small cap) Technology Index (in sterling terms)	128.3	61.3*	109.3
FTSE 100	6,222.5	3,417.7	82.1
FTSE All-Share	2,983.8	1,717.8	73.7
FTSE Small Cap	3,183.3	2,076.1	53.3

\* at 31 May 1995.



The premium/(discount) is the difference between Herald's quoted share price and its underlying fully diluted net asset value.

## DIRECTORS, MANAGER AND ADVISERS

### Directors

**Martin Boase, MA, FIPA** (Chairman), aged 68, formed advertising agency Boase Massimi Pollitt plc in 1968 which was floated on the London Stock Exchange in 1983. He was chairman of the Advertising Association from 1987 to 1992 and is currently chairman of The Maiden Group plc, Heal's plc, The Investment Trust of Investment Trusts PLC and Jupiter Dividend and Growth Investment Trust PLC.

**Timothy Abell, MA**, aged 70. He was formerly deputy chairman of Baring Investment Management Limited, chairman of Foreign & Colonial Eurotrust plc and chairman of the Association of Investment Trust Companies.

**Justin Dukes**, aged 59, is chairman of ECIC Management Limited, Intelmedia Limited and Picdar Limited and is a director of VTR plc. He was the founding managing director of Channel Four Television and joint managing director of the Financial Times Group. He is a former president of the Institute of Information Scientists and is a Companion of the Institute of Management.

**Colin McCarthy, FCA, MCT**, aged 63, joined Bowthorpe plc (now Spirent plc, the international network technology company) in 1962, and was financial director from 1982 until his retirement in 1999.

**Clive Parritt, FCA**, aged 57, is chief executive of The Business Exchange plc (a leading independent corporate finance house). He is a member of the Council of the Institute of Chartered Accountants in England and Wales. He is chairman of 422 Limited and a number of Venture Capital Trusts including Baronsmead VCT2 plc and Downing Classic VCT plc. He was, until February 2001, chairman of Baker Tilly, Chartered Accountants, having been its national managing partner for 10 years until June 1996. He has over 25 years' experience of providing financial and commercial advice to smaller and medium sized businesses in a wide range of industries.

### Secretary

Baillie Gifford & Co.  
1 Rutland Court  
Edinburgh EH3 8EY  
Tel: 0131 222 4000

### Registered Office

12 Charterhouse Square  
London EC1M 6AX

### Company Number

2879728 (England and Wales)

### Manager

Herald Investment Trust plc is managed by Herald Investment Management Limited ("HIML"). The senior director of HIML with prime responsibility for the management of Herald Investment Trust is Katie Potts.

### Katie Potts

Herald Investment Management Limited  
12 Charterhouse Square  
London EC1M 6AX  
Tel: 020 7553 6300  
Fax: 020 7490 8026  
Web-site: [www.heralduk.com](http://www.heralduk.com)  
E-mail: [info@heralduk.com](mailto:info@heralduk.com)

### Advisers

#### Solicitors

Macfarlanes  
10 Norwich Street  
London EC4A 1BD

#### Auditors

Ernst & Young  
Ten George Street  
Edinburgh EH2 2DZ

#### Bankers

The Bank of New York Europe Limited  
67 Lombard Street  
London EC3P 3DL

#### Stockbroker

UBS Warburg Limited  
1 Finsbury Avenue  
London EC2M 2PP

#### Registrars

Northern Registrars Limited  
Northern House  
Woodsome Park  
Fenay Bridge  
Huddersfield HD8 0LA  
Tel: 01484 600 900  
Fax: 01484 600 911

## CHAIRMAN'S STATEMENT

This is the seventh annual statement I have made for Herald Investment Trust, and disappointingly the poorest we have had to make. The diluted net asset value per share has declined by 12.7% during the year, although this was alleviated by a more modest 3.9% decline in share price – an increase in the share price premium to assets. In contrast the most relevant index, the Hoare Govett Smaller Companies Index, declined 2.2%. In comparison, in 1999 the Trust outperformed this benchmark by 93.3%, and has cumulatively outperformed since inception by nearly 300%. The 2000 decline reflected the hangover following a period of wild speculative froth in certain stocks within our chosen remit. On balance we were lucky to use that bubble as an opportunity to realise some supernormal profits on valuations that fundamentals did not justify. The market is now becoming much more rational. The US index, which is most relevant to our US portfolio, is the Russell 2000 (small cap) Technology Index, which fell 40.4%, albeit only 35.8% in £ terms, compared to our own decline in the US of 25.4%. Overall we were only 0.7% behind our hybrid benchmark index.

This year's profit shows a marginal improvement reflecting increased income from a higher cash/gilt element than the Trust has normally held. This is associated with our cautious view of market levels, which is offset by increased expenses, a follow-on from the rise in assets in 1999. While growth remains the focus of the fund, the income and hence the dividend, will be low. However, unlike Technology Trusts, Herald is pleased to say that we have always been able to pay a dividend out of current years' profits.

For long periods of the year the Trust achieved the distinction of being the best performing Trust over 5 years in tables appearing in the FT. The Trust no longer features in this table because the AITC thought it was inappropriate to be classified as a UK smaller companies Investment Trust. About 60% of the equities held are UK small companies, and there remains a stronger overlap in stock terms with these funds than the global technology funds with which we are sometimes compared. This is evidenced by a much stronger performance than any of the technology indices (techMARK –32.2%, FTSE IT Index –44.3%, NASDAQ –39.3%). We remain of the view that we are primarily UK smaller companies Investment Trust, albeit only investing in a subset of that remit. We believe that there are still opportunities to perform in our defined remit, and while the Manager's report will expand on some of the tangible issues we face, we continue to believe that there are opportunities to invest in solid growing businesses – many more now than a year ago.

*Martin Boase*  
Chairman

27 February 2001

## INVESTMENT MANAGER'S REPORT

It is frustrating to report a decline in total net assets of 13%, when returns in the first quarter were so strong. Nevertheless, it has required aggressive profit taking in certain stocks, which benefited from the speculative bubble that started in Q4 1999, and continued until March, to limit the losses to that level. The focus of the bubble was the Internet sector, which is so central to Herald's target investment remit, but it broadened to anything related to technology, and to a lesser extent, traditional media. As a long-term investor, focused on fundamental returns from our investments, the moves were bewildering. We have now seen material corrections in all the technology based markets, which is, from our perspective, a great relief. The German Neuer Markt in particular was notable as the bubble based on the least substance, and has declined from over 8,500 in March to c.2,000 now. A level, which is lower than any time since Autumn 1998. The FTSE techMARK 100 Index, which was launched at an incredibly unfortunate time, because it fuelled the fire, has now come back almost to a level it was launched at in October 1999. NASDAQ has similarly fallen by more than half, from the peak of 5,048 to 2,471 at the year-end, and was down 39.3% in the year. The FTSE IT Index was down 44.3%. Bearing in mind the fact that UK software companies, including support services, were the largest element of the portfolio at the end of 1999 (c1/3rd), aggressive profit taking was required. In spite of reducing the holding in Sherwood from 10% of the Company to 3.1% it still fell in value by £12.2m, and IMS/Teamtalk fell by as much. In contrast, Autonomy yielded a profit during the year of £12m, reflecting greater liquidity, and the ability to sell the holding. Other profitable stocks included Alphameric (£6.1m), Telemetrix (£5.7m), Surf Control (£4.5m) and Anite (£2.1m). In the US, Burr Brown, which was acquired by Texas Instruments, contributed well (\$6.2m), and profits during the year on Mercury Interactive of \$4.4m were realised. In Switzerland Logitech contributed SwFr4.9m, but this was offset by losses of SwFr5.5m on Publigroupe, a holding that has done well since purchase in 1996, and did particularly well in 1999. In the UK EDP disappointingly fell £5.4m. This enjoyed an extraordinary run in the early part of the year, but there was no liquidity. It has now fallen to asset value on equally low volumes.

The overall portfolio fell by less than the returns on each geographic segment (except UK) reflecting the high levels of cash and gilts held. This approached £100m in April, but has fallen to £58.4m at the year-end. In retrospect, reinvestment of cash was too early, but the investments were generally in lower risk areas. The media element of the portfolio has proved much more resilient, with interesting returns from Scottish Radio and Jazz FM.

### Portfolio performance attribution for the 12 months to 31 December 2000.

Computed relative to customised benchmark ( $\frac{2}{3}$  Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies) and  $\frac{1}{3}$  Russell 2000 (small cap) Technology Index (in sterling terms)).

PERFORMANCE ATTRIBUTION (in sterling terms)								
	Benchmark	Herald		Performance*		Contribution to relative return	Contribution attributable to:	
	allocation	asset allocation		Herald	Benchmark		Stock selection	Asset allocation
	01.01.00	01.01.00	31.12.00	Herald	Benchmark			
Equity markets	%	%	%	%	%	%	%	%
UK	66.7	63.5	56.8	(12.1)	(2.2)	(6.0)	(4.1)	(2.0)
Europe ex. UK	–	6.7	7.2	(15.0)	–	(0.2)	–	(0.2)
Americas	33.3	16.3	16.9	(25.4)	(35.8)	5.5	2.7	2.7
Japan	–	0.3	0.7	(19.5)	–	(0.1)	–	(0.1)
Asia Pacific ex. Japan	–	6.6	4.6	(37.1)	–	(2.0)	–	(2.0)
Bonds	–	1.0	12.2	1.2	–	2.0	–	2.0
Cash	–	5.6	1.6	3.0	–	0.4	–	0.4
Total	100.0	100.0	100.0	(13.0)	(12.3)	(0.7)	(1.4)	0.7

Source: HSBC.

\* The above figures represent the capital returns on the Company's portfolio.

Contributions cannot be added together, they are geometric; for example, to calculate how a return of (13.0%) (against a benchmark of (12.3%)) translates into a relative performance of (0.7%), divide the portfolio performance of 87.0 by the benchmark year end figure of 87.7.



## INVESTMENT MANAGER'S REPORT *continued*

### Market Background

Five major markets have become much more difficult: PCs, mobile phones, telecommunications, Internet business to consumer and business-to-business web sites, as well as traditional terrestrial TV.

1. **PCs.** This market has been the most extraordinary driver to growth for many companies, both directly and indirectly. The first PC appeared less than twenty years ago, some of the biggest companies have emerged from this market including Microsoft, Intel, Dell, and indirectly, Cisco, which has led the networking trend. Levels of penetration are now great, there is no technology necessitating a replacement cycle; computers purchased over the last couple of years can provide the killer applications of word processing, spreadsheets and internet access. Furthermore, the average selling price is declining, and market consolidation has been sufficient to make market share gains for the industry leaders more difficult to achieve. Even worse, there is an emergence of 'thin clients', terminals that can provide limited functionality, but sufficient for some applications. These include WB TVs for Internet access, personal digital appliances, and within the office, thin client terminals, which rely on central processing. These stocks have performed poorly and account for large blocks of market capitalisation. It is difficult to see any justification for performance even from these levels, because global PC volumes are expected to rise 10–15% in 2000 but in monetary terms by only 2%.

2. **Mobile Phones.** This sector has been another amazing growth market. In 2000, c.40% of phones were replacement ones. This is expected to rise to 45% in 2001. The market leaders have had product differentials such as better battery life. As the market matures these differentials will erode, hence the need for the third generation (3G) broadband to sustain the market for the equipment manufacturers, and the service providers alike. Whilst the need for broadband internet access is necessary for web TVs, for which a huge market is probable, it is more difficult to be sure that there is the need for broadband mobile communications. Worldwide c.412,000,000 mobile phones were sold in 2000 and estimates for 2001 have fallen to little more than 500,000,000 so the market is rapidly maturing. We believe there are enormous risks in this sector.

3. **Telecommunications.** This sector has been exposed to divergent influences. Positively, large growth in data traffic, with the emergence of the Internet. Negatively, the collapse of monopolies and the emergence of competition, combined with technological developments such as wave division multiplexing, which is expanding capacity more cheaply than previously imagined. With a dose of irrational euphoria, competing carriers raised cheap capital. The outcome was inadequate returns, and now funding fears, as cheap capital has become expensive or even unavailable. Whilst this will inevitably lead to more circumspect capital expenditure by the carriers, there is an enormous market for increased bandwidth both by the consumer and businesses. This will provide opportunities for equipment suppliers even if the carriers' margins will continue to be pressured. Selection is the key.

4. **B-to-B/B-to-C.** With regard to the Internet, investment judgement was very poor. People did not always recognise that a business model was simply not viable, whereas for others, expectations were just too high. Herald had limited benefit from this sector during the bubble, something that reflects our fundamental approach. On the downside it was an advantage.

5. **TV.** Herald has not been invested in traditional terrestrial TV for sometime. In part, as consolidation has occurred, there are no smaller companies left. In part we have held the strategic view that the value of a terrestrial licence has been radically reduced by the arrival of more terrestrial channels, satellite and cable. Furthermore, increased use of the Internet by the consumer will eat into TV viewing time. This fragmentation will make TV advertising rates hard to sustain, but is providing growth in other media e.g. Radio, Outdoor, Direct mail, and production, reflecting the increased use of rich media in various cheap distribution channels. This provides opportunities for small companies.

Overall the simultaneous emergence of the PC and the mobile phone, closely followed by the Internet, provided an extraordinary background for supernormal profits. Technology is still opening new markets, and we continue to believe that with our smaller company focus we will be able to identify new opportunities for growth. Nevertheless, we would caution against expectations for performance from many of yesterday's growth markets.

## INVESTMENT MANAGER'S REPORT *continued*

INVESTMENT CHANGES (£'000)				
	Valuation at 31 December 1999	Net acquisitions (disposals)	Appreciation (depreciation)	Valuation at 31 December 2000
Equities:				
UK	272,750	(44,437)*	(17,341)	210,972
Continental Europe	28,774	3,038*	(4,478)	27,334
Americas	69,284	14,307	(20,882)	62,709
Japan	1,296	1,619	(535)	2,380
Asia Pacific	29,129	(54)	(12,226)	16,849
	401,233	(25,527)	(55,462)	320,244
UK bonds	4,068	40,870	393	45,331
Total investments	405,301	15,343	(55,069)	365,575
Net liquid assets	27,319	(14,366)	79	13,032
Total assets	432,620	977	(54,990)	378,607

\*The takeover of Saatchi & Saatchi by Publicis Group results in the holding being transferred from UK to Continental Europe, with the market value of the holding in Saatchi & Saatchi at the date of takeover of £2,171,000 (book cost – £795,000) being included within the disposals and acquisitions figures respectively.

The figures above for total assets comprise assets less current liabilities before deduction of bank loan.

### Geographic Comment

#### UK

The stated return is a decline of 12.1% and is measured on a compounding monthly rate. The above table shows a capital decline of £17m in the UK – much more modest than the monthly compounded rate suggests and reflects realisations of £87m in the first half year, albeit offset by the reinvestment of £36m in more defensive stocks. While it remains frustrating not to have liquidated even more our excuses are:

1. Markets are not wholly rational, sales made in December 1999 looked foolish by February but wise a year later.
2. The top of the market was apparent but volume dried up.

Nevertheless, it reflects an underperformance relative to our benchmark of 9.9%. This marks underperformance in the UK for the first time in the seven-year history of the Trust, and is therefore particularly disappointing to report. It is even more disappointing to argue that we have returned to more normal valuation levels rather than compellingly cheap ones. The most fundamental positive to put forward is that there have been an unprecedented number of start-up companies in the UK in the recent past. One of the most demoralising aspects of the boom was that interesting companies were floated on absurdly high valuations. I am optimistic that we will have many more sensible opportunities in the next few months. Let us hope too that some of the larger investment banks return to valuing their reputations more than their bonuses! Unlike some funds we have not 'played the new issue game', which is another phenomenon that has added to the instability in the sector. So many marginal players came into the market to turn new issues. When the music stopped, certain companies had share registers of investors who were not long term.

The media sector has provided some ballast to the portfolio. While the returns on the upside have been less spectacular, the sector has not suffered the same correction. Indeed many of the traditional media stocks benefited from the surge in dot.com advertising.

On balance we believe that the UK will not fall into recession. If that proves the case then many current valuations provide a sensible level for future gains.

#### US

In spite of NASDAQ's weakness, the strength of so many US technology companies is awesome. Even the US market, with all its sophistication, got carried away with the Internet sector, but there are now some outstanding companies with very interesting valuations. Unlike the Neuer Markt, the speculative bubble was built on solid profits and businesses. The dilemma is the technical factors caused by a much broader awareness of the stock market amongst consumers, reflecting much broader direct investing, and share options forming a much greater part of remuneration. The NASDAQ correction has the potential to stimulate recessionary conditions in the economy as a whole, which will, in general, make

## INVESTMENT MANAGER'S REPORT *continued*

attractive stock market returns difficult to achieve anywhere. Our aim is to pick stocks that will prove to have long-term value.

The US portfolio declined by 25.4% in £ terms. The most relevant index is the Russell 2000 (small cap) Technology Index, which declined by 40.4% or 35.8% in £ terms.

### Europe

Overall, Europe has been one of the worst markets, but not the most difficult. Many of the collapses were predictable. Many argue that the US is more vulnerable after the exceptional growth rates it has enjoyed. From the micro perspective, in Europe there has not been the same degree of entrepreneurialism or the same degree of technical expertise. The one area in which Europe has led, is mobile phones, where Nokia and Ericsson have emerged as the GSM leaders. It will be difficult for them to maintain this position in 3G, which is based on CDMA technology, used in the US, and not TDMA used in GSM.

The German Neuer Markt has declined by 43%, but this is compounded by the weakness of the Euro so the £ return is -52%.

The European performance benefited from the takeover of Avenir in Norway, as well as the strong performance of Logitech. Highwave Optical also proved the best % return in the portfolio this year, +480% to give a realised profit of €855,000. This limited the decline to 15.0% in spite of the adverse currency movements.

### Far East

The Far East declined 35.6% in £ terms which was the poorest performing region. A number of Asian stock markets suffered from deteriorating economic and political fundamentals. Within the broad markets technology stock prices were driven to overvalued levels in the first quarter as retail investors bought into the technology boom. The fortunes of Asia technology companies are closely linked to the global electronics cycle and stocks fell back to earth as the outlook for cycle worsened over the year.

### Administration of the Trust

We were sorry that we had to accept the resignation of Stewart Ivory as Company Secretary following their acquisition by Colonial First State Investments. From September Baillie Gifford have assumed responsibility for the secretarial and administration function of the Trust. The fund management team at Herald Investment Management Ltd continues in place.

### Outlook

Whilst we are much more comfortable in a less speculative environment, there are clearly greater macro concerns than there have been for some time. Nevertheless there are strong contractual commitments to equity markets through the culture of pensions and contractual savings. The sheer weight of cash makes a disaster scenario unlikely. Herald, with its smaller company exposure, has been fortunate in making spectacular returns from certain stocks. We are optimistic that similar opportunities will continue to emerge. We have the scope to invest cash balances, and to reposition the portfolio less defensively in due course.

### Areas of Interest include:

#### Communications and Networking

- "Always-on"
- Broadband
  - Cable, xDSL
  - Wireless
- Bandwidth
  - Local Loop
  - Metropolitan
  - Backbone
- Optical

#### Business Intelligence

- IT
  - Cost versus Revenue Driver
- Leverage "Digital Assets"
  - Internet – SFA, SCM
  - External – B2B/B2C, CRM, SCM
- Content Management
- Knowledge Management

#### The "Post-PC" Era

- Mobile/Wireless Access
  - Bluetooth
  - Wireless Ethernet
  - Next Generation Mobile Networks
- Non-PC Devices
  - PDAs
  - Mobile Phones
  - Internet Appliances
  - Set-Top Boxes

#### Hardware

- Storage Area Networks
- Network Attached Storage
- Security
- Semiconductors
- Manufacturing Outsourcing

#### Multi-Media Communications

- Cable TV
- Satellite Broadcasting
- Unified Messaging
- Interactivity
- Personalisation/Filtering

#### Media and Internet

- Content
- Convergence
- E-Business
- E-Commerce
- Security

#### Services

- Ongoing Skills Shortage
- Outsourcing

## TOP TWENTY HOLDINGS

A brief description of the twenty largest holdings in companies, and the comments thereon of the Investment Manager, are as follows:

### Telemetrix plc

Telemetrix primarily serves the international telecommunications and networking industries. It has two main businesses in the UK-Zetex which manufactures specialist semiconductors, and Trend which manufactures telecommunications test equipment targeting the ISDN market.

Country	United Kingdom
Valuation	£13,531,000
% of total assets	3.6
% of issued share capital held	3.8

### Anite Group plc

Anite is a group supplying IT products and services. It focuses on certain vertical markets including travel and telecoms. They have a German subsidiary supplying ERP, CRM and SRM integration consultancy and services.

Country	United Kingdom
Valuation	£8,863,000
% of total assets	2.3

### Azlan Group plc

Azlan is the leading European distributor of networking products. Cisco is its largest supplier. It is also focusing on security products, another growth area with suppliers such as RSA, and training.

Country	United Kingdom
Valuation	£7,762,000
% of total assets	2.1
% of issued share capital held	3.9

### Alba plc

Alba designs and sells audio and video equipment, TVs, domestic appliances, power tools, electronic garden tools and giftware. It sells its products in the UK and Europe.

Country	United Kingdom
Valuation	£7,747,000
% of total assets	2.0

### Acal plc

Acal distributes electronic components, industrial controls and document imaging equipment and also repairs and distributes personal computer parts. Acal operates worldwide, but has a high proportion of its sales in Continental Europe.

Country	United Kingdom
Valuation	£7,113,000
% of total assets	1.9
% of issued share capital held	4.0

### Scottish Radio Holdings plc

Scottish Radio has leading radio stations such as Radio Clyde, and has successfully diversified into Northern Ireland newspapers. It is currently in a bid situation.

Country	United Kingdom
Valuation	£7,061,000
% of total assets	1.9

### Alphameric plc

Alphameric provides point to multipoint data broadcast services using satellite and terrestrial broadcast. It also provides the associated systems and services, and is having notable success in the betting industry. It also supplies EPOS systems for the retail industry and keyboards.

Country	United Kingdom
Valuation	£6,659,000
% of total assets	1.8

### Informa Group plc

Informa was formed by the merger of IBC and LLP. It runs targeted conferences for professional audiences of between 25-250 people. The publishing division publishes about 200 newsletters, and the leading title is Lloyds List.

Country	United Kingdom
Valuation	£6,000,000
% of total assets	1.6

### Tempus Group plc

Tempus is a media buyer based in the UK. It also has overseas operations principally in Continental Europe.

Country	United Kingdom
Valuation	£5,802,000
% of total assets	1.5

### Linx Printing Technologies

Linx is a manufacturer of continuous ink jet printers. As the installed base grows so does the recurring revenue stream from the sale of inks. The acquisition of a laser business has proved successful.

Country	United Kingdom
Valuation	£5,369,000
% of total assets	1.4
% of issued share capital held	9.9

## TOP TWENTY HOLDINGS *continued*

### ARM Holdings plc

ARM designs RISC microprocessors that are designed into embedded applications by its customers. The business model provides a visible royalty stream for the life of the customers' products.

Country	United Kingdom
Valuation	£5,313,000
% of total assets	1.4

### RSA Security Inc

RSA is the leading player in network security. It has three areas of revenue: (i) Bsafe which is installed on PCs (via Microsoft) and mobile phones; (ii) SecirID for user authentication; (iii) Keon is their PKI (public key infrastructure) product and has the greatest growth potential.

Country	United States
Valuation	£5,132,000
% of total assets	1.4

### GWR Group plc

GWR has emerged as one of the UK leaders, following an aggressive acquisition policy. They are also the leaders in digital radio.

Country	United Kingdom
Valuation	£4,781,000
% of total assets	1.3

### N.R.J. Groupe

NRJ is one of the major operators of commercial radio stations in France. It also has interests in radio stations in a number of other European countries including Belgium, Switzerland and Sweden.

Country	France
Valuation	£4,745,000
% of total assets	1.3

### Surfcontrol plc

Surfcontrol, formerly called JSB, was founded in 1981 as an ICL VAR, but switched in 1988 to sell exclusively its own software products, particularly MultiView, a product that enabled computer users to use multiple applications on the same terminal. More recently it has concentrated on developing and marketing a suite of software products enabling network managers to control the usage of the Internet on corporate networks – for example prohibiting access to unsuitable sites.

Country	United Kingdom
Valuation	£4,449,000
% of total assets	1.2

### Sherwood International plc

Sherwood's traditional strength lay in software products for the Lloyds insurance market. The areas of growth are facilities management, and Amarta, a life insurance product.

Country	United Kingdom
Valuation	£4,286,000
% of total assets	1.1
% of issued share capital held	3.1

### Superscape plc

Superscape develops p.c. based virtual reality software, which gives images in three dimensions at low cost. The company is at an embryonic stage, but has developed Lego's Creator product, on which it receives a royalty and has on-going business with Intel.

Country	United Kingdom
Valuation	£4,034,000
% of total assets	1.1
% of issued share capital held	4.5

### Ubinetics Holdings

Ubinetics develops leading edge wireless communication solutions. In particular 3G test equipment, and GSM phones to operate with PDAs—Palm in particular.

It is a subsidiary of PA Consulting.

Country	United Kingdom
Valuation	£4,000,000
% of total assets	1.1

### Rolfe & Nolan plc

Rolfe & Nolan is a leading supplier of software for Futures and Options. It has a high element of recurring revenues, and a growing presence in the US.

Country	United Kingdom
Valuation	£3,517,000
% of total assets	0.9
% of issued share capital held	6.4

### Bloomsbury Publishing plc

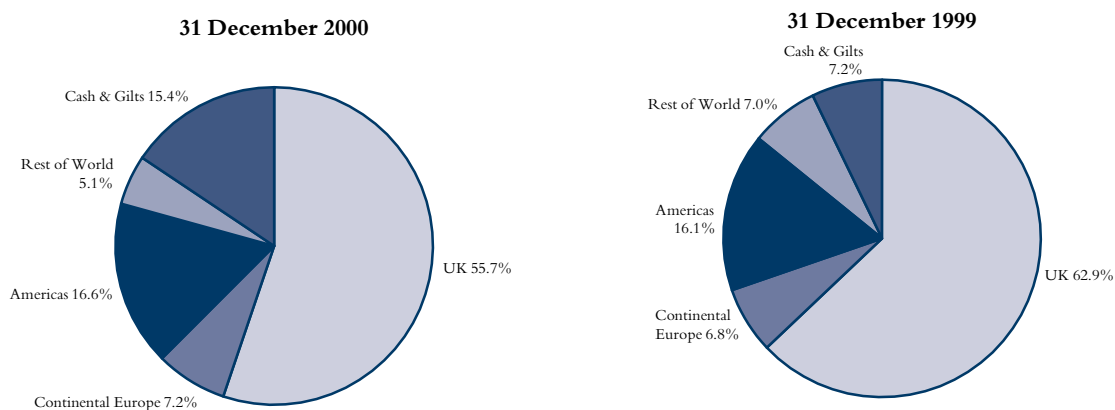
Bloomsbury is a publisher, which Herald invested in at flotation. It has benefited from publishing Harry Potter, and Microsoft commissioned Bloomsbury to create their Encarta dictionary. It acquired A&C Black, publishers of Who's Who in 2000.

Country	United Kingdom
Valuation	£3,380,000
% of total assets	0.9

## CLASSIFICATION OF INVESTMENTS

Classification	Continental					2000 Total %	1999 Total %
	UK %	Europe %	Americas %	Japan %	Asia Pacific %		
<b>EQUITIES:</b> (including convertible and preference stock)							
<b>INDUSTRIALS</b>	<b>4.6</b>	<b>1.5</b>	<b>2.6</b>	<b>0.6</b>	<b>1.4</b>	<b>10.7</b>	<b>12.6</b>
Aerospace and defence	–	–	0.1	–	–	0.1	–
Electronic and electrical equipment	4.6	1.5	2.5	0.6	1.4	10.6	12.6
<b>CONSUMER GOODS</b>	<b>0.2</b>	<b>–</b>	<b>0.1</b>	<b>–</b>	<b>–</b>	<b>0.3</b>	<b>0.2</b>
Healthcare and pharmaceuticals	0.2	–	0.1	–	–	0.3	0.2
<b>SERVICES AND UTILITIES</b>	<b>24.8</b>	<b>2.1</b>	<b>4.0</b>	<b>–</b>	<b>2.4</b>	<b>33.3</b>	<b>37.1</b>
Distributors	4.8	–	1.4	–	–	6.2	3.7
Retailers	–	–	–	–	0.1	0.1	0.1
Leisure, entertainment and hotels	0.3	–	0.1	–	–	0.4	–
Media and photography	15.6	2.0	0.9	–	2.1	20.6	21.8
Support services	3.0	–	1.5	–	–	4.5	4.8
Telecommunication services	1.1	0.1	0.1	–	0.2	1.5	6.7
<b>FINANCIALS</b>	<b>0.1</b>	<b>0.2</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>0.3</b>	<b>0.1</b>
Speciality and other finance	0.1	–	–	–	–	0.1	0.1
Investment companies	–	0.2	–	–	–	0.2	–
<b>INFORMATION TECHNOLOGY</b>	<b>26.0</b>	<b>3.4</b>	<b>9.9</b>	<b>–</b>	<b>0.7</b>	<b>40.0</b>	<b>42.8</b>
Information technology hardware	7.0	0.6	4.5	–	0.5	12.6	9.3
Software and computer services	19.0	2.8	5.4	–	0.2	27.4	33.5
<b>TOTAL EQUITIES</b> (including convertible and preference stock)	<b>55.7</b>	<b>7.2</b>	<b>16.6</b>	<b>0.6</b>	<b>4.5</b>	<b>84.6</b>	
Total equities – 1999 (including convertible and preference stock)	62.9	6.8	16.1	0.3	6.7		92.8
<b>BONDS/GILTS</b>	<b>12.0</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>12.0</b>	<b>0.9</b>
<b>NET LIQUID ASSETS</b>	<b>3.0</b>	<b>–</b>	<b>0.1</b>	<b>–</b>	<b>0.3</b>	<b>3.4</b>	<b>6.3</b>
<b>TOTAL ASSETS</b> (before deduction of bank loan)	<b>70.7</b>	<b>7.2</b>	<b>16.7</b>	<b>0.6</b>	<b>4.8</b>	<b>100.0</b>	
Total assets – 1999	70.1	6.8	16.1	0.3	6.7		100.0
<b>BANK LOAN</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>(0.9)</b>	<b>(0.9)</b>	<b>(0.8)</b>
<b>EQUITY SHAREHOLDERS' FUNDS</b>	<b>70.7</b>	<b>7.2</b>	<b>16.7</b>	<b>0.6</b>	<b>3.9</b>	<b>99.1</b>	
Equity shareholders' fund – 1999	70.1	6.8	16.1	0.3	5.9		99.2
Number of equity investments (including convertible and preference stock)	105	21	95	4	24	249	199

## GEOGRAPHICAL SPREAD OF INVESTMENTS



## DETAILED LIST OF INVESTMENTS

AT 31 DECEMBER 2000

Classification	Name	Market value £'000	%
<b>UNITED KINGDOM</b>			
Electronic and electrical equipment	Alba	7,747	
	Amstrad	3,162	
	Druck Holdings	558	
	Intelek	675	
	Linx Printing Technologies	5,369	
		17,511	4.6
Healthcare and pharmaceuticals Distributors	Biotrace International	744	0.2
	Abacus Polar	1,382	
	Acal	7,113	
	Action Computer Supplies	1,302	
	Deltron Electronics	1,186	
	Diploma	2,779	
	†Netcentric Systems Northamber	1,550 3,025	
		18,337	4.8
Leisure, entertainment and hotels	†Cyberes	1,000	
	††World Travel Holdings	345	
		1,345	0.3
Media and photography	365 Corporation	839	
	†Alibi Communications	272	
	†Ambient	3,042	
	Applied Optical Technologies	2,354	
	†BV Group	440	
	Bloomsbury Publishing	3,380	
	†C & B Publishing	89	
	†Channel Health	1,413	
	†Clipserv.com	642	
	Cordiant Communications	1,385	
	GWR Group	4,781	
	Informa Group	6,000	
	Jazz FM	3,143	
	Johnston Press	1,017	
	Maiden Group	1,425	
	†Motionposter	730	
	Music Choice Europe	528	
	†Online Classics	925	
	Osprey Communications Group	21	
	§Quarto Group	968	
	Scottish Radio Holdings	7,061	
	Sterling Publishing Group	1,541	
	†Stratus Holdings	310	
	†Synigence	610	
	Taylor & Francis Group	486	
	Taylor Nelson Sofres	2,854	
	Teamtalk.com	2,514	
Tempus Group	5,802		
†VFG	1,152		
†West 175 Media Group Wilmington Group	249 2,946		
		58,919	15.6
Support services	BNB Resources	872	
	Harvey Nash Group	3,296	
	†Ingenta	940	
	Lorien	1,033	
	††Mondas 8% CULS	632	
	PSD Group	1,491	
	Spring Group	1,195	
	†Systems International Group †Thomson Intermedia	1,275 738	
		11,472	3.0
Telecommunication services	Atlantic Telecom Group	261	
	IMS Group	1,016	
	PNC Tele.com	917	
	Project Telecom	1,980	
		4,174	1.1
Speciality and other finance	†Adaptive Venture Managers	82	
	*HIML Jersey Ltd	-	
	*Herald Investment Management Ltd	252	
		334	0.1
Information technology hardware	ARM Holdings	5,313	
	IQE (EASDAQ)	693	
	Plasmon	1,271	
	Telemetrix	13,531	
	Telspec	479	
	*Ubinetics Holdings	4,000	
	Vislink Zen Research	1,024 31	
		26,342	7.0



## DETAILED LIST OF INVESTMENTS *continued*

AT 31 DECEMBER 2000

Classification	Name	Market value £'000	%
Software and computer services	Affinity Internet Holdings	683	
	AIT Group	2,765	
	Alphameric	6,659	
	Anite Group	8,863	
	Azlan Group	7,762	
	Bright Station	835	
	†Bsoftb	806	
	†Clarity Commerce Solutions	1,084	
	Electronic Data Processing	1,229	
	†Eurotelecom Communications	32	
	Expocentric	956	
	†Harrier Group	189	
	†i-DocumentSystems Group	1,458	
	†IMS Maxims	381	
	†Intechnology	1,339	
	†Iq-Ludorum	633	
	Keystone Solutions Group	424	
	Lynx Group	3,076	
	•Manpower Software	132	
	†Minorplanet Systems	2,200	
	MMT Computing	1,503	
	Morse Holdings	1,133	
	Netbenefit	385	
	†Netcall	1,532	
	Northgate Information Solutions	894	
	NSB Retail Systems	1,508	
	†OneClickHR	1,162	
	Orbital Software Holdings	706	
	Patsystems	3,090	
	Rolfe & Nolan	3,517	
	Sherwood International	4,286	
	‡Statpro Group	1,078	
	Superscape	4,034	
Surfcontrol (EASDAQ)	4,449		
Vocalis Group	1,011		
		71,794	19.0
	TOTAL UNITED KINGDOM EQUITIES	210,972	55.7
<b>CONTINENTAL EUROPE</b>			
Electronic and electrical equipment	‡Draka Holdings	1,811	
	Egide	1,124	
	Logitech	2,778	
		5,713	1.5
Media and photography	N.R.J. Groupe	4,745	
	Publigroupe	2,255	
	United Internet NMBC	493	
		7,493	2.0
Telecommunication services	Enitel	277	0.1
Investment companies	•Sadot R & D	926	0.2
Information technology hardware	Nera	2,280	
	Teles NMBC	111	
		2,391	0.6
Software and computer services	Algol Spa (EASDAQ)	974	
	*Atex Media	-	
	Esker	236	
	Hands	383	
	Horizon Technology	1,982	
	IB Groupe Com	867	
	Merkantidata	875	
	Profdoc	917	
	Plaut NM	1,838	
	Reply	1,456	
	Smartforce	1,006	
		10,534	2.8
	TOTAL EUROPEAN EQUITIES	27,334	7.2
<b>AMERICAS</b>			
Aerospace and defence	Titan	309	0.1
Electronic and electrical equipment	ACT Manufacturing	478	
	Artesyn Technologies	106	
	ESS Tech. INC. Com	515	
	M-Systems Flash Disk Pioneer	1,679	
	PSI Technologies Holdings	176	
	Radisys	996	
	Remec	668	
	‡Reptron	139	
	Rockford	335	



## DETAILED LIST OF INVESTMENTS *continued*

AT 31 DECEMBER 2000

Classification	Name	Market value £'000	%
Electronic and electrical equipment ( <i>continued</i> )	Silicon Image	182	
	Sipex	1,602	
	Texas Instruments	1,586	
	Three-Five Systems	241	
	Xicor	362	
	Zoran	311	
		9,376	2.5
Healthcare and pharmaceuticals	Sonosite	427	0.1
Distributors	Bell Microproducts	2,032	
	Black Box Del.	1,358	
	Jaco Electronics	439	
	Kent Electronics	773	
	NU Horizons Electronics	90	
	Pioneer Standard Electronics	442	
		5,134	1.4
Leisure, entertainment and hotels	Pegasus Solutions	279	0.1
Media and photography	Cinar Films B	201	
	Cinar B subvoting	14	
	Lions Gate Entertainment	423	
	Mediacom Comms 'A'	345	
	Medialink Worldwide	220	
	Modem MDA. Poppe Tyson 'A'	177	
	Multivision Communications	23	
	Penton Media	540	
	Scholastic	1,483	
Support services	Computer Horizons	209	
	First Consulting Group	413	
	GP Strategies	274	
	Infospace	349	
	Internet.com	239	
	Management Network Group	397	
	OneSource Information	3,051	
	Optio Software	220	
	Pomeroy Computer Resources	306	
	Technology Solutions	142	
	Webex Communications	140	
		5,740	1.5
Telecommunication services	Lexent	458	
	USN Communications	1	
		459	0.1
Information technology hardware	Adaptive Broadband	328	
	Advanced Energy Industries	1,205	
	Airmet Communications	316	
	APW	791	
	Asyst Technology Corp.	1,979	
	Breezecom	192	
	Brooks Automation	376	
	Computer Network Technology	1,061	
	Copper Mountain Networks	818	
	Credence Systems Corp.	2,310	
	DMC Stratex Networks	1,205	
	Exabyte	288	
	Lecroy Corp. Com	692	
	Micros Systems	550	
	Microvision Wash	117	
	MRV Communications	1,791	
	Nova Measuring Instruments	749	
	Pinnacle Holdings	364	
	Precision OP. Mass	132	
	Rainbow Technologies	1,059	
Rimage	173		
Signal Technologies	268		
Xircom	332		
		17,096	4.5
Software and computer services	Advanced Digital Information	1,694	
	Advent Software	2,414	
	Brightstar Information Technology Group	58	
	Carreker-Antinori	1,919	
	Centra Software	648	
	Datastream Systems	261	
	Digital River	8	
	Diversinet	30	
	Engage Technologies	25	
	Epiq. Systems	917	
	Extended Systems	469	
	F5 Networks	64	
	Intrusion Com	95	
Keynote Systems	475		

## DETAILED LIST OF INVESTMENTS *continued*

AT 31 DECEMBER 2000

Classification	Name	Market value £'000	%
Software and computer services ( <i>continued</i> )	Macrovision	2,973	
	MSC Software	263	
	Multex	443	
	NET Genesis	218	
	Netscout Systems	669	
	Optibase	89	
	Phoenix International	38	
	Portal Software	262	
	Retalix Ord.	964	
	RSA Security	5,132	
	Select Software Tools	2	
	Sequoia Software	153	
Walker Interactive Systems	180		
		20,463	5.4
	TOTAL AMERICAN EQUITIES	62,709	16.6
<b>JAPAN</b>			
Electronic and electrical equipment	Hitachi AIC	694	
	New Japan Radio	287	
	Yamaichi Electronics	536	
	Yokowo	863	
		2,380	0.6
	TOTAL JAPANESE EQUITIES	2,380	0.6
<b>ASIA PACIFIC</b>			
Electronic and electrical equipment	Ambit Microsystems	863	
	Chroma Ate	353	
	Huneeed Technologies	489	
	Korea Electronic	293	
	Natsteel Broadway (SES)	1,220	
	Omni Industries	1,870	
	Universal Scientific Industrial	178	
		5,266	1.4
Retailers	Wine Planet Holdings	335	0.1
Media and photography	LG ad	529	
	Oriental Press Group	704	
	Shaw Brothers	519	
	Sing Tao Holding	1,234	
	South China Morning Post	2,489	
	¶Star Publications	2,630	
	8,105	2.1	
Telecommunication services	Telemedia Networks International	454	
	T S Telecom	185	
	639	0.2	
Information technology hardware	JC Hyun System	96	
	NERA Telecommunications	584	
	V-Tech Holdings	423	
	Wyse Technology Taiwan	706	
	1,809	0.5	
Software and computer services	Catuity Inc	437	
	E-Net	54	
	Quiktrak	156	
	Surfboard	48	
	695	0.2	
	TOTAL ASIA PACIFIC EQUITIES	16,849	4.5
	Value of equity stocks	317,668	
	Convertible preference stocks having an element of equity	417	
	Convertible loan stocks having an element of equity	2,112	
	Warrants having an element of equity	47	
	TOTAL EQUITY INVESTMENTS	320,244	84.6
FIXED INTEREST	UK Treasury 2½ % IL 2001	4,288	
	UK Treasury 7% 2001	41,043	
	TOTAL FIXED INTEREST	45,331	12.0
NET LIQUID ASSETS		13,032	3.4
TOTAL ASSETS AT MARKET VALUE (before deduction of bank loan)		378,607	100.0

(† denotes holding listed on AIM)  
 (\* denotes unquoted security)  
 (‡ denotes holding wholly or partly in convertible loan stock)  
 (§ denotes holding wholly or partly in preference loan stock)  
 (¶ denotes holding wholly or partly in warrants)

## LONG TERM RECORD

CAPITAL								
At 31 December	Total assets £'000	Bank loans £'000	Equity shareholders' funds £'000	Net asset value per share p	Diluted net asset value per share† p	Share price p	Warrant price p	(Discount)/ premium‡ %
□ Inception	64,170	–	64,170	98.72	98.72	90.90#	45.50	(7.9)
1994	60,823	–	60,823	93.57	93.57	91.00	38.00	(2.7)
*1995	89,689	–	89,689	137.98	132.36§	127.00	55.00	(4.0)
1996	130,055	–	130,055	156.89	150.88§	136.00	61.00	(9.9)
1997	147,424	–	147,424	177.84	171.80	136.00	60.50	(20.8)
1998	170,982	–	170,982	206.25	201.70	161.50	77.50	(19.9)
1999	432,620	(3,343)	429,277	517.44	494.22	511.00	411.00	3.4
<b>2000</b>	<b>378,607</b>	<b>(3,233)</b>	<b>375,374</b>	<b>447.55</b>	<b>431.43</b>	<b>491.00</b>	<b>382.50</b>	<b>13.8</b>

\* Restated for change in accounting policy to account for income on an xd basis.

† The diluted net asset value per ordinary share figures have been calculated in accordance with FRS14 (see note 17, page 33).

‡ (Discount)/premium is the difference between Herald's quoted share price and its underlying diluted net asset value (FRS14).

§ The diluted net asset values at 31 December 1995 and 1996 have been restated with the adoption of FRS14. The previously reported fully diluted net asset values were 131.65p and 149.45p respectively.

□ Inception date 16 February 1994, 100p was shareholders' subscription price before launch costs of 1.3p.

# 90.9p is the capital gains tax (CGT) base subscription price for shareholders adjusting for warrants which were issued on a 1 for 5 basis. The CGT base for the warrant is 45.5p.

REVENUE						GEARING RATIOS	
Period to 31 December	Gross revenue £'000	Available for ordinary shareholders £'000	Earnings per ordinary share net** p	Dividend ordinary share net p	Expense ratio†† %	Actual gearing‡‡	Potential gearing§§
1994	1,286	439	0.68	0.50	0.82	85	100
*1995	1,968	780	1.20	0.65	1.32	92	100
1996	2,897	1,035	1.32	0.81	1.46	89	100
1997	3,185	1,118	1.35	0.85	1.29	92	100
1998	3,845	1,134	1.37	0.90	1.36	94	100
1999	3,658¶	717	0.86	0.85	0.95	93	101
<b>2000</b>	<b>6,508</b>	<b>778</b>	<b>0.93</b>	<b>0.85</b>	<b>1.40</b>	<b>86</b>	<b>101</b>

\* Restated for change in accounting policy to account for income on an xd basis.

\*\* The calculation of earnings per ordinary share is based on the revenue from ordinary activities after taxation and the weighted average number of ordinary shares in issue (see note 8, page 29).

†† Ratio of total operating costs against average shareholders' funds.

‡‡ Total assets (including all debt used for investment purposes) less all cash and fixed interest securities (excluding convertibles) divided by shareholders' funds.

§§ Total assets (including all debt used for investment purposes) divided by shareholders' funds.

¶ Restated for the adoption of FRS16 "Current Tax" (see note 1, page 27).

CUMULATIVE PERFORMANCE								
At 31 December	Diluted net asset value per share†	Share price	Benchmark	Hoare Govett Smaller Cos Index	Russell 2000 Technology Index	Earnings per ordinary share	Dividend per ordinary share net	Retail price index
Inception	100	100	100	100	–	–	–	–
1994	95	100	84	83	100¶¶	100	100	100
1995	134	140	95	93	129	176	130	103
1996	153	150	108	107	132	194	162	106
1997	174	150	125	113	139	199	170	110
1998	204	178	123	104	154	201	180	113
1999	501	562	211	158	326	126	170	115
<b>2000</b>	<b>437</b>	<b>540</b>	<b>185</b>	<b>154</b>	<b>209</b>	<b>137</b>	<b>170</b>	<b>118</b>

all figures have been rebased to 100.

#### Compound Annual Returns

5 year	26.7%	31.1%	14.3%	10.6%	10.2%	(5.0%)	5.5%	2.7%
From inception	23.5%	27.2%	9.2%	6.4%	13.1%	5.4%	9.2%	2.8%

¶¶ Index at 31 May 1995.

# DIRECTORS' REPORT

The Directors present their report and accounts for the year ended 31 December 2000.

## Business Activity

The Company carries on business as an investment trust. It was approved by the Inland Revenue as an investment trust under Section 842 of the Income and Corporation Taxes Act 1988 for the year ended 31 December 1998. In the opinion of the Directors the Company has subsequently conducted its affairs so as to enable it to continue to obtain such approval.

The Company will continue to seek approval under Section 842 of the Income and Corporation Taxes Act 1988 each year. However, under Corporation Tax Self Assessment, which applies to accounting periods ended after 30 June 1999, the Inland Revenue will no longer be obliged to give written approval. Instead the Inland Revenue have twelve months after the return filing date in which to give notice that they intend to enquire into the return but, if no such notice is given then approval may be assumed to have been obtained.

The Company is an investment company within the meaning of Section 266 of the Companies Act 1985.

The Ordinary shares of the Company are qualifying investments for personal equity plans and individual savings accounts and it is the Directors' intention that the Company will conduct its affairs so as to continue to be a qualifying trust.

## Investment Policy and Objectives

The objective of the Company's management is to secure an attractive level of overall return for its shareholders primarily from capital growth but also from income over the life of the Company. The Company spreads its risks across a diversified portfolio of quoted securities in smaller companies which specialise in products, services or applications in the communications and multimedia sectors. The Company has certain specific investment guidelines, including that investee companies will have an equity market capitalisation of up to approximately £750 million at the time of initial investment. Securities acquired by the Company will normally be quoted on the Official List (which includes the Alternative Investment Market) of the London Stock Exchange or equivalent markets overseas.

The Directors consider it desirable that shareholders be given the opportunity to consider the future of the Company at regular intervals. Accordingly, an ordinary resolution will be proposed at the Annual General Meeting of the Company in 2004 (and at every third subsequent Annual General Meeting) to the effect that the Company should continue as an investment trust. If such resolution is not passed, the Directors will prepare and submit to shareholders (for approval by special resolution) proposals for the unitisation or other reconstruction of the Company. If these proposals are not approved the Company will be wound up.

The Articles of Association of the Company permit it to borrow up to one-fifth of its total capital and reserves. At 31 December 2000 borrowings of yen 551,550,000 (£3.2 million market value) had been made.

The Company's policy is to adopt a long-term approach to investment.

## Results and Dividend

The net revenue after tax for the period was £778,000 (1999 – £717,000).

The Directors recommend a dividend of 0.85p per Ordinary share for the year ended 31 December 2000, which, if approved by the Annual General Meeting, will be payable on 20 April 2001 to holders registered on 23 March 2001. The payment will amount to £713,000 and the transfer to reserves will therefore be £65,000.

The net asset value (NAV) of the Company at 31 December 2000 represented a value of 447.55p per Ordinary share (diluted (FRS14) 431.43p). This represented a fall of 13.5% during the year (diluted (FRS14) 12.7%) and a rise of 353.4% (diluted (FRS14) 337.1%) since the date of committal of funds (16 February 1994) after allowing for launch expenses of 1.3p per share.

## Investment Report and Outlook

The Chairman's Statement incorporates a review of the highlights of the year to 31 December 2000.

## The Board

Other than as declared in the following paragraph and in the section headed "Management and Administration" below, your Board has complete independence from the investment manager, all its members being non-executive. All have been Directors for the whole period under review.

## DIRECTORS' REPORT *continued*

### The Board *continued*

Other than in respect of Mr Boase's shareholding of 7.2% of the Ordinary share capital of the investment management company, there were no contracts subsisting during or at the end of the year in which a Director was or is materially interested.

The Director's holdings in the Company's shares, all of which are beneficially owned, were as follows:

Name	Number of Ordinary Shares		Number of Warrants	
	2000	1999	2000	1999
Martin Boase	50,000	50,000	–	60,000
Timothy Abell	11,158	11,158	2,000	2,000
Justin Dukes	1,158	1,158	–	–
Colin McCarthy	8,112	8,112	1,000	1,000
Clive Parritt	5,637	5,637	1,000	1,000

Mr M Boase retires by rotation and, being eligible, is recommended by the Board for re-election.

Mr T Abell retires having reached the age of 70. He is recommended by the Board for reappointment.

There have been no changes intimated in the Directors' interests up to 26 February 2001.

### Management and Administration

For the entire year under review the management of the Company was contracted to Herald Investment Management Limited ("HIML"). HIML is regulated by IMRO.

The senior director of HIML with prime responsibility for the management of Herald Investment Trust is Katie Potts, who is also a substantial shareholder of HIML. HIML was employed initially under a three-year contract. This period has now expired and the contract is subject to 12 months' notice. HIML is remunerated at a monthly rate of 0.0833% of the Company's net asset value.

At 31 December 2000 the Company was the beneficial owner of 14% of the Ordinary share capital of HIML.

Administration of the Company and its investments is contracted by HIML to Baillie Gifford & Co., who took over the appointment from Colonial First State Investments (formerly Stewart Ivory) on 1 September 2000. Baillie Gifford & Co. also act as company secretary.

Custody of investments is contracted to The Bank of New York Europe Limited.

### Significant Shareholdings

At 26 February 2001 the Directors have been notified of the following shareholdings comprising 3% or more of the issued share capital of the Company:

Name	Ordinary Shares	% of issue
Newton Investment Management Limited	9,283,467	11.1
Henderson Investors Limited	5,895,576	7.0
Windsor Life Assurance	2,700,000	3.2

### Payment of Suppliers

It is the Company's payment policy to obtain the best possible terms for all business. The Company negotiates with its suppliers the terms on which business will take place and abides by such terms.

The Company did not have any trade creditors at 31 December 2000.

### Auditors

Ernst & Young have expressed their willingness to continue in office as auditors, and a resolution to reappoint them will be proposed at the Annual General Meeting.

## DIRECTORS' REPORT *continued*

### Annual General Meeting

The Annual General Meeting of the Company will be held on 18 April 2001. The following resolution will be proposed as special business.

### Authority to Repurchase the Company's Ordinary Shares

At the Company's Annual General Meeting held on 19 April 2000 it was resolved that the Company be authorised to purchase in the market up to 12,435,956 Ordinary shares (14.99% of its Ordinary share capital in issue at that time). Between the date of that Annual General Meeting and the date of this notice no Ordinary shares have in fact been bought back by the Company. The Board continues to believe, however, that the ability of the Company to purchase its own Ordinary shares in the market will potentially benefit all shareholders of the Company. The repurchase of Ordinary shares at a discount to the underlying net asset value ("NAV") should enhance the NAV per Ordinary share of the remaining shares and may also enable the Company to address more effectively any imbalance between supply and demand for the Company's Ordinary shares.

Accordingly, the Directors are now recommending in Resolution 7 that this authority to purchase the Company's own Ordinary shares should be renewed and should now expire at the Company's Annual General Meeting to be held in 2002. Authority will be sought to purchase up to 14.99% of the Company's Ordinary shares in issue at the date of the passing of the resolution (the maximum permitted under the Listing Rules of the London Stock Exchange) at a price that is not less than 25p per share (the nominal value of each share) and not more than 5% above the average middle-market quotation for the five business days preceding the day of purchase. The authority being sought, the full text of which can be found in Resolution 7 in the Notice of Meeting, will last until the date of the Annual General Meeting in 2002. The decision as to whether the Company repurchases any shares will be at the absolute discretion of the Board and will only be considered when it is in the interests of the Company and its shareholders as a whole. It is the intention that purchases will only be made at a discount to net asset value.

The Directors consider that the implementation of the facility to repurchase the Company's own Ordinary shares is in the interests of shareholders as a whole and unanimously recommend all holders to vote in favour by completing and returning the enclosed form of proxy. The proxy form should be returned to the Company's Registrar as soon as possible but in any event so as to arrive no later than 48 hours before the time of the Annual General Meeting.

By order of the Board

*Baillie Gifford & Co.*  
Secretaries

27 February 2001

## STATEMENT OF DIRECTORS' RESPONSIBILITIES

Company law requires the Directors to prepare accounts for each financial year which give a true and fair view of the state of affairs of the Company as at the end of the year and of the surplus or deficit for the year. In preparing the accounts, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates which are reasonable and prudent; and
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts.

The Directors are responsible for ensuring that proper accounting records are kept which disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the accounts comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

On behalf of the Board

*Martin Boase*  
Chairman

27 February 2001

# CORPORATE GOVERNANCE

## Code of Best Practice

The Directors have considered the principles set out in the Combined Code on Corporate Governance and, following guidance issued by the London Stock Exchange in September 1999, can confirm that the Company has, except where otherwise stated, complied with all material aspects of the Combined Code throughout the year.

## The Principles of Good Governance

### The Board

The Board's regular meetings take place every three months. There is no formal schedule of matters reserved for Board approval. Such a schedule would be inappropriate since the Board decides on all aspects of the activities of the Company including investment policy, borrowings, treasury matters and dividend policy. The Board also reviews the financial statements, investment transactions, revenue budgets and performance.

The Board is comprised entirely of non-executive Directors who, except as disclosed in the Directors' Report, are independent of the managers. The executive responsibilities for investment management and administration have been delegated to Herald Investment Management Limited and Baillie Gifford & Co respectively, and in the context of a Board comprised entirely of non-executive Directors, there is no chief executive officer. Martin Boase was appointed Chairman at inception, as the Board is small there is no recognised senior independent member. The Directors all have appropriate business and financial experience with which to conduct the business of the Board. Information on the Board members can be found on page 4.

Given the non-executive nature of the Board a separate nomination committee has not been established. It is the view of the Board that the appointment of new Directors should be a matter for consideration by the Board as a whole. Under the provisions of the Company's Articles, a Director appointed during the year is required to retire and seek election by shareholders at the next Annual General Meeting. The Articles also require that the Directors retire by rotation and submit themselves for re-election at least once every three years.

There is an agreed procedure for Directors to seek independent professional advice if necessary and at the Company's expense.

### Remuneration

Since all directors are non-executive, the Company is not required to comply with the principles of the Combined Code in respect of executive Directors' remuneration. There is no separate remuneration committee and the Board as a whole considers changes to Directors' fees from time to time. It is the Company's policy that remuneration of Directors should be set at a reasonable level that is commensurate with the duties and responsibilities of the role and consistent with the requirement to attract and retain Directors of the appropriate quality and experience.

No Director has a contract of service and there is no notice period. Directors' fees are detailed on page 29; no other benefits are provided.

### Internal Control and Risk Management

The practical measures to ensure compliance with regulation and company law, and to provide effective and efficient operations and investment management have been delegated to Herald Investment Management Limited and Baillie Gifford & Co, as detailed in the Directors' Report. The Board acknowledges its responsibilities to supervise and control the discharge by the managers and secretaries of their obligations.

The managers are responsible for the design, implementation and maintenance of control policies and procedures to safeguard the assets of the Company and to manage its affairs properly. This responsibility also extends to maintaining effective operational and compliance controls and risk management.

The Company's investments are segregated from the investment and administration functions through the appointment of The Bank of New York Europe Limited as independent custodian of the Company's investments.

The managers have a compliance function in accordance with IMRO regulations. The Board receives a report on monitoring procedures at least annually. In addition, Baillie Gifford & Co conducts an annual review of its internal controls which is documented within an internal controls report. This report is independently reviewed by its auditors. A copy of the internal controls report is submitted to the Board. Baillie Gifford's head of internal audit and compliance provides the Board with regular reports on its monitoring programs as they relate to its secretarial and administrative function.

The Directors acknowledge their responsibility for the Company's system of internal controls and for reviewing its effectiveness. The system of internal controls is designed to manage rather than eliminate risk and can only provide reasonable but not absolute assurance against material misstatement or loss. The Directors confirm that they have reviewed the effectiveness of the system and it is their intention to review its effectiveness on a regular basis.



## CORPORATE GOVERNANCE *continued*

The Board has undertaken a full review of all aspects of the published guidance “Internal Control: Guidance for Directors on the Combined Code” (the Turnbull guidance) and believes that as of July 2000 its approach to internal controls review accords with the Turnbull recommendations. The Board confirms that, by formalising its review of the effectiveness of internal controls, it has established the procedures necessary to implement the Turnbull guidance. To ensure that risk management and internal control are considered on a regular basis and that a full risk and control assessment is undertaken on an annual basis, the following processes have been established in compliance with the guidance:

- Internal control strategy has been formalised with the production of a detailed risk map whereby significant risks are identified and the key controls to manage those risks are confirmed as in place and operating effectively.
- Baillie Gifford’s reporting procedures for the internal audit and compliance department with regard to its risk framework and regulatory monitoring programs have been defined and formalised within a service level agreement.
- Regular reports on internal control are prepared by the managers and submitted for Board review.

These procedures ensure that consideration is given regularly to the nature and extent of risks facing the Company and that they are being actively monitored. Where changes in risk have been identified during the year, they also provide a mechanism to assess whether further action is required to manage the risks identified. The Board confirms that these procedures have been in place since July 2000, are operating effectively and continue to be in place up to the date of approval of this Report.

### **Accountability and Audit**

The respective responsibilities of the Directors and the auditors in connection with the Financial Statements are included on pages 20 and 23.

The accounts have been prepared on the going concern basis, as it is the Directors’ opinion that the Company will continue in operational existence for the foreseeable future.

An Audit Committee has been established in compliance with the Combined Code consisting of all Directors. The Audit Committee’s authority and duties are defined within its formal terms of reference. The Chairman of the Board has been appointed Chairman of the Audit Committee.

An investment management agreement between the Company and Herald Investment Management Limited sets out the matters over which the managers have been delegated authority by the Board. The management agreement is terminable on not less than 12 months’ notice and the Audit Committee reviews the terms of the management agreement.

The Board, currently comprising exclusively non-executive directors, meets periodically as an audit committee to review the Company’s interim and annual financial statements. The Board approves the level of fees for audit and non-audit services and considers the relationship with the Company’s auditors.

### **Relations with Shareholders**

The Company’s managers meet regularly with institutional shareholders and report to the Board. The Company’s Annual General Meeting is used as an opportunity to communicate with private shareholders and the Board announces the level of proxies lodged. The notice period for the Annual General Meeting is twenty working days. The Company has given discretionary voting powers to the investment managers, HIML. The managers vote against resolutions they consider may damage shareholders rights or economic interests. HIML give consideration to socially responsible investments when making investment decisions as they believe this to be in the best interest of the Company in the long term, but their overriding consideration is to produce good investment returns for shareholders.

### **Compliance**

The Board considers that throughout the year the Company has been in compliance with the Code Provisions set out in Section 1 of the Combined Code on Corporate Governance issued by the UK Listing Authority of the Financial Services Authority. The areas of variation are that there is no formal schedule of matters reserved for the Board and there is no recognised senior independent member of the Board, the absence of which have been explained above. As previously stated, internal control procedures have been in place since July 2000 which accord with the guidance for directors on compliance with the Combined Code.

On behalf of the Board

*Martin Boase*  
Chairman

27 February 2001



# AUDITORS' REPORT

## TO THE SHAREHOLDERS OF HERALD INVESTMENT TRUST PLC

We have audited the accounts on pages 24 to 34, which have been prepared under the historical cost convention modified to include the revaluation of fixed asset investments and the accounting policies set out on page 27.

### **Respective Responsibilities of Directors and Auditors**

The Directors are responsible for preparing the annual report. As described on page 20, this includes responsibility for preparing the accounts in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, the Listing Rules of the Financial Services Authority and by our profession's ethical guidance.

We report to you our opinion as to whether the accounts give a true and fair view and are properly prepared in accordance with the Companies Act. We also report to you if, in our opinion, the Directors' Report is not consistent with the accounts, if 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 the information specified by law or the Listing Rules regarding Directors' remuneration and transactions with the Company is not disclosed.

We review whether the corporate governance statement on pages 21 and 22 reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risk and controls, or form an opinion on the effectiveness of either the Company's corporate governance procedures or its risk and control procedures.

We read the other information contained in the annual report, including the corporate governance statement, and consider whether it is consistent with the audited accounts. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts.

### **Basis of Audit Opinion**

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the accounts, 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 provide us with sufficient evidence to give reasonable assurance that the accounts 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 accounts.

### **Opinion**

In our opinion the accounts give a true and fair view of the state of affairs of the Company as at 31 December 2000 and of its net revenue for the year ended and have been properly prepared in accordance with the Companies Act 1985.

ERNST & YOUNG  
*Registered Auditor*  
Edinburgh

27 February 2001

## STATEMENT OF TOTAL RETURN

(incorporating the revenue account)

FOR THE YEAR ENDED 31 DECEMBER 2000

	Notes	2000			1999		
		Revenue £'000	Capital £'000	Total £'000	Revenue (restated) £'000	Capital £'000	Total (restated) £'000
(Losses)/gains on investments	9	–	(55,069)	(55,069)	–	258,619	258,619
Unrealised gain/(loss) on loan		–	110	110	–	(343)	(343)
Currency gains/(losses)		–	79	79	–	(53)	(53)
Income	2	6,508	–	6,508	3,658	–	3,658
Investment management fee	3	(5,230)	–	(5,230)	(2,580)	–	(2,580)
Other administrative expenses	4	(390)	–	(390)	(276)	–	(276)
<b>Net return before finance costs and taxation</b>		888	(54,880)	(53,992)	802	258,223	259,025
Finance costs of borrowings	5	(84)	–	(84)	(74)	–	(74)
<b>Return on ordinary activities before taxation</b>		804	(54,880)	(54,076)	728	258,223	258,951
Tax on ordinary activities	6	(26)	–	(26)	(11)	–	(11)
<b>Return on ordinary activities after taxation</b>		778	(54,880)	(54,102)	717	258,223	258,940
Ordinary dividend payable	7	(713)	–	(713)	(705)	–	(705)
<b>Transfer to/(from) reserves</b>		65	(54,880)	(54,815)	12	258,223	258,235
<b>Return per Ordinary share</b>							
Basic	8	0.93p	(65.67p)	(64.74p)	0.86p	311.33p	312.19p
Diluted		0.89p	(63.03p)	(62.14p)	0.83p	300.53p	301.36p
Dividend per Ordinary share		0.85p	–	0.85p	0.85p	–	0.85p

The revenue column of this statement is the revenue account of the Company.

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

The accompanying notes on pages 27 to 34 are an integral part of this statement.

# BALANCE SHEET

AT 31 DECEMBER 2000

	Notes	2000		1999	
		£'000	£'000	£'000	£'000
<b>Fixed assets</b>					
Investments	9		365,575		405,301
<b>Current assets</b>					
Debtors	11	2,309		1,123	
Short term investments		4,000		–	
Cash at bank and in hand		8,230		27,531	
		14,539		28,654	
<b>Creditors: amounts falling due within one year</b>	12	(1,507)		(1,335)	
Net current assets			13,032		27,319
			378,607		432,620
<b>Creditors: amounts falling due after one year</b>					
Overseas currency loan	13		(3,233)		(3,343)
<b>TOTAL NET ASSETS</b>			375,374		429,277
<b>Capital and reserves</b>					
Called-up share capital	14		20,968		20,740
Share premium	15		68,999		67,900
Warrant reserve	15		1,789		2,204
Capital reserve – realised	15		217,867		91,061
Capital reserve – unrealised	15		64,039		245,725
Revenue reserve	15		1,712		1,647
<b>EQUITY SHAREHOLDERS' FUNDS</b>	16		375,374		429,277
<b>NET ASSET VALUE PER ORDINARY SHARE</b>					
Basic	17		447.55p		517.44p
Diluted (FRS14)			431.43p		494.22p
Fully diluted			431.98p		494.40p

The accounts were approved by the Board of Directors and signed on their behalf on 27 February 2001.

*Martin Boase*  
Chairman

The accompanying notes on pages 27 to 34 are an integral part of this statement.

**CASH FLOW STATEMENT**  
FOR THE YEAR ENDED 31 DECEMBER 2000

	Notes	2000		1999	
		£'000	£'000	£'000	£'000
<b>Net cash inflow from operating activities</b>	18		348		1,013
<b>Servicing of Finance</b>					
Loan interest		(83)		(36)	
<b>Net cash outflow from servicing of finance</b>			(83)		(36)
<b>Taxation</b>					
Tax recovered		–		66	
<b>Total tax recovered</b>			–		66
<b>Financial investment</b>					
Purchase of investments		(212,244)		(69,001)	
Sale of investments		196,392		87,198	
Currency movement		79		(53)	
<b>Net cash (outflow)/inflow from financial investment</b>			(15,773)		18,144
<b>Equity dividend paid</b>			(705)		(746)
<b>New cash (outflow)/inflow before use of liquid resources and financing</b>			(16,213)		18,441
<b>Management of liquid resources†</b>					
Increase in term deposits			(4,000)		–
<b>Financing</b>					
Issue of Ordinary shares		912		60	
Currency loan		–		3,000	
<b>Net cash inflow from financing</b>			912		3,060
<b>(DECREASE)/INCREASE IN CASH</b>	19		(19,301)		21,501
<b>RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS</b>					
(Decrease)/increase in cash in period	19		(19,301)		21,501
Increase in short term investments			4,000		–
Increase in bank loan			–		(3,000)
Exchange movement			110		(343)
<b>MOVEMENT IN NET FUNDS IN PERIOD</b>			(15,191)		18,158
<b>NET FUNDS AT 1 JANUARY 2000</b>			24,188		6,030
<b>NET FUNDS AT 31 DECEMBER 2000</b>			8,997		24,188

† The Company includes as liquid resources term deposits of less than one year.

The accompanying notes on pages 27 to 34 are an integral part of this statement.

## NOTES TO THE ACCOUNTS

---

### 1. Accounting policies

The financial statements have been prepared in accordance with applicable accounting standards. The particular accounting policies adopted, which are unchanged from last year and have been applied consistently, except for the adoption of FRS16 “Current Tax” are set out below.

The change introduced by FRS16, accounting for UK dividend income net of tax, has been reflected in the 2000 financial statements with corresponding changes to the comparative figures. In the year to 31 December 2000 this reduces gross income and taxation equally by £209,000 (1999 – £244,000); the net effect has no impact upon the revenue return attributable to equity shareholders.

(a) Accounting convention

The accounts are prepared under the historical cost convention, as modified by the revaluation of investments. The accounts have been prepared in accordance with the Statement of Recommended Practice “Financial Statements of Investment Trust Companies”.

(b) Investments

Listed investments are valued at closing mid-market prices. Investments on the Alternative Investment Market are included at their quoted mid-market prices. Where material unlisted investments are valued by Directors on the basis of latest information in line with the relevant principles of the British Venture Capital Association Guidelines.

(c) Income from investments

Dividend income is accounted for when the entitlement to the income is established (normally on the ex-dividend date). Interest receivable is accounted for on an accruals basis.

(d) Capital reserves

The Company is precluded by its Articles from making any distribution of capital profits by way of dividend. Realised profits and losses on disposals of investments are dealt with in the realised capital reserve. Unrealised revaluation movements are dealt with through the unrealised capital reserve. Special dividends representing repayments of capital are dealt with through the unrealised capital reserve.

(e) Investment management fees

Investment management fees are charged wholly to revenue.

(f) Finance costs

Finance costs are accounted for on an accruals basis and are charged through the revenue account.

(g) Deferred taxation

Deferred tax is provided, using the liability method, on all material timing differences to the extent that it is probable that a liability will crystallise.

(h) Foreign currency

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and loans denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date. Exchange differences of a revenue nature are taken to the revenue account. Those of a capital nature are taken to capital reserve.

---

## NOTES TO THE ACCOUNTS *continued*

### 2. Income

	2000	1999
	£'000	£'000 (restated)
<b>Income from investments</b>		
Franked dividends from listed investments†	1,843	2,143
Franked dividends from unlisted investments†	35	35
Unfranked income from unlisted (AIM) UK convertible bonds	11	–
Overseas dividend income	495	660
Unfranked income from foreign convertible bonds	35	33
Gilt interest income	2,597	105
	5,016	2,976
<b>Other income</b>		
Deposit interest	1,446	660
Underwriting commission	46	22
	1,492	682
Total income	6,508	3,658
<b>Total income comprises:</b>		
Dividends	2,373	2,838
Interest from investments	2,643	138
Other	1,492	682
	6,508	3,658
<b>Income from investments</b>		
Listed UK	4,440	2,248
Listed overseas	530	693
Unlisted	46	35
	5,016	2,976

In the year to 31 December 1999 special dividends representing a repayment of capital and amounting to £73,000 were taken direct to Capital Reserves – Unrealised. (2000 – Nil) and a special dividend amounting to £184,000 was taken direct to Income (2000 – Nil).

†Restated to comply with FRS16 “Current Tax” (see note 1)

### 3. Investment management fee – *all charged to revenue*

	2000	1999
	£'000	£'000
Investment management fee	4,743	2,467
Irrecoverable VAT thereon	487	113
	5,230	2,580

Herald Investment Management Limited (“HIML”) are appointed investment managers under a management agreement which is terminable on twelve months notice. Their fee is calculated on a monthly rate of 0.0833% of the Company’s net asset value and is subject to VAT at the appropriate rate.

The Company registered for VAT during the year to 31 December 1999 and was able to recover VAT of £334,000 for that year and three previous years. This repayment was off-set against VAT incurred in the year to 31 December 1999.

## NOTES TO THE ACCOUNTS *continued*

### 4. Other administrative expenses – all charged to revenue

	2000	1999
	£'000	£'000
Custodian's fees	125	51
Registrars' fees	46	24
Directors' fees	53	53
Auditors' fees – audit work	9	9
– non-audit work	–	19
AITC its campaign	43	49
Miscellaneous expenses	114	71
	390	276

#### Directors' fees

The fees of the Chairman are £13,200 (1999 – £13,200) per year and those of the other Directors £9,900 each (1999 – £9,900 each) per year.

### 5. Finance costs of borrowings – all charged to revenue

	2000	1999
	£'000	£'000
Bank loan repayable within five years	84	74
	84	74

### 6. Taxation

	2000	1999
	£'000	£'000
Overseas taxation	26	11
	26	11

Restated to comply with FRS16 "Current Tax" (see note 1).

### 7. Ordinary dividend

	2000	1999	2000	1999
			£'000	£'000
Proposed dividend per ordinary share	0.85p	0.85p	713	705
	0.85p	0.85p	713	705

The proposed dividend will be paid on 20 April 2001 to all shareholders on the register as at the close of business on 23 March 2001.

### 8. Return per Ordinary share

	2000			1999		
	Revenue	Capital	Total	Revenue	Capital	Total
Basic	0.93p	(65.67p)	(64.74p)	0.86p	311.33p	312.19p
	0.93p	(65.67p)	(64.74p)	0.86p	311.33p	312.19p
Diluted	0.89p	(63.03p)	(62.14p)	0.83p	300.53p	301.36p
	0.89p	(63.03p)	(62.14p)	0.83p	300.53p	301.36p

Basic revenue return per Ordinary share is based on the net revenue on ordinary activities after taxation of £778,000 (1999 – £717,000) and on 83,571,294 Ordinary shares (1999 – 82,941,828) being the weighted average number of Ordinary shares in issue during the year.

Basic capital return per Ordinary share is based on the net capital loss for the financial year of £54,880,000 (1999 – gain £258,223,000) and on 83,571,294 Ordinary shares (1999 – 82,941,828) being the weighted average number of Ordinary shares in issue during the year.

The diluted returns per Ordinary share are calculated on the weighted average number of warrants in issue during the year adjusted by the difference between the average price of the Ordinary shares during the year and the Subscription price of 100p, giving a weighted average of 87,065,313 (1999 – 85,921,489) shares. The income return of 0.89p (1999 – 0.83p) and capital return of (63.03p) (1999 – 300.53p) are based on the same income and capital figures used in the basic return calculation.

## NOTES TO THE ACCOUNTS *continued*

### 9. Fixed assets – investments

	2000 £'000	1999 £'000
Listed at market valuation on the London Stock Exchange	224,799	256,086
Listed at market valuation on other recognised Stock Exchanges	109,272	127,862
AIM	27,252	21,101
Unquoted*	4,252	252
<b>Total fixed asset investments</b>	<b>365,575</b>	<b>405,301</b>

	Listed in UK £'000	Listed overseas £'000	AIM £'000	Unquoted £'000	Total £'000
Cost of investments at 1 January 2000	89,476	62,626	6,574	557	159,233
Unrealised appreciation/(depreciation) at 1 January 2000	166,610	65,236	14,527	(305)	246,068
<b>Value of investment at 1 January 2000</b>	<b>256,086</b>	<b>127,862</b>	<b>21,101</b>	<b>252</b>	<b>405,301</b>
Movements in the year:					
Purchases at cost	85,067	99,036	24,388	4,000	212,491
Sales – proceeds	(97,813)	(82,297)	(17,038)	–	(197,148)
– realised gains	76,834	35,860	14,033	–	126,727
Decrease in unrealised appreciation	(95,604)	(72,601)	(13,591)	–	(181,796)
Change in listing	1,024	617	(1,641)	–	–
Merger, non cash adjustment	(795)	795	–	–	–
<b>Value of investments held at 31 December 2000</b>	<b>224,799</b>	<b>109,272</b>	<b>27,252</b>	<b>4,252</b>	<b>365,575</b>
Cost of investments at 31 December 2000	153,793	116,637	26,316	4,557	301,303
Unrealised appreciation/(depreciation) at 31 December 2000	71,006	(7,365)	936	(305)	64,272
<b>Value of investments at 31 December 2000</b>	<b>224,799</b>	<b>109,272</b>	<b>27,252</b>	<b>4,252</b>	<b>365,575</b>

	2000 £'000	1999 £'000
<b>(Losses)/gains on investments</b>		
Realised gains on sales	126,727	40,278
(Decrease)/increase in unrealised appreciation	(181,796)	218,341
	<b>(55,069)</b>	<b>258,619</b>

\* The unquoted balance comprises Herald Investment Management Limited and HIML Jersey Ltd included at their cost of £251,561 (1999 – £251,561), Ubinetics at a cost of £4,000,000 and Atex Media (grey market value at 31 December 2000 of £259,000) at zero.

At 31 December 2000 the Company was the beneficial owner of 14% (1999 – 14%) of the Ordinary share capital of both HIML and HIML Jersey Ltd. HIML is incorporated in the United Kingdom whereas HIML Jersey Ltd is incorporated in Jersey.



## NOTES TO THE ACCOUNTS *continued*

### 10. Financial assets

A full list of the Company's investments is given on pages 13 to 16. In addition, a geographical analysis of the portfolio, an analysis of the investment portfolio by broad industrial or commercial sector and a review of the 20 largest equity investments by their aggregate market value, are contained in the investment review section on pages 10 to 12. All financial assets and liabilities are included in the accounts at market value (see note 1).

Exposure to currency risk through asset allocation is indicated on page 12. Included within the analysis provided on pages 13 to 16 is the Company's holding in warrants which confer the right to convert into equity shares. An analysis of the currency exposure and maturity profile of these warrants at 31 December is provided below:

	2000		1999	
	Market value £'000	Maturity date	Market value £'000	Maturity date
<b>Warrants:</b>				
Sterling	2	22/02/2002	–	–
	45	18/05/2001	–	–
Malaysian ringgit	–	21/08/2005	–	–
Israeli shekel	–	28/02/2001	–	–
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>

The interest rate risk profile of the Company's financial assets at 31 December was:

	2000			1999		
	Market value £'000	Interest rate	Maturity date	Market value £'000	Interest rate	Maturity date
<b>Fixed rate:</b>						
UK Treasury	41,043	7.00%	06/11/2001	–	–	–
UK convertible bond	632	8.00%	31/10/2005	–	–	–
European convertible bond	1,091	4.50%	18/05/2001	658	4.50%	18/05/2001
US convertible bond	139	6.75%	01/08/2004	117	6.75%	01/08/2004
<b>Floating rate:</b>						
UK Treasury index linked (interest rate linked to RPI)	4,288	5.35%	24/09/2001	4,068	5.21%	24/09/2001
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>

#### Short term investments:

	2000	1999
	£'000	£'000
5.6875% sterling term deposit (matured 5 January 2001)	4,000	–
	<u>          </u>	<u>          </u>

#### Cash:

UK deposits	7,786	27,528
Foreign deposits – US dollar	319	–
– Taiwan dollars	125	3
	<u>          </u>	<u>          </u>
	8,230	27,531
	<u>          </u>	<u>          </u>

The cash deposits generally comprise call or short term money market deposits of less than one month.

Short term debtors and creditors have been excluded from the disclosure of financial instruments.

### 11. Debtors

	2000	1999
	£'000	£'000
<b>Due within one year:</b>		
Income accrued	765	452
Sales for subsequent settlement	1,279	523
Taxation recoverable	131	87
Other debtors	134	61
	<u>          </u>	<u>          </u>
	2,309	1,123
	<u>          </u>	<u>          </u>

## NOTES TO THE ACCOUNTS *continued*

### 12. Creditors

	2000	1999
	£'000	£'000
<b>Amounts falling due within one year:</b>		
Purchases for subsequent settlement	377	130
Proposed final dividend	713	705
Other creditors and accruals	417	500
	1,507	1,335

Included in other creditors and accruals is £309,000 (1999 – £358,000) in respect of the investment management fee.

### 13. Financial liabilities

#### Overseas currency loan

The overseas currency loan (yen denominated) becomes due for repayment on 7 January 2004. The interest rate on the loan until maturity is 2.5%. The initial cost of the loan was £3,000,000, market value £3,233,000 (1999 – £3,343,000). The fair value of the loan is not materially different from the carrying value.

Short-term debtors and creditors have been excluded from the disclosure of financial instruments.

### 14. Called-up share capital

		2000	1999
Authorised:			
Ordinary shares of 25p:	Number	109,000,000	109,000,000
	£'000	27,250	27,250
Allotted, issued and fully paid:			
Ordinary shares of 25p:	Number	83,873,599	82,961,686
	£'000	20,968	20,740

At the Annual General Meeting in April 2000 Shareholders granted the Company authority to purchase shares in the market up to 12,435,956 Ordinary shares (equivalent to 14.99% of its issued share capital at that date). No Ordinary shares were bought back during the year and, therefore at 31 December 2000 the Company's authority to buy back shares remained unchanged at 12,435,956. Under the provisions of the Company's Articles share buy-backs are funded from the realised capital reserve. The nominal value of the share capital would be maintained by the provision of a capital redemption reserve.

At 1 January 2000 there were 4,845,663 Warrants in issue, which entitle the holders to subscribe for one Ordinary share per Warrant at a price of 100p. On 1 May 2000, in accordance with the terms and subject to the conditions of the Warrants, 911,913 Ordinary shares were allotted in respect of Warrants on which the subscription rights had been exercised. At 31 December 2000 there were 3,933,750 Warrants in issue which entitle the holders to subscribe for one Ordinary share per Warrant at a price of 100p, exercisable on 30 April (or, if later, the date thirty days after the date on which copies of the audited accounts of the Company for its then immediately preceding financial year are dispatched to shareholders) in any of the years 2001 to 2003 inclusive.

### 15. Reserves

	Share premium	Warrant reserve	Capital reserve – realised	Capital reserve – unrealised	Revenue reserve
	£'000	£'000	£'000	£'000	£'000
Balance at 1 January 2000	67,900	2,204	91,061	245,725	1,647
Arising on exercise of warrants	684	–	–	–	–
Transfer on warrants exercised	415	(415)	–	–	–
Net gain on realisation of investments	–	–	126,727	–	–
Decrease in unrealised appreciation	–	–	–	(181,796)	–
Exchange difference on currency loan	–	–	–	110	–
Other exchange differences	–	–	79	–	–
Retained net revenue for the year	–	–	–	–	65
Balance at 31 December 2000	68,999	1,789	217,867	64,039	1,712

## NOTES TO THE ACCOUNTS *continued*

### 16. Reconciliation of movements in shareholders' funds

	2000	1999
	£'000	£'000
Shareholders' funds at 1 January 2000	429,277	170,982
Total recognised gains and losses for the year (after dividend payments)	(54,815)	258,235
Proceeds from exercise of warrants	912	60
Shareholders' funds at 31 December 2000	375,374	429,277

### 17. Net asset value per Ordinary share

The net asset value per Ordinary share and the net assets attributable to the Ordinary shareholders at the year end calculated in accordance with the Articles of Association were as follows:

	2000	1999	2000	1999
			£'000	£'000
Ordinary shares – basic	447.55p	517.44p	375,374	429,277
– diluted (FRS14)	431.43p	494.22p	375,374	429,277
– fully diluted	431.98p	494.40p	379,308	434,123

The movements in the year of the assets attributable to the ordinary shares were as follows:

Total net assets at 1 January 2000	429,277	170,982
Total recognised gains and losses for the year	(54,102)	258,940
Dividend appropriated in the year	(713)	(705)
Proceeds from exercise of warrants	912	60
Total net assets at 31 December 2000	375,374	429,277

Net asset value per Ordinary share is based on net assets as shown above and 83,873,599 (1999 – 82,961,686) Ordinary shares, being the number of Ordinary shares in issue at each date.

The diluted net asset value per Ordinary share, calculated in accordance with Financial Reporting Standard 14 (FRS14) is 431.43p (1999 – 494.22p). This is based on net assets as shown above and on 87,006,178 (1999 – 86,859,078) Ordinary shares, being the number of Ordinary shares in issue at the year end plus the notional number of Ordinary shares that would have been issued for no consideration using a year end share price of 491.0p (1999 – 511.0p).

The fully diluted net asset value per Ordinary share has been calculated on the assumption that the warrants in issue were fully exercised at the year end at 100p each, resulting in net assets as shown above and 87,807,349 (1999 – 87,807,349) Ordinary shares in issue.

The number of outstanding warrants at 31 December 2000 was 3,933,750 (1999 – 4,845,663).

### 18. Reconciliation of net revenue before finance costs and taxation to net cash inflow from operating activities

	2000	1999
	£'000	£'000 (restated)
Net revenue on ordinary activities before finance costs and taxation	888	802
(Increase)/decrease in accrued income	(320)	76
(Increase) in debtors	(73)	(41)
(Increase)/decrease in creditors	(83)	264
Income tax suffered	(38)	(77)
Overseas tax suffered	(26)	(11)
Net cash inflow from operating activities	348	1,013

## NOTES TO THE ACCOUNTS *continued*

### 19. Analysis of changes in net funds

	At 1 January 1999 £'000	Cash flows £'000	Exchange movement £'000	At 31 December 2000 £'000
Cash at bank and in hand	27,531	(19,301)	–	8,230
Current asset investments	–	4,000	–	4,000
Loans due within more than year	(3,343)	–	110	(3,233)
	<u>24,188</u>	<u>(15,301)</u>	<u>110</u>	<u>8,997</u>

### 20. Derivatives and Other Financial Instruments

In accordance with the corporate objective of maximising total returns the Company invests in securities on a worldwide basis. The Company makes use of gearing to achieve improved performance in rising markets. Other financial instruments consist of cash, short term debtors and creditors.

The main risks arising from the Company's financial instruments are market price, foreign currency, liquidity and interest rate risks. The Manager's policies for managing these risks, which have been applied throughout the year, are summarised below.

#### Market Price Risk

The Company's investment portfolio is exposed to market price fluctuations which are monitored by the Manager in pursuance of the corporate objective. Securities held by the Company are valued at mid-market prices (Accounting Policy (b)). These valuations also represent the fair value of the investments.

#### Foreign Currency Risk

Herald invests on a worldwide basis and the balance sheet can be affected by movements in foreign currency exchange rates. The list of equity investments on pages 13 to 16 shows the countries in which the Company is invested. The securities in the portfolio are priced in local currency or euros.

The Company does not hedge the sterling value of investments that are priced in other currencies. Overseas income is subject to currency fluctuations. The Company does not hedge this currency risk.

The Company has authority to write options against individual shares held within the portfolio. No such transactions were undertaken in the year under review.

The main foreign currency exposure at 31 December 2000 is detailed in note 10 Financial assets and note 13 Financial liabilities.

#### Liquidity Risk

The Company's assets mainly comprise readily realisable securities. Cash balances are held with The Bank of New York Europe Limited. Short term flexibility is achieved by an overdraft facility.

#### Interest Rate Risk

The majority of the Company's assets are equity shares and other investments which neither pay interest nor have a maturity date. However, the Company does hold Treasury stocks and Convertible Bonds, the interest rate and maturity dates of which are detailed in note 10 Financial assets. Interest is accrued on sterling cash balances at a rate linked to the UK base rate.

At the year end the Company had borrowings totalling yen 551,550,000 (£3.2 million market value) which become due for repayment in January 2004 (see note 13).

# NOTICE OF ANNUAL GENERAL MEETING

Notice is hereby given that the Annual General Meeting of Herald Investment Trust plc will be held at 12 Charterhouse Square, London EC1M 6AX on 18 April 2001 at 11.30 am for the following purposes:

## Ordinary Business

1. To receive and adopt the Directors' report, the annual accounts and the Auditors' report in respect of the year ended 31 December 2000.
2. To declare a dividend of 0.85p per share in respect of the year ended 31 December 2000.
3. To re-elect Mr M Boase as a Director of the Company.

To consider resolution No. 4, special notice having been received of the intention to propose the resolution as an ordinary resolution (see note 4).

4. To reappoint Mr T Abell, who has reached the age of 70, as a Director of the Company.
5. To reappoint Ernst & Young as Auditors to the Company
6. To authorise the Directors to fix the remuneration of the Auditors.

## Special Business

To consider and, if thought fit, to pass the following Special Resolution:

7. THAT, the Company be generally and subject as hereinafter appears unconditionally authorised in accordance with Section 166 of the Companies Act 1985 (the "Act") to make market purchases (within the meaning of Section 163 of the Act) of its issued shares of 25p each in the capital of the Company in substitution for any existing authority under section 166 of the Act but without prejudice to any exercise of any such authority prior to the date hereof.

### PROVIDED ALWAYS THAT

- (i) the maximum number of shares hereby authorised to be purchased shall be 14.99% of the issued share capital on the date on which this resolution is passed;
- (ii) the minimum price which may be paid for a share shall be 25p;
- (iii) the maximum price which may be paid for a share shall be an amount equal to 105% of the average of the middle market quotations for a share taken from and calculated by reference to the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the share is purchased;
- (iv) any purchase of shares will be made in the market for cash at prices below the prevailing net asset value per share (as determined by the Directors);
- (v) unless previously varied, revoked or renewed, the authority hereby conferred shall expire at the conclusion of the Annual General Meeting of the Company to be held in 2002; and
- (vi) the Company may make a contract to purchase shares under the authority hereby conferred prior to the expiry of such authority and may make a purchase of shares pursuant to any such contract notwithstanding such expiry.

By order of the Board

*Baillie Gifford & Co.*  
Secretaries

Registered Office:  
12 Charterhouse Square  
London EC1M 6AX

14 March 2001

## NOTES

1. A shareholder entitled to attend and vote at the meeting is entitled to appoint one or more proxies to attend and, on a poll, to vote in his stead. Such proxy need not be a member of the Company.
2. A form of proxy is enclosed and to be valid must be lodged with the Registrars of the Company not less than forty-eight hours before the time fixed for the meeting.
3. To be entitled to attend and vote at the meeting (and for the purpose of the determination by the Company of the number of votes they may cast), members must be entered on the Company's register of members at 11.30 am on 16 April 2001 ("the specified time"). If the meeting is adjourned to a time not more than 48 hours after the specified time applicable to the original meeting, that time will also apply for the purpose of determining the entitlement of members to attend and vote (and for the purpose of determining the number of votes they may cast) at the adjourned meeting. If, however, the meeting is adjourned for a longer period then, to be so entitled, members must be entered on the Company's register of members at the time which is 48 hours before the time fixed for the adjourned meeting or, if the Company gives notice of the adjourned meeting, at the time specified in that notice.
4. In accordance with section 293 of the Companies Act 1985 special notice has been given to the Company of the resolution to reappoint a Director who is over the age of 70.
5. No Director has a contract of service with the Company.

## FURTHER SHAREHOLDER INFORMATION

- **How to Invest** The Company's shares and warrants are traded on the London Stock Exchange. They can be bought by placing an order with a stockbroker or by asking a professional adviser to do so.
- **Sources of Further Information on the Trust** The price of shares and warrants is quoted daily in the *Financial Times* and that of the ordinary shares in *The Daily Telegraph* and *The Times*. The NAV per share is calculated and released daily to the London Stock Exchange and monthly to the Association of Investment Trust Companies.
- **Key Dates** Ordinary shareholders normally receive a dividend in respect of each financial year which is normally paid in April. The AGM is normally held in April. Warrants are exercisable on 30 April 2001 to 2003.
- **Taxation** The price of the Ordinary shares (adjusted for the price of attributable warrants) on 21 February 1994, which was the first day of trading, was 90.9p. Up to 5 April 1998 the basis for calculating non-trading gains or losses was the difference between that price, or any subsequent purchase price, and the sale price, using the indexation allowance for inflation. However, this indexation allowance was frozen at 5 April 1998, and replaced by a taper relief. Taper relief, however, cannot create or increase a loss. Any shareholder uncertain of his or her position is recommended to seek expert advice.
- **PEPs/ISAs** The Ordinary shares of the Company are qualifying investments for personal equity plans and individual saving accounts. PEPs ceased to be available for further investment from 5 April 1999. The ISA is a new tax efficient investment product introduced by the Government. Any individual contemplating investment should consult his or her own adviser.

### **Herald is an investment trust. Investment trusts offer investors the following advantages:**

- Participation in a diversified portfolio of shares.
- Constant supervision at low cost by experienced professional managers.
- Freedom from capital gains tax on capital profits realised within the portfolio.
- The opportunity to achieve improved performance for shareholders' funds in rising markets by the borrowing of additional money.



