HERALD INVESTMENT TRUST plc

REPORT & ACCOUNTS

31 December 2001

CONTENTS

COMPANY SUMMARY

COMPANY DATA AT 31 DECEMBER 2001		
Total assets less current liabilities	**Shareholders' funds**	**Market capitalisation**
£276m	**£273m**	**£266m**

Policy and Objective	Herald's objective is to achieve capital appreciation through investments in smaller quoted companies, in the areas of communications and multi-media. Investments will be made throughout the world but at least 50% of the portfolio will be invested in the UK and Europe. 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 ⅔ Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies) and ⅓ Russell 2000 (small cap) Technology Index (in sterling terms).
Management Details	Herald Investment Management Limited ('HIML') is the appointed investment manager 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 84,453,686 ordinary shares of 25p each which are issued and fully paid. There are also 3,353,663 Warrants which are exercisable at 100p each on 30 April in either 2002 or 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 payable in arrears.
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.

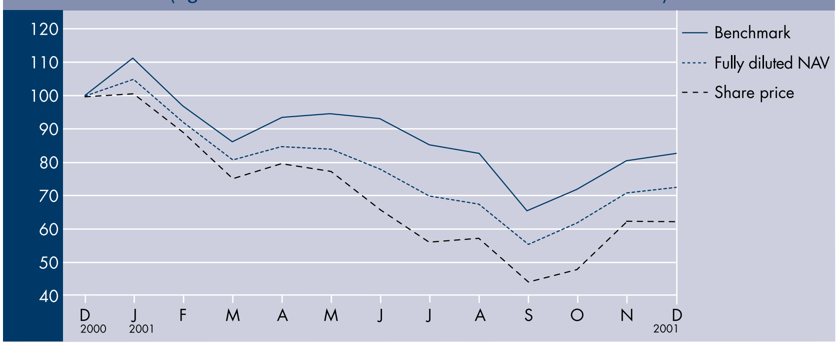
YEAR'S SUMMARY

	31 December 2001	31 December 2000	% change
Total assets (before deduction of bank loan)	£275.6m	£378.6m	(27.2)
Bank loan	£2.9m	£3.2m	9.4
Equity shareholders' funds	£272.7m	£375.4m	(27.4)
Net asset value per ordinary share	322.9p	447.5p	(27.8)
Diluted net asset value per ordinary share (FRS 14)	314.5p	431.4p	(27.1)
Fully diluted net asset value per ordinary share	314.4p	432.0p	(27.2)
Share price	306.0p	491.0p	(37.7)
Warrant price	212.5p	382.5p	(44.4)
FTSE 100	5,217.4	6,222.5	(16.2)
FTSE All-Share	2,523.9	2,983.8	(15.4)
FTSE Small Cap	2,579.2	3,183.3	(19.0)
Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies)	2,283.4	2,702.2	(15.5)
Russell 2000 (small cap) Technology Index (in sterling terms)	102.1	128.3	(20.4)
Benchmark composite index			(17.1)
Dividend per ordinary share	0.85p	0.85p	–
Earnings per ordinary share (basic)	1.36p	0.93p	46.2
Expense ratio	1.07%	1.40%	
(Discount)/premium (to basic net asset value)	(5.3%)	9.7%	
(Discount)/premium (to diluted net asset value (FRS14))	(2.7%)	13.8%	

	Year to 31 December 2001		Year to 31 December 2000	
Year's high and low (on month end values)	**High**	**Low**	**High**	**Low**
Share price	495.0p	218.5p	652.5p	458.0p
Warrant price	394.5p	125.0p	551.5p	361.5p
Net asset value	470.3p	246.6p	732.6p	447.3p
Fully diluted net asset value	453.7p	240.1p	697.7p	431.7p
Premium/(discount) (to fully diluted net asset value)	13.7%	(11.6%)	13.8%	(7.2%)

	31 December 2001	31 December 2000
Total return per ordinary share (basic)		
Revenue	1.36p	0.93p
Capital	(123.01p)	(65.67p)
Total	(121.65p)	(64.74p)

HERALD'S SHARE PRICE, FULLY DILUTED NAV AND BENCHMARK* (in sterling terms)
(figures have been rebased to 100 at 31 DECEMBER 2000)



Source: Thomson Financial 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).
Dividends are not reinvested.

LONG TERM PERFORMANCE SUMMARY

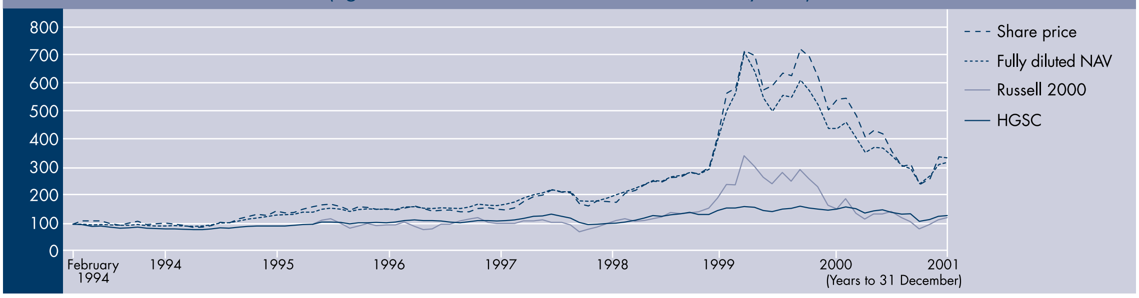
The following charts indicate how an investment in Herald has performed relative to its comparative indices (applied retrospectively) and its underlying fully diluted net asset value over the period since inception of the Company.

	31 December 2001	Inception 16 February 1994	% change
Fully diluted net asset value per ordinary share	314.4p	98.7p	218.5
Share price	306.0p	90.9p	236.6
Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies)	2,283.4	1,750.0	30.5
Russell 2000 (small cap) Technology Index (in sterling terms)	102.1	83.2*	22.7
FTSE 100	5,217.4	3,417.7	52.7
FTSE All-Share	2,523.9	1,717.8	46.9
FTSE Small Cap	2,579.2	2,076.1	24.2

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

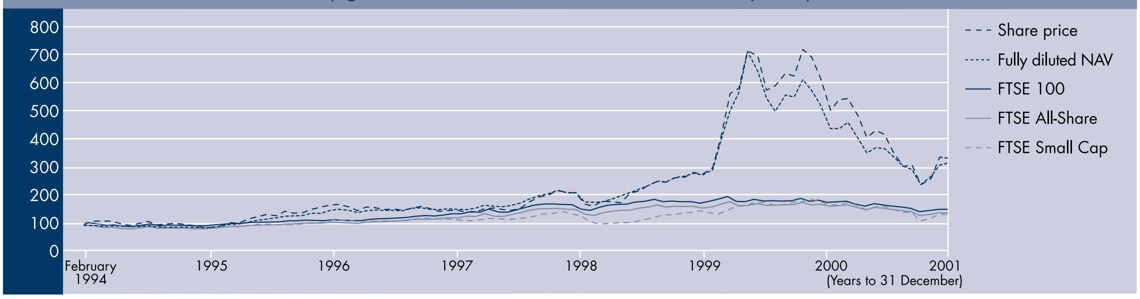
RELATIVE PERFORMANCE OF HERALD'S FULLY DILUTED NAV AND SHARE PRICE TO THE COMPONENT INDICES OF THE COMPOSITE BENCHMARK SINCE INCEPTION

(figures have been rebased to 100 at 16 February 1994)



RELATIVE PERFORMANCE OF HERALD'S FULLY DILUTED NAV AND SHARE PRICE TO FTSE INDICES SINCE INCEPTION

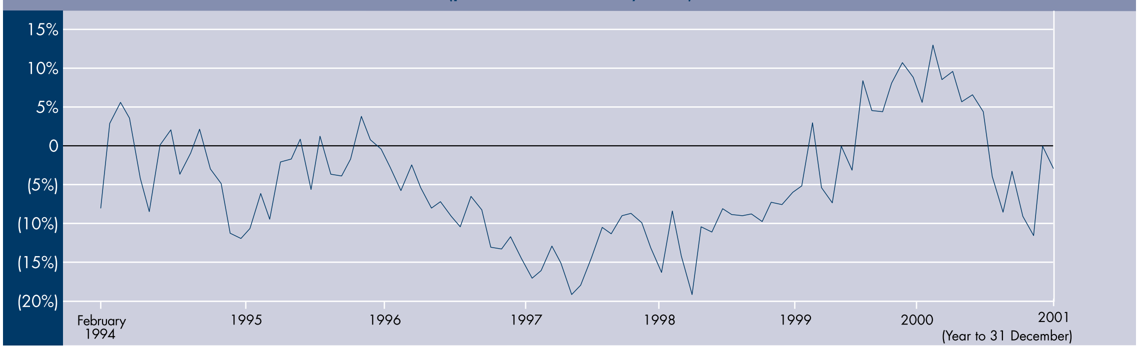
(figures have been rebased to 100 at 16 February 1994)



Source: Thomson Financial Datastream

PREMIUM/(DISCOUNT) TO FULLY DILUTED NET ASSET VALUE

(plotted on a monthly basis)



Source: Thomson Financial Datastream

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 69, 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 71, was formerly deputy chairman of Baring Investment Management Limited, chairman of Foreign & Colonial Eurotrust plc and chairman of the Association of Investment Trust Companies.

Clay Brendish, CBE, aged 54, was appointed to the Board on 23 July 2001. He has been in the computer systems environment and high technology industry for over 30 years. He was formerly Executive Chairman of Admiral plc and, in turn, Deputy Chairman of CMG plc when the companies merged, he has also held a number of Government advisory posts. He is a trustee of the Economist Newspapers Limited, a member of the Independent Television Commission, a council member of the City University of London and is President of the Institute of Management.

Justin Dukes, aged 60, is chairman of ECIC Management Limited, Intelmedia Limited and Intelfax 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 64, joined Bowthorpe plc (now Spirent plc, the international network technology company) in 1962, and was financial director from 1982 until his retirement in 1999.

Douglas McDougall, OBE, aged 57, was appointed to the Board on 13 February 2002. He has extensive experience in the fund management industry and is a former senior partner of Baillie Gifford & Co. He is chairman of The Law Debenture Corporation plc, Foreign & Colonial Eurotrust PLC, The Independent Investment Trust PLC and 3i Bioscience Investment Trust plc. He is a former chairman of IMRO, of the Association of Investment Trust Companies and of the Fund Managers' Association.

Clive Parritt, FCA, aged 58, 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 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.
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Tel: 0131 222 4000

Registered Office

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London EC1M 6AX

Company Number

2879728 (England and Wales)

Manager

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

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CHAIRMAN'S STATEMENT

The difficult market background in 2001 has adversely affected Herald Investment Trust in its eighth year. The derating of many of the Trust's underlying investments that started in 2000 continued in 2001, and this was compounded by trading conditions that transpired to be even weaker than the Manager expected. The portfolio entered the year much more defensively positioned in choice of stocks, and with over 15% in cash and gilts, compared with a year earlier. In 2000 net disposals of £44m were made from the UK portfolio, and we modified the remit so that the UK element could be reduced. The Trust is now at least 50% UK and Europe as compared with at least 50% in the UK previously. Over the same period the US element was increased by £14m. Whilst this proved absolutely the correct direction, it transpired that the move was not aggressive enough to avoid the adverse market movements in the UK and Europe in particular. The UK portfolio was down c40%, and Europe a similar amount. In spite of this the overall reduction in assets was limited to 27%. This reflected the high cash/gilt balances, the reduction in the UK weighting, which at one point fell to a low of 45%, utilising the flexibility in last year's change of remit to its maximum, and much stronger performances in the US and Far East markets. Furthermore, the defensive stock selection led to the greatest outperformance relative to the average performance of stocks in the Trust's defined remit, in each of its four geographic markets, in any year of the Trust's history. Nevertheless, this is not reflected in performance relative to the Hoare Govett Smaller Companies Index (HGSCI), which remains in the long term the most important benchmark. We view the technology bubble as a transitory aberration, which has passed. The HGSCI declined only 15.5%, and the Russell 2000 Technology Index in the US, fell 22.5% in local currency terms. However, investors should also be aware that the sectors in which the fund focuses have performed much worse. For example the FTSE-Information Technology index fell 66.3%, and Techmark 100 fell 42.6%, in spite of the much stronger contribution from the healthcare and biotechnology stocks, in which this Trust does not invest. The HGSCI media sector fell by 39.4%, which provided no shelter in the storm. In fact the weighted average decline of the four sectors in the HGSCI, which include most of the Trust's UK holdings, fell 49.2%.

It is interesting to note that in both the US and Europe large capitalisation stocks in the target sectors declined slightly more than small capitalisation stocks. The Manager had hoped that the smaller company focus would have provided slightly more protection than has transpired. This reflected a cautious view on the more difficult environment for the major markets of PCs and telecommunications including mobile phones, which are so heavily weighted in the world technology indices. This caution proved correct, but has led to a further derating of stocks across the board including smaller companies. Unfortunately the Manager does not see a resumption of growth in these major markets to the levels of the second half of the 1990s, and remains concerned that the product cycles of much of the sector are ex-growth, which may not be popularly perceived. Technology investing is all about product cycles, and we continue to look for emerging new companies, and we strongly believe that the smaller companies arena provides opportunities for this. In the media sector, terrestrial TV's structural difficulties were foreseen. Eventually there will be a recovery in the advertising cycle, albeit it is strange in the UK to have a sharp advertising downturn coinciding with a consumer boom. Advertising may remain weak even when interest rates start to rise and the consumer retreats.

The high cash and gilt level has led to an increase in revenue, so we are able to maintain a dividend with improved cover. As in previous years all expenses have been charged through the profit and loss account. We are pleased that we have been able to pay a dividend, albeit modest, throughout the life of the Trust. Clearly capital appreciation is the principal objective.

Overall, whilst we reiterate last year's warning, that future performance from yesterday's growth markets may prove difficult, and whilst there remain more macro uncertainties than usual, we are more confident that there are opportunities to exploit. Investors must, I fear, be patient, but valuations clearly have a much lower starting point as well.

Changes to Board

Tim Abell, who has been a Director of the Company since its inception in 1994, will not be standing for re-election at the Annual General Meeting on 17 April 2002. We would like to thank him for his enormous contribution during his time on the Board and wish him well in the future.

We would also like to welcome on to the Board Clay Brendish who brings to the Board over 30 years' experience in the computer systems environment and high technology industry. Clay Brendish was formerly Executive Chairman of Admiral plc and, in turn, Deputy Chairman of CMG plc when the companies merged, he has also held a number of Government advisory posts. He is a trustee of the Economist Newspapers Limited, a member of the Independent Television Commission, a council member of the City University of London and is President of the Institute of Management.

In addition, we are pleased to report that Douglas McDougall, OBE, has agreed to join the Board. Douglas McDougall has extensive experience in the fund management industry and is a former senior partner of Baillie Gifford & Co. He is chairman of the Law Debenture Corporation plc, Foreign & Colonial Eurotrust PLC, The Independent Investment Trust PLC and 3i Bioscience Investment Trust plc. He is a former chairman of IMRO, of the Association of Investment Trust Companies and of the Fund Managers' Association.

Shareholders will be asked to vote on their appointment at the Annual General Meeting.

Martin Boase
Chairman

13 February 2002

INVESTMENT MANAGERS' REPORT

It is incredibly depressing for any Manager to report such a decline in assets. While the return on capital for shareholders is disappointing –27%, the return on effort for the Manager is dispiriting, particularly when we broadly read the macro scene correctly. One consolation is to look sideways and realise how much worse we could have done, and indeed most people have done when addressing our target sectors! However, there is a much more important positive element. As far as we were concerned the speculative bubble was a scary period, and the market has become much healthier.

Fundamentally we aim to understand business in general, and the companies in which we invest in particular – we are not comfortable gambling in the momentum game. There was a period when the market was driven by speculators, who did not follow our basic principles, which meant that for a time our skills were irrelevant – well fortunately not completely irrelevant. We were lucky enough to enjoy a share price appreciation in many of our investments way above the level that fundamentals could justify. The agony of 2000 was how much to sell of companies with sound long term prospects, but a share price very forward looking. We did aggressively take profits in the latter part of 1999 and the first half of 2000, and our move into cash and US equities, and away from conceptually valued stocks helped limit our decline in 2001. The other difficulty was the extraordinarily frenetic pace reflected in fund managers' desks being buried in mounds of flotation documents, and their diaries filled with meetings continuously from breakfast to dinner, day in day out. It was also difficult to cope time wise with the extraordinary level of interest from private investors and others. I am afraid this also led to less successful investments than we are accustomed to making, when decisions had to be made quicker than we would like. In retrospect, we should have been braver and stood back more, but we recognise that our task is to second guess markets and timing is more difficult than fundamentals! As the solid companies hit the stratosphere, we had to take greater risks to find value by investing in early stage companies, some of which have proved successful, but not all. It is a relief to return to a more normal market where there is time to reflect, and time to do due diligence on companies before the offer closes, and the chance to invest in sound businesses at sensible valuations and worthwhile allocations, and eat sandwiches for lunch!

From the start of 1999 to the end of 2001 – pre-bubble and burst, we have retained an increase in basic assets per share of 57%. Over this period the FTSE media sector has risen 7.6%, the FTSE-Information Technology index has fallen 42.3%, which generally account for 75% of the portfolio. The US market returns have been somewhat better. For example Bloomberg's software index is only down 4.7%. Unfortunately we could not benefit from the better performances in the healthcare, pharmaceutical and biotechnology sectors, which are not in the chosen remit, because we have no specialist expertise to offer there.

It is interesting to compare the cumulative returns from pre-bubble to the end of 2001:

Overall since 31 December 1998 to 31 December 2001

Herald Basic NAV	+56.5%
Russell 2000 Technology Index	–5.4%
Russell 1000 Technology Index	–19.7%
NASDAQ	–11.0%
HGSCI	+25.6%
FTSE-Information Technology	–42.3%
FTSE-Media	+7.6%

We would contend that the extraordinary bubble gave us a one-off opportunity to make some supernormal profits, which we are now able to re-invest at much more sensible levels.

Portfolio performance attribution for the 12 months to 31 December 2001.
Computed relative to customised benchmark (⅔ Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies) and ⅓ Russell 2000 (small cap) Technology Index (in sterling terms)) with net income reinvested.

PERFORMANCE ATTRIBUTION (in sterling terms)								
	Benchmark allocation	Herald asset allocation		Performance*		Contribution to relative return	Contribution attributable to:	
							Stock selection	Asset allocation
	01.01.01	01.01.01	31.12.01	Herald	Benchmark			
Equity markets	%	%	%	%	%	%	%	%
UK	66.7	56.8	51.5	(40.5)	(13.0)	(18.6)	(18.1)	(0.5)
Europe ex. UK	–	7.2	5.6	(42.7)	–	(2.7)	–	(2.7)
Americas	33.3	16.9	22.0	(8.0)	(20.5)	2.6	2.8	(0.2)
Japan	–	0.7	0.2	(58.2)	–	(0.3)	–	(0.3)
Asia Pacific ex. Japan	–	4.6	5.8	12.9	–	1.4	–	1.4
Bonds	–	12.2	9.7	5.0	–	3.4	–	3.4
Cash	–	2.5	6.3	(0.6)	–	0.6	–	0.6
Yen loan	–	(0.9)	(1.1)	(10.6)	–	(0.1)	–	(0.1)
Total	100.0	100.0	100.0	(26.6)	(14.0)	(14.7)	(15.8)	1.4

Source: HSBC.

* The above returns are calculated on a total return basis with net income reinvested.

Contributions cannot be added together, as they are geometric; for example, to calculate how a return of (26.6%) (against a benchmark of (14.0%)) translates into a relative return of (14.7%), divide the portfolio return of 73.4 by the benchmark return of 86.0 and subtract one.

UK

Since inception the UK has cumulatively made c85% of the Trust's profits (nearly £190m), and UK dividends have paid Herald Investment Trust's dividends. Initially the fund was over 90% in the UK, but fell in 1996 when an element of the portfolio was invested in the US, and in the Far East. For an extended period the Trust was c⅔rds in the UK, and that remains our internal benchmark. However, following the bubble that was so pronounced in the UK and even more in Europe, this proportion fell with aggressive profit taking to 55.7% at the end of 2000. For much of 2001 it has been lower still reflecting the under performance of the UK market, this year. It reached a low of c45% in September with the market and following the realisation of Tempus Group for £6.65m during the Havas/WPP bid period. In fact there have been several takeovers this year totalling c£18m – Tempus, Lynx and Action proving the most relevant, and helpful to performance. This was significant in performance terms in relation to a portfolio of £140.6m at the year-end. In spite of the bids net investment into the UK has been £18.5m reflecting the belief that value has emerged from time to time. Whilst many companies have disappointed at the earnings level, some have not, but have still declined viciously in share price terms. An extreme example is Surfcontrol, which declined from $47 to $20.5, but delivered well.

	Year to 31 December 2001
Herald UK portfolio	–40.5%
HGSCI (extended capital gains ex. investment companies)	–15.5%
HGSCI Media	–39.4%
HGSCI Information Technology	–56.8%
HGSCI Electronics	–42.6%
HGSCI Telecommunications	–43.2%
HGSCI weighted 4 sectors	–49.2%

The media, IT, and telecommunications stocks are all in the Herald remit, some of the electronics sector is, and there are also stocks classified within distribution and support services, but too few to make the sector performance relevant. The figures give an idea of the market background.

In spite of the increased investor interest, and capital raised in the UK by so many companies, it is disappointing how few have come through on the world stage. Even more money has been lost in Europe. The internet is an amazing tool, which shrinks the world, and gives small UK companies a greater chance of competing globally. It would be a great pity if the foolish stampede reverses to the point where sound ideas and businesses struggle to raise the necessary capital.

US

The performance of the Trust's US portfolio justifies the diversification with the US orbit markedly less weak than the European markets, and the US portfolio performance markedly ahead of any US index. The compounded monthly return reports a loss of 8.0%, but the performance of losing £3.1m on a starting value of £62.7m and an ending value of £60.0m, with net investment of £0.4m suggests a simple return of –5.9%, so market timing helped. The net investment of £14m in US equities last year was also helpful, with the defensive purchases generally performing positively. It is hard to get excited about investing outside the US such is the excitement of the leading edge markets there, as well as the dynamism and the respect for shareholders, both culturally and through regulations. However, recent visits have made us concerned that the expectation for a recovery throughout 2002 is too great, and worry that share prices are discounting too rapid a recovery, and recently it has been easier for us to find pricing anomalies in Europe.

	Year to 31 December 2001
Herald US return	– 8.0% compounded
Russell 2000 Technology Index	–22.5% (£ adjusted –20.4%)
Russell 1000 Technology Index	–30.0% (£ adjusted –28.2%)

Europe

The European markets hardly existed, in a smaller companies' sense, when Herald was floated in 1994. The avalanche of new issues over the last four years has changed that. Initially they were launched into a speculative bubble particularly in Germany on astonishingly high valuations. The Neuer Markt declined 60.2% in the year to 1,087 having peaked in March 2000 at 8,522.3 (–87% from peak to 31/12/01). The Nouveau Marche (–62.7%) and Nuovo Mercato (–45.6%) were similarly impacted. Whilst the markets remain primitive there will almost certainly be interesting opportunities to salvage in the wreckage.

Far East

The Far East recovered a little after last year's fall-out. It is interesting that while business confidence and spending has been hit the consumer has carried on spending. This year fewer PCs and mobile phones, but more DVDs etc. These are all made in the Far East. It is difficult to see the Far East bucking the trend too much if their customers in US and Europe slow down their spending.

INVESTMENT CHANGES (£'000)

	Valuation at 31 December 2000	Net acquisitions (disposals)	Appreciation (depreciation)	Valuation at 31 December 2001
Equities:				
UK	210,972	18,451	(88,794)	140,629
Continental Europe	27,334	597	(12,221)	15,710
Americas	62,709	382*	(3,098)	59,993
Japan	2,380	(452)	(1,408)	520
Asia Pacific	16,849	(2,868)*	1,688	15,669
	320,244	16,110	(103,833)	232,521
UK bonds	45,331	(18,855)	(96)	26,380
Total investments	365,575	(2,745)	(103,929)	258,901
Net liquid assets	13,032	3,752	(61)	16,723
Total assets	378,607	1,007	(103,990)	275,624

*Includes £647,000 book cost which has been transferred from the Americas to Asia Pacific due to the reclassification of PSI Technologies.

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

Outlook

Valuations of many of the larger technology stocks seem to be discounting a sharp recovery to previously achieved growth rates. Our caution in last year's accounts on major markets – in particular PCs, mobile phones, telecommunications, B-to-B/B-to-C and terrestrial television has been vindicated. 2002 will not be as bad, but on the whole recovery seems well discounted. The area of the market where there is often evident value is at the very small end. This reflects the polarization of markets, brokers and fund managers towards scale, as well as the fact that the market has not fully digested such low rates of interest. On the whole there is an illiquidity discount at the microcap level. There is high stock specific risk at this end of the market, and this risk is compounded by the fact that undervalued situations will remain undervalued. This Trust has made the most money when stocks have been purchased on a value basis, have grown into the radar screen, and gained a growth multiple. That continues to be one of our main philosophies. Whilst we would rather not envisage great returns this year we would prefer to manage the Herald Investment Trust portfolio than a FTSE 100 portfolio, and look forward to a solid year.

13 February 2002

TOP TWENTY HOLDINGS

A brief description of the twenty largest holdings in companies are as follows:

Acal

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	£7,243,000
% of total assets	2.6
% of issued share capital held	4.6

Alba

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	£6,336,000
% of total assets	2.3

Azlan Group

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	£5,471,000
% of total assets	2.0
% of issued share capital held	3.9

Telemetrix

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 ADSL markets and ISDN market.

Country	United Kingdom
Valuation	£5,261,000
% of total assets	1.9
% of issued share capital held	3.6

Anite Group

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	£5,200,000
% of total assets	1.9

Lynx Group

Lynx is a leading provider of software solutions for financial services to customers such as Independent Financial Advisers, banks, building societies, asset and fund managers.

Country	United Kingdom
Valuation	£5,190,000
% of total assets	1.9

Biotrace International

Biotrace designs, manufactures and sells a range of systems for rapid hygiene and biological testing. Products include contamination detecting kits sold predominantly to the food and drink sector.

Country	United Kingdom
Valuation	£4,812,000
% of total assets	1.7
% of issued share capital held	9.6

Alphameric

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 and accounting systems for the retail industry and keyboards.

Country	United Kingdom
Valuation	£4,361,000
% of total assets	1.6
% of issued share capital held	3.9

OneSource Information

OneSource provides web-based business and financial information. The company integrates up-to-date information on public and private companies from various information sources.

Country	United States
Valuation	£4,122,000
% of total assets	1.5
% of issued share capital held	5.2

Chordiant Software

Chordiant Software provides customer relationship management software that enables companies to offer their customers personalised marketing, sales programmes and customer support across multiple communications channels.

Country	United States
Valuation	£3,913,000
% of total assets	1.4

Scottish Radio Holdings

Scottish Radio has leading radio stations such as Radio Clyde, and has successfully diversified into Northern Ireland newspapers.

Country	United Kingdom
Valuation	£3,756,000
% of total assets	1.4

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	£3,641,000
% of total assets	1.3
% of issued share capital held	9.9

Taylor Nelson Sofres

Taylor Nelson Sofres is a market research company that collects and provides data about customers needs, competitors, market trends and overviews.

Country	United Kingdom
Valuation	£3,397,000
% of total assets	1.2

Diploma

Diploma is the holding company for a group of subsidiaries that distribute an assortment of products including scientific equipment and telcommunications products.

Country	United Kingdom
Valuation	£3,365,000
% of total assets	1.2
% of issued share capital held	4.3

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	£3,177,000
% of total assets	1.2

Motionposter

Motionposter has developed a new marketing medium encompassing the use of a series of illuminated posters that are fixed to a rail or metro tunnel wall. The Group plans to present travellers with a view of a silent cinema film that is created in the window of the train as it travels through the tunnel.

Country	United Kingdom
Valuation	£3,125,000
% of total assets	1.1
% of issued share capital held	7.6

Advent Software

Advent Software is a leading provider of software products that automate and integrate the investment management process. Its flagship product is a portfolio accounting and management system for investment firms. About half of the company's sales comes from services and support.

Country	United States
Valuation	£3,089,000
% of total assets	1.1

Logitech

Logitech produces computer mice that help the user move the cursor around the screen, as well as trackballs, game controllers, keyboards, PC video cameras and multimedia speakers.

Country	Switzerland
Valuation	£3,017,000
% of total assets	1.1

Minorplanet Systems

Minorplanet Systems provides a vehicle management service using the Global Positioning System to measure and record the position of a vehicle at regular time intervals as well as measure and log the vehicles speed and distance travelled.

Country	United Kingdom
Valuation	£2,891,000
% of total assets	1.0

Johnston Press

Johnston Press plc is a major publisher of quality local newspapers both paid and free, in addition to offering associated publishing services. The company also has over 70 local internet sites offering news coverage throughout the UK.

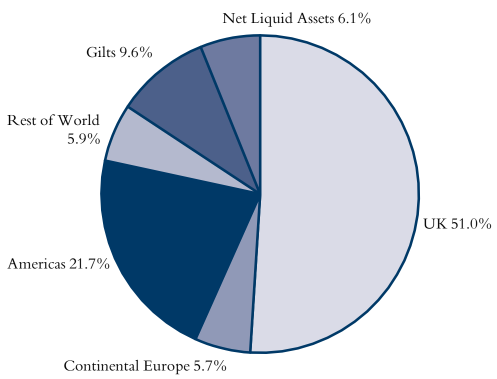
Country	United Kingdom
Valuation	£2,852,000
% of total assets	1.0

CLASSIFICATION OF INVESTMENTS

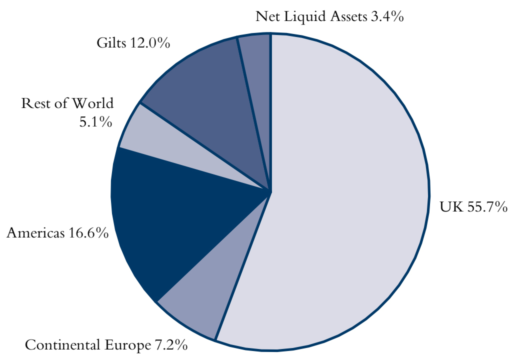
Classification	UK %	Continental Europe %	Americas %	Japan %	Asia Pacific %	2001 Total %	2000 Total %
EQUITIES: (including convertible and preference stock)							
INDUSTRIALS	**5.0**	**1.7**	**3.9**	**0.2**	**1.9**	**12.7**	**10.7**
Aerospace and defence	–	–	–	–	–	–	0.1
Electronic and electrical equipment	5.0	1.7	3.9	0.2	1.9	12.7	10.6
CONSUMER GOODS	**1.7**	**–**	**0.2**	**–**	**–**	**1.9**	**0.3**
Healthcare and pharmaceuticals	1.7	–	0.2	–	–	1.9	0.3
SERVICES AND UTILITIES	**21.4**	**1.5**	**5.3**	**–**	**2.7**	**30.9**	**33.3**
Distributors	5.2	–	0.8	–	–	6.0	6.2
Retailers	–	–	–	–	–	–	0.1
Leisure, entertainment and hotels	0.4	–	0.2	–	–	0.6	0.4
Media and photography	12.5	1.5	1.4	–	2.7	18.1	20.6
Support services	1.9	–	2.8	–	–	4.7	4.5
Telecommunication services	1.4	–	0.1	–	–	1.5	1.5
FINANCIALS	**0.1**	**0.2**	**–**	**–**	**–**	**0.3**	**0.3**
Speciality and other finance	0.1	–	–	–	–	0.1	0.1
Investment companies	–	0.2	–	–	–	0.2	0.2
INFORMATION TECHNOLOGY	**22.8**	**2.3**	**12.3**	**–**	**1.1**	**38.5**	**40.0**
Information technology hardware	4.4	0.4	3.1	–	0.9	8.8	12.6
Software and computer services	18.4	1.9	9.2	–	0.2	29.7	27.4
TOTAL EQUITIES (including convertible and preference stock)	**51.0**	**5.7**	**21.7**	**0.2**	**5.7**	**84.3**	
Total equities – 2000 (including convertible and preference stock)	55.7	7.2	16.6	0.6	4.5		84.6
GILTS	**9.6**	**–**	**–**	**–**	**–**	**9.6**	12.0
NET LIQUID ASSETS	**5.7**	**–**	**–**	**–**	**0.4**	**6.1**	3.4
TOTAL ASSETS (before deduction of bank loan)	**66.3**	**5.7**	**21.7**	**0.2**	**6.1**	**100.0**	
Total assets – 2000	70.7	7.2	16.7	0.6	4.8		100.0
BANK LOAN	**–**	**–**	**–**	**–**	**(1.0)**	**(1.0)**	(0.9)
EQUITY SHAREHOLDERS' FUNDS	**66.3**	**5.7**	**21.7**	**0.2**	**5.1**	**99.0**	
Equity shareholders' funds – 2000	70.7	7.2	16.7	0.6	3.9		99.1
Number of equity investments (including convertible and preference stock)	100	18	81	2	21	222	249

GEOGRAPHICAL SPREAD OF INVESTMENTS

31 December 2001



31 December 2000



DETAILED LIST OF INVESTMENTS

AT 31 DECEMBER 2001

Classification	Name	Market value £'000	%
UNITED KINGDOM			
Electronic and electrical equipment	Alba	6,336	
	Amstrad	2,091	
	Intelek	1,213	
	Linx Printing Technologies	3,641	
	TTP Communications	386	
		13,667	5.0
Healthcare and pharmaceuticals	Biotrace International	4,812	1.7
Distributors	Abacus Polar	884	
	Acal	7,243	
	Deltron Electronics	837	
	Diploma	3,365	
	†Netcentric Systems	105	
	Northamber	2,025	
		14,459	5.2
Leisure, entertainment and hotels	†Cyberes	773	
	†World Travel Holdings	356	
		1,129	0.4
Media and photography	365 Corporation	261	
	†Alibi Communications	132	
	†Ambient	1,537	
	Applied Optical Technologies	2,156	
	†BV Group	135	
	Bloomsbury Publishing	793	
	†Channel Health	270	
	¶†Clipserver.com	10	
	†Digital Classics	333	
	†First Artist Corp	520	
	GWR Group	1,894	
	Incisive Media	653	
	Informa Group	2,844	
	Jazz FM	2,183	
	Johnston Press	2,852	
	Maiden Group	1,290	
	†Motionposter	3,125	
	Music Choice Europe	474	
	§Quarto Group	896	
	Scottish Radio Holdings	3,756	
	Sterling Publishing Group	157	
	†Synigence	222	
	Taylor & Francis Group	524	
	Taylor Nelson Sofres	3,397	
	Teamtalk media	1,661	
	†Ten Alps Comm	327	
	Wilmington Group	1,726	
	WMRC	500	
		34,628	12.5
Support services	BNB Resources	329	
	Harvey Nash Group	456	
	†Ingenta	713	
	Lorien	1,166	
	‡†Mondas 8% CULS	546	
	PSD Group	714	
	†RDL Group	225	
	†Rexonline	500	
	†Thomson Intermedia	524	
		5,173	1.9
Telecommunication services	IMS Group	1,018	
	PNC Telecom	750	
	Project Tele.com	1,977	
		3,745	1.4
Speciality and other finance	†Adaptive Venture Managers	81	
	*HIML Jersey Ltd	–	
	*Herald Investment Management Ltd	252	
		333	0.1
Information technology hardware	IQE (EASDAQ)	1,675	
	Plasmon	2,152	
	Roxboro Group	1,424	
	Telemetrix	5,261	
	*Ubinetics Holdings	1,000	
	Vislink	504	
		12,016	4.4

DETAILED LIST OF INVESTMENTS *continued*

AT 31 DECEMBER 2001

Classification	Name		Market value £'000	%
Software and computer services	Affinity Internet Holdings		423	
	AIT Group		1,948	
	Alphameric		4,361	
	Anite Group		5,200	
	Azlan Group		5,741	
	†Bsoftb		218	
	†Clarity Commerce Solutions		1,067	
	Electronic Data Processing		940	
	Expocentric		330	
	†Fayrewood		1,922	
	Guardian IT		465	
	†Harrier Group		1,117	
	†i-Documentsystems Group		1,563	
	†IMS Maxims		200	
	Interactive Digital Solutions		525	
	†Intechnology		712	
	†Iq-Ludorum		531	
	Keystone Solutions Group		659	
	Lynx Group		5,190	
	¶Manpower Software		281	
	†Minorplanet Systems		2,891	
	MMT Computing		660	
	Netbenefit		182	
	†Netcall		380	
	Northgate Information Solutions		2,596	
	NSB Retail Systems		257	
	†OneClickHR		1,470	
	Patsystems		420	
	Retail Decisions		1,267	
	Rolfe & Nolan		928	
	SDL Group		768	
	Sherwood International		1,789	
	Smartlogik Group		136	
	Statpro Group		688	
	Superscape		195	
	Surfcontrol (EASDAQ)		1,992	
	Vocalis Group		655	
			50,667	18.4
	TOTAL UNITED KINGDOM EQUITIES		140,629	51.0
CONTINENTAL EUROPE				
Electronic and electrical equipment	Draka Holdings	Netherlands	1,225	
	Lintech Computer	Germany	349	
	Logitech	Switzerland	3,017	
			4,591	1.7
Media and photography	N.R.J. Groupe	France	3,177	
	Publigroupe	Switzerland	624	
	United Internet NMBC	Germany	431	
			4,232	1.5
Investment companies	Sadot R & D	Israel	507	0.2
Information technology hardware	Nera	Norway	1,159	
	Teles NMBC	Germany	29	
			1,188	0.4
Software and computer services	*Atex Media	Norway	–	
	Esker	France	180	
	IONA Techs	Ireland	619	
	Merkantildata	Norway	273	
	Profdoc	Norway	1,095	
	Plaut NM	Germany	258	
	Reply	Italy	1,927	
	Horizon Technology	Ireland	160	
	Smartforce	Ireland	680	
			5,192	1.9
	TOTAL EUROPEAN EQUITIES		15,710	5.7
AMERICAS				
Electronic and electrical equipment	Alvarion		41	
	Artesyn Technologies		512	
	Asat Holdings		260	
	Elantec		923	
	Harmonic Lightwaves		619	
	HI/FN		198	
	M-Systems Flash Disk Pioneer		1,847	
	Plexus		593	
	Power Integrations		314	
	Radisys		777	
	Remec		1,399	

DETAILED LIST OF INVESTMENTS *continued*

AT 31 DECEMBER 2001

Classification	Name		Market value £'000	%
Electronic and electrical equipment (*continued*)	‡Reptron		116	
	Rockford		590	
	Silicon Image		258	
	Sipex		1,457	
	Three-Five Systems		219	
	Zoran		673	
			10,796	3.9
Healthcare and pharmaceuticals	Sonosite		706	0.2
Distributors	Black Box Delivery		1,526	
	Jaco Electronics		304	
	Pioneer Standard Electronics		523	
			2,353	0.8
Leisure, entertainment and hotels	Pegasus Solutions		585	0.2
Media and photography	Cinar B	Canada	121	
	Cinar B subvoting		8	
	Emmis Broadcasting		650	
	Lions Gate Entertainment	Canada	430	
	Mediacom Comms 'A'		502	
	Modem MDA. Poppe Tyson 'A'		184	
	Multivision Communications	Canada	8	
	Penton Media		129	
	Scholastic		1,729	
			3,761	1.4
Support services	Computer Horizons		287	
	First Consulting Group		1,505	
	FYI INC		921	
	Management Network Group		237	
	OneSource Information		4,122	
	Optio Software		210	
	Sapient		159	
	Technology Solutions		153	
			7,594	2.8
Telecommunication services	Lexent		343	0.1
Information technology hardware	Asyst Technology Corp.		1,666	
	Computer Network Technology		489	
	Credence Systems Corp.		1,276	
	DMC Stratex Networks		641	
	Lecroy Corp. Com		513	
	Micros Systems		517	
	MRV Communications		1,428	
	Nova Measuring Systems		471	
	Rainbow Technologies		508	
	Rimage		167	
	Signal Technologies		158	
	Spectralink		589	
			8,423	3.1
Software and computer services	Advanced Digital Information		1,405	
	Advent Software		3,089	
	Akami Techs		536	
	Brightstar Information Technology Group		9	
	Carreker-Antinori		517	
	Centra Software		2,721	
	Chordiant Software		3,913	
	Datastream Systems		381	
	Epiq. Systems		1,263	
	Extended Systems		257	
	HPL Techs		613	
	I-Many		663	
	Keynote Systems		321	
	Logicvision		263	
	Macromedia		611	
	Macrovision		242	
	MSC Software		429	
	Multex		201	
	Netscout Systems		543	
	PDF Solutions		505	
	Retalix		1,355	
	Roxio		569	
	RSA Security		2,609	
	Seachange International		469	
	Serena Software		747	
	Sphinx International		31	
	SPSS		243	
	Stellent		406	
	Versity		521	
			25,432	9.2
	TOTAL AMERICAN EQUITIES		59,993	21.7

DETAILED LIST OF INVESTMENTS *continued*

AT 31 DECEMBER 2001

Classification	Name			Market value £'000	%
JAPAN					
Electronic and electrical equipment	Yamaichi Electronics			251	
	Yokowo			269	
				520	0.2
	TOTAL JAPANESE EQUITIES			520	0.2
ASIA PACIFIC					
Electronic and electrical equipment	Arcontech Corp	Hong Kong		360	
	Advantech Co	Taiwan		530	
	Chroma Ate	Taiwan		634	
	¶Kingboard Chemicals	Hong Kong		380	
	Korea Electronic	Korea		606	
	PSI Technologies Holdings	Philippines		204	
	SCMP Group	Hong Kong		2,154	
	Venture Marketing	Singapore		396	
				5,264	1.9
Media and photography	BMC Media	Australia		65	
	Health Comm Network	Australia		445	
	I-Cable Comm	Hong Kong		1,572	
	Informatics Holdings	Singapore		721	
	LG ad	Korea		1,374	
	Shaw Brothers	Hong Kong		634	
	Star Publications	Malaysia		2,492	
				7,303	2.7
Information technology hardware	JC Hyun System	Korea		100	
	NERA Telecommunications	Singapore		1,220	
	V-Tech Holdings	Hong Kong		328	
	Wyse Technology Taiwan	Taiwan		905	
				2,553	0.9
Software and computer services	Catuity Inc	Australia		91	
	Solution 6	Australia		458	
				549	0.2
	TOTAL ASIA PACIFIC EQUITIES			15,669	5.7
	Value of equity stocks		231,379		
	Convertible preference stocks having an element of equity		463		
	Convertible loan stocks having an element of equity		662		
	Warrants having an element of equity		17		
TOTAL EQUITY INVESTMENTS				232,521	84.3
FIXED INTEREST	UK Treasury $2\frac{1}{2}$% IL 2003		16,794		
	UK Treasury 2% IL 2006		9,586		
TOTAL FIXED INTEREST				26,380	9.6
NET LIQUID ASSETS				16,723	6.1
TOTAL ASSETS AT MARKET VALUE (before deduction of bank loan)				275,624	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
2000	378,607	(3,233)	375,374	447.55	431.43	491.00	382.50	13.8
2001	**275,624**	**(2,892)**	**272,732**	**322.94**	**314.53**	**306.00**	**212.50**	**(2.7)**

* 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
2000	6,508	778	0.93	0.85	1.40	86	101
2001	**4,728**	**1,145**	**1.36**	**0.85**	**1.07**	**84**	**101**

* 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".

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
1995	134	140	95	93	100¶¶	176	130	103
1996	153	150	109	107	98	194	162	106
1997	174	150	126	113	103	199	170	110
1998	204	178	124	104	113	201	180	113
1999	501	562	213	158	240	126	170	115
2000	437	540	186	154	154	137	170	118
2001	**319**	**337**	**160**	**130**	**123**	**200**	**170**	**119**

all figures have been rebased to 100.

Compound Annual Returns

5 year	15.8%	17.6%	8.0%	4.0%	4.6%	0.6%	1.0%	2.3%
From inception	15.6%	16.4%	6.1%	3.4%	3.5%	10.4%	7.9%	2.5%

¶¶ Index at 9 April 1996, being the first date funds were first available for international investment.

DIRECTORS' REPORT

The Directors present their report and accounts for the year ended 31 December 2001.

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 years ended 31 December 1999 and 2000. 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 formally request approval under Section 842 of the Income and Corporation Taxes Act 1988 each year in accordance with a recent agreement reached between the Inland Revenue and the AITC whereby provisional Section 842 status may be granted outwith the Corporation Tax Self Assessment (CTSA) regime. Final approval of Section 842 status will not be received until two years after the end of the accounting period, when the two year enquiry period permitted under the CTSA rules has expired.

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

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 2001 borrowings of yen 551,550,000 (£2.9 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 £1,145,000 (2000 – £778,000).

The Directors recommend a dividend of 0.85p per Ordinary share for the year ended 31 December 2001, which, if approved by the Annual General Meeting, will be payable on 19 April 2002 to holders registered on 22 March 2002. The payment will amount to £718,000 and the transfer to reserves will therefore be £427,000.

The net asset value (NAV) of the Company at 31 December 2001 represented a value of 322.94p per Ordinary share (diluted (FRS14) 314.53p). This represented a fall of 27.8% during the year (diluted (FRS14) 27.1%) and a rise of 227.2% (diluted (FRS14) 218.5%) 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 and the Investment Managers' Report incorporates a review of the highlights of the year to 31 December 2001, and the outlook for the Company.

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 with the exception of Mr Clay Brendish who was appointed on 23 July 2001.

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 Board *continued*

The Director's at the year end, and their interests in the Company, all of which are beneficially owned, were as follows:

Name	Number of Ordinary Shares 2001	2000	Number of Warrants 2001	2000
Martin Boase	50,000	50,000	–	–
Timothy Abell	11,158	11,158	2,000	2,000
Clay Brendish (appointed 23 July 2001)	–	–	–	–
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 C M Brendish was appointed to the Board on 23 July 2001. His appointment falls to be confirmed at the Annual General Meeting.

Mr D C P McDougall was appointed to the Board on 13 February 2002. His appointment also falls to be confirmed at the Annual General Meeting. Mr McDougall has no interest in any shares in the Company.

Mr C A Parritt retires by rotation and, being eligible, is recommended by the Board for re-election.

Mr T Abell will retire from the Board at the conclusion of the Annual General Meeting.

There have been no changes intimated in the Directors' interests up to 21 February 2002.

Management and Administration

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

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 0.08333% of the Company's net asset value.

At 31 December 2001 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 also act as company secretary.

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

Significant Shareholdings

At 21 February 2002 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	12,346,868	14.6
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 2001.

Auditors

On 28 June 2001, Ernst & Young, the Company's auditor, transferred its entire business to Ernst & Young LLP, a limited liability partnership incorporated under the Limited Liability Partnerships Act 2000. The Directors consented to treating the appointment of Ernst & Young as extending to Ernst & Young LLP with effect from 28 June 2001. A resolution to re-appoint Ernst & Young LLP as the Company's auditor and to authorise the Directors to fix their remuneration will be put to the forthcoming Annual General Meeting.

Annual General Meeting

The Annual General Meeting of the Company will be held on 17 April 2002. 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 18 April 2001 it was resolved that the Company be authorised to purchase in the market up to 12,572,652 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 8 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 2003. 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 UK Listing Authority) 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 8 in the Notice of Meeting, will last until the date of the Annual General Meeting in 2003. 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

25 February 2002

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;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for 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

Colin McCarthy
Director

25 February 2002

CORPORATE GOVERNANCE

Code of Best Practice

The Directors have considered the principles set out in the Combined Code and 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 principles B.1 to B.3 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 as independent custodian of the Company's investments.

The managers have a compliance function in accordance with FSA 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 Baillie Gifford & Co.'s auditors. A copy of the internal controls report is submitted to the Board. Baillie Gifford's head of compliance and internal audit department 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 they have procedures in place to review its effectiveness on a regular basis.

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 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 the 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 throughout the Company's financial year, 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 FSA. 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 for the full year which accord with the guidance for directors on compliance with the Combined Code.

On behalf of the Board

Colin McCarthy
Director

25 February 2002

INDEPENDENT AUDITORS' REPORT

TO THE MEMBERS OF HERALD INVESTMENT TRUST PLC

We have audited the Company's financial statements for the year ended 31 December 2001 which comprise the Statement of Total Return, Balance Sheet, Cash Flow Statement, and the related notes 1 to 20. These financial statements have been prepared on the basis of the accounting policies set out therein.

Respective responsibilities of Directors and Auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements, United Kingdom Auditing Standards and the Listing Rules of the Financial Services Authority.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, 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 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 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 risks and controls, or form an opinion on the effectiveness of the Company's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. This other information comprises the Year's Summary, Chairman's Statement, Portfolio Review and Directors' Report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom 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 financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

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

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company as at 31 December 2001 and of its net revenue for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

ERNST & YOUNG LLP
Registered Auditor
Edinburgh

25 February 2002

STATEMENT OF TOTAL RETURN

(incorporating the revenue account)

FOR THE YEAR ENDED 31 DECEMBER 2001

	Notes	2001 Revenue £'000	2001 Capital £'000	2001 Total £'000	2000 Revenue £'000	2000 Capital £'000	2000 Total £'000
Losses on investments	9	–	(103,929)	(103,929)	–	(55,069)	(55,069)
Unrealised gain on loan		–	341	341	–	110	110
Currency (losses)/gains		–	(61)	(61)	–	79	79
Income	2	4,728	–	4,728	6,508	–	6,508
Investment management fee	3	(3,205)	–	(3,205)	(5,230)	–	(5,230)
Other administrative expenses	4	(272)	–	(272)	(390)	–	(390)
Net return before finance costs and taxation		1,251	(103,649)	(102,398)	888	(54,880)	(53,992)
Finance costs of borrowings	5	(75)	–	(75)	(84)	–	(84)
Return on ordinary activities before taxation		1,176	(103,649)	(102,473)	804	(54,880)	(54,076)
Tax on ordinary activities	6	(31)	–	(31)	(26)	–	(26)
Return on ordinary activities after taxation		1,145	(103,649)	(102,504)	778	(54,880)	(54,102)
Ordinary dividend payable	7	(718)	–	(718)	(713)	–	(713)
Transfer to/(from) reserves		427	(103,649)	(103,222)	65	(54,880)	(54,815)
Return per Ordinary share	8						
Basic		1.36p	(123.01p)	(121.65p)	0.93p	(65.67p)	(64.74p)
Diluted (FRS 14)		1.32p	(119.45p)	(118.13p)	0.89p	(63.03p)	(62.14p)
Dividend per Ordinary share		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 2001

	Notes	2001 £'000	2001 £'000	2000 £'000	2000 £'000
Fixed assets					
Investments	9		258,901		365,575
Current assets					
Debtors	11	1,857		2,309	
Short term investments		–		4,000	
Cash at bank and in hand		19,243		8,230	
		21,100		14,539	
Creditors: amounts falling due within one year	12	(4,377)		(1,507)	
Net current assets			16,723		13,032
			275,624		378,607
Creditors: amounts falling due after one year					
Overseas currency loan	13		(2,892)		(3,233)
TOTAL NET ASSETS			272,732		375,374
Capital and reserves					
Called-up share capital	14		21,113		20,968
Share premium	15		69,698		68,999
Warrant reserve	15		1,525		1,789
Capital reserve – realised	15		204,113		217,867
Capital reserve – unrealised	15		(25,856)		64,039
Revenue reserve	15		2,139		1,712
EQUITY SHAREHOLDERS' FUNDS	16		272,732		375,374
NET ASSET VALUE PER ORDINARY SHARE					
Basic	17		322.94p		447.55p
Diluted (FRS14)			314.53p		431.43p
Fully diluted			314.42p		431.98p

The accounts were approved by the Board of Directors and signed on their behalf on 25 February 2002.

Colin McCarthy
Director

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

CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2001

	Notes	2001 £'000	2001 £'000	2000 £'000	2000 £'000
Net cash inflow from operating activities	18		1,571		348
Servicing of Finance					
Loan interest		(79)		(83)	
Net cash outflow from servicing of finance			(79)		(83)
Financial investment					
Purchase of investments		(124,980)		(212,244)	
Sale of investments		130,695		196,392	
Currency movement		(61)		79	
Net cash inflow/(outflow) from financial investment			5,654		(15,773)
Equity dividend paid			(713)		(705)
Net cash inflow/(outflow) before use of liquid resources and financing			6,433		(16,213)
Management of liquid resources†					
Decrease/(increase) in term deposits			4,000		(4,000)
Financing					
Issue of Ordinary shares		580		912	
Net cash inflow from financing			580		912
INCREASE/(DECREASE) IN CASH	19		11,013		(19,301)
RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS	19				
Increase/(decrease) in cash in period			11,013		(19,301)
(Decrease)/increase in short term investments			(4,000)		4,000
Exchange movement on loan			341		110
MOVEMENT IN NET FUNDS IN PERIOD			7,354		(15,191)
NET FUNDS AT 1 JANUARY			8,997		24,188
NET FUNDS AT 31 DECEMBER			16,351		8,997

† 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, are set out below.

(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

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.

2. Income

	2001 £'000	2000 £'000
Income from investments		
Franked dividends from listed investments	1,763	1,843
Franked dividends from unlisted investments	35	35
Unfranked income from unlisted (AIM) UK convertible bonds	41	11
Overseas dividend income	502	495
Unfranked income from foreign convertible bonds	5	35
Gilt interest income	1,844	2,597
	4,190	5,016
Other income		
Deposit interest	534	1,446
Underwriting commission	4	46
	538	1,492
Total income	4,728	6,508
Total income comprises:		
Dividends	2,300	2,373
Interest from investments	1,890	2,643
Other	538	1,492
	4,728	6,508
Income from investments		
Listed UK	3,607	4,440
Listed overseas	507	530
Unlisted	76	46
	4,190	5,016

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

	2001 £'000	2000 £'000
Investment management fee	2,890	4,743
Irrecoverable VAT thereon	315	487
	3,205	5,230

Herald Investment Management Limited are appointed investment managers under a management agreement which is terminable on twelve months notice. Their fee is calculated on a monthly rate of 0.08333% of the Company's net asset value and is subject to VAT at the appropriate rate.

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

	2001 £'000	2000 £'000
Custodian's fees	48	125
Registrars' fees	31	46
Directors' fees	57	53
Auditors' fees – audit work	10	9
AITC **it**s campaign	18	43
Miscellaneous expenses	108	114
	272	390

Directors' fees

The fees of the Chairman are £13,200 (2000 – £13,200) per year and those of the four Directors who served on the Board throughout the year are £9,900 each (2000 – £9,900 each) per year. In addition Mr C M Brendish, who was appointed a Director on 23 July 2001, received fees of £4,394.

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

	2001 £'000	2000 £'000
Bank loan repayable within five years	75	84

6. Taxation

	2001 £'000	2000 £'000
Overseas taxation	31	26

7. Ordinary dividend

	2001	2000	2001 £'000	2000 £'000
Proposed dividend per ordinary share	0.85p	0.85p	718	713

The proposed dividend will be paid on 19 April 2002 to all shareholders on the register as at the close of business on 22 March 2002.

8. Return per Ordinary share

	2001 Revenue	2001 Capital	2001 Total	2000 Revenue	2000 Capital	2000 Total
Basic	1.36p	(123.01p)	(121.65p)	0.93p	(65.67p)	(64.74p)
Diluted	1.32p	(119.45p)	(118.13p)	0.89p	(63.03p)	(62.14p)

Basic revenue return per Ordinary share is based on the net revenue on ordinary activities after taxation of £1,145,000 (2000 – £778,000) and on 84,262,972 Ordinary shares (2000 – 83,571,294) 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 £103,649,000 (2000 – loss £54,880,000) and on 84,262,972 Ordinary shares (2000 – 83,571,294) 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 (341.6p (2000 –572.5p)) and the Subscription price of 100p, giving a weighted average of 86,769,677 (2000 – 87,065,313) shares. The income return of 1.32p (2000 – 0.89p) and capital return of (119.45p) (2000 – (63.03p)) are based on the same income and capital figures used in the basic return calculation.

9. Fixed assets – investments

	2001 £'000	2000 £'000
Listed at market valuation on the London Stock Exchange	143,251	224,799
Listed at market valuation on other recognised Stock Exchanges	91,892	109,272
AIM	22,506	27,252
Unquoted*	1,252	4,252
Total fixed asset investments	258,901	365,575

	Listed in UK £'000	Listed overseas £'000	AIM £'000	Unquoted £'000	Total £'000
Cost of investments at 1 January 2001	153,793	116,637	26,316	4,557	301,303
Unrealised appreciation/(depreciation) at 1 January 2001	71,006	(7,365)	936	(305)	64,272
Value of investments at 1 January 2001	224,799	109,272	27,252	4,252	365,575
Movements in the year:					
Purchases at cost	80,246	34,580	13,121	–	127,947
Sales – proceeds	(89,903)	(36,921)	(3,868)	–	(130,692)
– realised gains/(losses)	1,688	(12,775)	(2,606)	–	(13,693)
Decrease in unrealised appreciation	(73,263)	(2,264)	(11,709)	(3,000)	(90,236)
Change in listing	(316)	–	316	–	–
Value of investments held at 31 December 2001	143,251	91,892	22,506	1,252	258,901
Cost of investments at 31 December 2001	145,508	101,521	33,279	4,557	284,865
Unrealised depreciation at 31 December 2001	(2,257)	(9,629)	(10,773)	(3,305)	(25,964)
Value of investments at 31 December 2001	143,251	91,892	22,506	1,252	258,901

(Losses)/gains on investments	2001 £'000	2000 £'000
Realised (losses)/gains on sales	(13,693)	126,727
Decrease in unrealised appreciation	(90,236)	(181,796)
	(103,929)	(55,069)

* The unquoted balance comprises Herald Investment Management Limited and HIML Jersey Ltd included at their cost of £251,561 (2000 – £251,561), Ubinetics at £1,000,000 and Atex Media (grey market value at 31 December 2001 of £172,000) at zero.

At 31 December 2001 the Company was the beneficial owner of 14% (2000 – 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.

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:

	2001		2000	
	Market value £'000	Maturity date	Market value £'000	Maturity date
Warrants:				
Sterling	10	31/03/2002	2	22/02/2002
	5	31/08/2002	45	18/05/2001
Hong Kong dollar	2	31/12/2049	–	–

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

	2001			2000		
	Market value £'000	Interest rate	Maturity date	Market value £'000	Interest rate	Maturity date
Fixed rate:						
UK Treasury	–	–	–	41,043	7.00%	06/11/2001
UK convertible bond	546	8.00%	31/10/2005	632	8.00%	31/10/2005
European convertible bond	–	–	–	1,091	4.50%	18/05/2001
US convertible bond	116	6.75%	01/08/2004	139	6.75%	01/08/2004
Floating rate:			Weighted average period until maturity			
UK Treasury index linked (interest rate linked to RPI)	26,380	5.36%	2½ years	4,288	5.35%	24/09/2001

	2001 £'000	2000 £'000
Short term investments:		
5.6875% sterling term deposit (matured 5 January 2001)	–	4,000
Cash:		
UK deposits	18,235	7,786
Foreign deposits – US dollar	–	319
– Taiwan dollars	968	125
– Korean wan	40	–
	19,243	8,230

The cash deposits generally comprise call or overnight deposit accounts which are payable on demand. The benchmark rate which determines the interest payments received on cash balances is the bank base rate.

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

11. Debtors

	2001 £'000	2000 £'000
Due within one year:		
Income accrued	498	765
Sales for subsequent settlement	1,276	1,279
Taxation recoverable	8	131
Other debtors	75	134
	1,857	2,309

12. Creditors

	2001 £'000	2000 £'000
Amounts falling due within one year:		
Purchases for subsequent settlement	3,344	377
Proposed final dividend	718	713
Other creditors and accruals	315	417
	4,377	1,507

Included in other creditors and accruals is £227,000 (2000 – £309,000) 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 £2,892,000 (2000 – £3,233,000). 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

		2001	2000
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	84,453,686	83,873,599
	£'000	21,113	20,968

At the Annual General Meeting in April 2001 Shareholders granted the Company authority to purchase shares in the market up to 12,572,652 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 2001 the Company's authority to buy back shares remained unchanged at 12,572,652. 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 2001 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. On 30 April 2001, in accordance with the terms and subject to the conditions of the Warrants, 580,087 Ordinary shares were allotted in respect of Warrants on which the subscription rights had been exercised. At 31 December 2001 there were 3,353,663 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 either 2002 or 2003.

15. Reserves

	Share premium £'000	Warrant reserve £'000	Capital reserve – realised £'000	Capital reserve – unrealised £'000	Revenue reserve £'000
Balance at 1 January 2001	68,999	1,789	217,867	64,039	1,712
Arising on exercise of warrants	435	–	–	–	–
Transfer on warrants exercised	264	(264)	–	–	–
Net loss on realisation of investments	–	–	(13,693)	–	–
Decrease in unrealised appreciation	–	–	–	(90,236)	–
Exchange difference on currency loan	–	–	–	341	–
Other exchange differences	–	–	(61)	–	–
Retained net revenue for the year	–	–	–	–	427
Balance at 31 December 2001	69,698	1,525	204,113	(25,856)	2,139

16. Reconciliation of movements in shareholders' funds

	2001 £'000	2000 £'000
Shareholders' funds at 1 January 2001	375,374	429,277
Total recognised gains and losses for the year (after dividend payments)	(103,222)	(54,815)
Proceeds from exercise of warrants	580	912
Shareholders' funds at 31 December 2001	272,732	375,374

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:

	2001	2000	2001 £'000	2000 £'000
Ordinary shares – basic	322.94p	447.55p	272,732	375,374
– diluted (FRS14)	314.53p	431.43p	272,732	375,374
– fully diluted	314.42p	431.98p	276,086	379,308

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

	2001	2000
Total net assets at 1 January 2001	375,374	429,277
Total recognised gains and losses for the year	(102,504)	(54,102)
Dividend appropriated in the year	(718)	(713)
Proceeds from exercise of warrants	580	912
Total net assets at 31 December 2001	272,732	375,374

Net asset value per Ordinary share is based on net assets as shown above and 84,453,686 (2000 – 83,873,599) 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 314.53p (2000 – 431.43p). This is based on net assets as shown above and on 86,711,381 (2000 – 87,006,178) 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 306.0p (2000 – 491.0p).

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 (2000 – 87,807,349) Ordinary shares in issue.

The number of outstanding warrants at 31 December 2001 was 3,353,663 (2000 – 3,933,750).

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

	2001 £'000	2000 £'000
Net revenue on ordinary activities before finance costs and taxation	1,251	888
Decrease/(increase) in accrued income	273	(320)
Decrease/(increase) in debtors	59	(73)
(Increase) in creditors	(97)	(83)
Income tax repaid/(suffered)	116	(38)
Overseas tax suffered	(31)	(26)
Net cash inflow from operating activities	1,571	348

19. Analysis of changes in net funds

	At 1 January 2000 £'000	Cash flows £'000	Exchange movement £'000	At 31 December 2001 £'000
Cash at bank and in hand	8,230	11,013	–	19,243
Current asset investments	4,000	(4,000)	–	–
Loans due within more than one year	(3,233)	–	341	(2,892)
	8,997	7,013	341	16,351

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, where material unlisted investments are valued by the Directors on the basis of latest information in line with the relevant principles of the British Venture Capital Association Guidelines (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 2001 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. Short term flexibility is achieved by an overdraft facility of £2 million with The Bank of New York.

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 (£2.9 million market value) (2000 – 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 17 April 2002 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 2001.
2. To declare a dividend of 0.85p per share in respect of the year ended 31 December 2001.
3. To re-elect Mr C A Parritt as a Director of the Company.
4. To elect Mr C M Brendish as a Director of the Company.
5. To elect Mr D C P McDougall as a Director of the Company.
6. To reappoint Ernst & Young LLP as Auditors to the Company.
7. 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:

8. 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 2003; 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

6 March 2002

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 15 April 2002 ("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. 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 2002 or 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.
- **ISAs/PEPs** The Ordinary shares of the Company are qualifying investments for individual saving accounts and personal equity plans. PEPs ceased to be available for further investment from 5 April 1999. 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.

Pillans & Wilson, Edinburgh. 67326