

# **HERALD INVESTMENT TRUST plc**

## **Interim Report**

For the six months ended 30 June 2000

### **Investment Policy**

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

## CHAIRMAN'S REVIEW

This is my seventh interim statement for the Trust, and I am pleased to say that further progress has been made. However, the period has proved a remarkable roller coaster ride, with the first ten weeks continuing the remarkable re-rating of technology stocks in the UK in particular, then mid-March through to May seeing a considerable correction. In early March the fund was +55% from the start of the year. In contrast Techmark was +52% and Russell2000 Technology Index was +60%. It is therefore somewhat disappointing that growth by the end of June in the Trust's basic NAV/share was only up 9.9%. However, this compared to the Techmark Index declining by 10%, and the FTSE-IT index falling 23% in the period. The gain was only retained by aggressive profit taking, in spite of limited liquidity in many cases, particularly in February and March when c£50m was realised from the UK portfolio, and c£7m from Europe. Overall £84m has been realised from the UK portfolio in the first half, and c£34m reinvested, with only May and June having a positive net investment. In spite of some net investment in the US and the Far East markets, which have proved more robust than the UK, cash levels remain high. The Manager believes that interim figures for many of the UK technology companies are unlikely to prove a pleasant surprise, and that better opportunities to invest the cash will emerge in the next few months. There is no doubt that traditional IT spend has not accelerated out of the Y2k doldrums, while the internet euphoria is evaporating fast as a number of dotcoms show the fragility of their business model, with alarming cash outflows sometimes proving terminal. The traditional media sector has enjoyed tangible benefits from the dotcom advertising binge. Although start-ups with heavy ad spends may diminish, traditional businesses will continue to develop their e-commerce, and internet activities and this should compensate for the fading start-ups.

### Summary of Performance

	At inception 16 February 1994	At 31 December 1999	At 30 June 2000	Performance since 31 December 1999	Performance since inception
Basic NAV per share	98.7p	517.4p	568.6p*	+9.9%†	+476.1%
Fully diluted					
NAV per share	98.9p	494.2p	547.6p*	+10.8%	+453.7%
Share price	90.9p	511.0p	575.0p	+12.5%	+532.6%
Warrant price	45.5p	411.0p	476.0p	+15.8%	+946.1%
FTSE 100 Index	3,417.7	6,930.2	6,312.7	-8.9%	+84.7%
HGSC Index					
(ext. cap gains ex IT)	1,750.0	2,762.9	2,701.7	-2.2%	+54.4%
Russell 2000					
Technology Index	—	322.0	355.3	+10.3%	—

\* The NAV figures are stated on a capital only basis, and do not include any income retention at that date. This is because the Company only pays one dividend per year and no provision has been made at this stage. However, the NAV figures given after the Balance Sheet do include the Revenue Reserve uplift for the period. The fully diluted NAV figures given after the Balance Sheet take into account the price of the ordinary shares at the period ends, as required by FRS 14.

† Growth in basic NAV per share was depressed by 1.1% on the exercise of 911,913 warrants. This explains the somewhat anomalous higher return on the fully diluted NAV per share.

Particularly strong contributors have been JSB, Autonomy, Alphameric, Burr-Brown, Telemetrix, MRV, Logitech and M-Systems. In June Texas Instruments announced terms of an acquisition for Burr-Brown, the largest US holding which has been held since 1996. This stock has cumulatively contributed c\$17.5m profits to the fund, and will now be sold, as TI is too large for the remit. Admiral, another stalwart holding, was sold on its acquisition by CMG, at a cumulative profit of nearly £16m. On the other hand Sherwood, IMS and EDP, in particular, all gave up some of the previous year's profit.

### **Capital performance of the Trust from 31 December 1999 to 30 June 2000**

UK Equities	+2.8%
European Equities	+23.5%
US Equities	+29.7%
Other Overseas Equities	-4.9%
Total Portfolio	+11.0%

The UK equity performance in particular does not reflect the cash realised when the market was particularly frothy. This has helped achieve the overall return of 11% in spite of the majority of the portfolio being invested in UK equities.

Income grew by 90% to £3.3m, reflecting a much greater income from interest cash balances and gilts following the high level of cash raised in the first quarter. However, the management fee grew in line with assets by 132%, and other expenses grew 159%. The latter's increase reflects (i) a contribution of £24K to the AITC campaign (ii) a large increase in the number of shareholders reflecting private investor interest and the associated registrar fees totalling £42K(+296%), and (iii) a large increase in custodian fees reflecting both the larger size of the Trust, and a higher number of transactions, a bi-product of the volatile market conditions. Overall, therefore, net income has declined from £0.39m to £0.2m. The Trust targets capital growth, and not income. However, unlike pure technology funds, the Trust has always made a profit, and it is still hoped that a small dividend will be payable this year. However, as the income is the net result of much larger revenue and expenditure figures it is difficult to forecast.

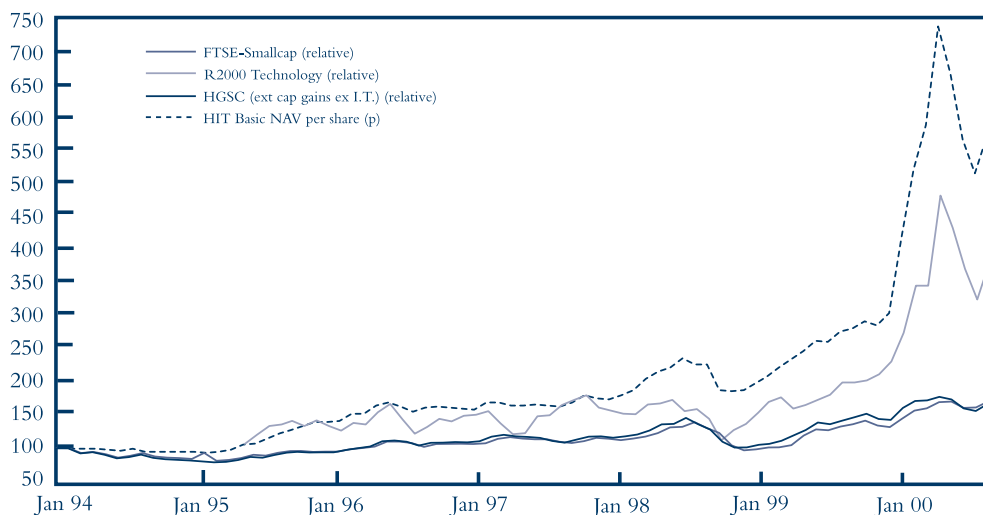
Whilst volatile markets are in some ways unnerving, sensible profit taking and reinvestment at lower levels does provide opportunities to improve the long term performance of the fund. Valuations are now more forward looking than they used to be. This is likely to remain the case, while interest in the area remains strong. This will make performance more difficult, and stock selection more vital than ever. The US has performed better than the UK. There are many outstanding companies in this market, many of which are much more modestly valued than stocks in the UK. European stocks are generally even more expensive than the UK reflecting the interest in the Neuer Markt, and the Nouveau Marche by retail investors, and the shortage of stocks.

Herald is unusual in being an Investment Trust which focuses on investing in smaller companies only in growth sectors, which means that, over the years, a very high proportion of the fund has been invested as primary capital when young emerging companies have been seeking additional capital. For the Manager it has been one of the most fulfilling aspects of their role to watch the companies that they have helped to fund flourish. We are very grateful to a range of smaller London based brokers who have so professionally helped to provide these opportunities in a sensibly regulated way. There is a similar, or even greater professionalism in the US, but conspicuously less so in Germany and other Continental countries. From our practical perspective we do not understand the reasoning behind the proposed Stock Exchange merger which will focus technology stocks on the currently primitive Neuer Markt in Frankfurt.

As stated before the satisfactory performance relative to the FT-All Share Index further vindicates our chosen target market. We continue to believe that the area has more potentially exciting growth situations, and our long term confidence remains.

**Martin Boase**

*26 July 2000*



## STATEMENT OF TOTAL RETURN

for the six months ended 30 June 2000 (Unaudited)

	Six months to 30 June 2000			Six months to 30 June 1999		
	Revenue	Capital	Total	Revenue Restated	Capital	Total
	£'000	£'000	£'000	£'000	£'000	£'000
Gains on investments	—	46,792	46,792	—	55,796	55,796
Unrealised loss/gain on loan	—	(100)	(100)	—	109	109
Currency gain/loss	—	42	42	—	(16)	(16)
Income	3,308	—	3,308	1,737	—	1,737
Investment management fee	(2,795)	—	(2,795)	(1,206)	—	(1,206)
Loan interest	(44)	—	(44)	(36)	—	(36)
Other expenses	(246)	—	(246)	(95)	—	(95)
<b>Net return before tax</b>	<b>223</b>	<b>46,734</b>	<b>46,957</b>	<b>400</b>	<b>55,889</b>	<b>56,289</b>
Taxation	(20)	—	(20)	(10)	—	(10)
<b>Return on ordinary activities after taxation</b>	<b>203</b>	<b>46,734</b>	<b>46,937</b>	<b>390</b>	<b>55,889</b>	<b>56,279</b>
<b>Return per Ordinary share</b>						
— Basic	<b>0.24p</b>	<b>56.12p</b>	<b>56.36p</b>	<b>0.47p</b>	<b>67.40p</b>	<b>67.87p</b>
— Fully diluted	<b>0.23p</b>	<b>53.71p</b>	<b>53.94p</b>	<b>0.46p</b>	<b>65.37p</b>	<b>65.83p</b>

The basic return per Ordinary share calculations are based on a weighted average number of shares in issue during each period. For the period to 30 June 2000, the weighted average number of Ordinary shares was 83,267,327 (1999: 82,921,642).

Comparative figures for 1999 have been restated following the publication of FRS16—Current Tax. This results in a reduction to dividend income and tax charge amounts of £129,000 for the six months to 30 June 1999.

The fully-diluted returns per Ordinary share have been calculated on the weighted average warrants in issue during the period adjusted by the difference between the average price of the Ordinary shares during the period and the Subscription price of £1.00, giving a weighted average of 87,015,024 (1999: 85,502,770) shares. The unadjusted fully-diluted number of shares at 30 June 2000 was 87,807,349 compared to 87,807,349 at 30 June 1999.

There were 3,933,750 warrants in issue at 30 June 2000 (1999: 4,845,663).

## SUMMARISED BALANCE SHEET

at 30 June 2000 (Unaudited)

	30 June 2000 £'000	31 December 1999 £'000
Investments	449,527	405,301
Net current assets	31,041	27,319
Currency loan	(3,443)	(3,343)
Shareholders' funds	477,125	429,277
<b>Capital and Reserves:</b>		
Share capital	20,968	20,740
Share premium account	68,999	67,900
Warrant reserve	1,790	2,204
Capital reserve		
—Realised	184,945	91,061
—Unrealised	198,573	245,725
Revenue reserve	1,850	1,647
	477,125	429,277
<b>Net Asset Value per Ordinary share</b>		
— Basic	568.86p	517.44p
— Fully diluted	547.64p	494.22p

The Balance Sheet at 31 December 1999 is an abridged version of that contained in the full Accounts for that year, which received an unqualified audit report and which have been filed with the Registrar of Companies.

## CASH FLOW STATEMENT

for the six months ended 30 June 2000 (Unaudited)

	Six months to 30 June 2000 £'000	Six months to 30 June 1999 £'000
<b>Operating activities</b>		
Net cash (outflow)/inflow from operating activities	(58)	516
<b>Taxation</b>		
Tax paid	(88)	(7)
<b>Servicing of finance</b>		
Loan interest	(40)	(36)
<b>Capital expenditure and financial investment</b>		
Purchase of investments	(128,419)	(29,239)
Sale of investments	133,549	34,591
Currency movement	42	(16)
<b>Net cash inflow from capital expenditure and financial investment</b>	<u>5,172</u>	<u>5,336</u>
<b>Equity dividend paid</b>	<u>(705)</u>	<u>(746)</u>
<b>NET CASH INFLOW BEFORE FINANCING</b>	<u>4,281</u>	<u>5,063</u>
<b>Financing</b>		
Issue of ordinary shares	912	60
Currency loan	—	3,000
<b>NET CASH INFLOW FROM FINANCING</b>	<u>912</u>	<u>3,060</u>
<b>NET CASH INFLOW</b>		
Decrease/(increase) in cash	(2,807)	1,123
Increase in deposits	8,000	7,000
Increase in cash deposits	<u>5,193</u>	<u>8,123</u>

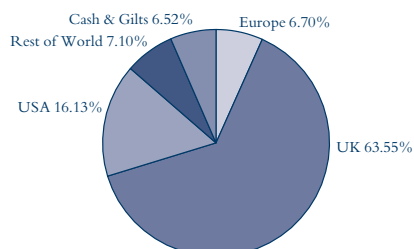
## TOP TWENTY EQUITY HOLDINGS

in companies, by market value at 30 June 2000

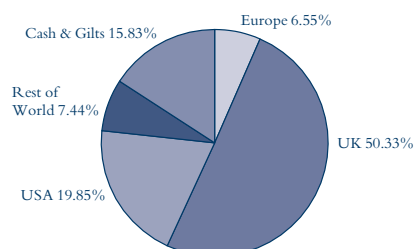
Company	Sector	£'000	% of portfolio
Telemetrix	ISDN testers and semiconductors	13,533	3.01
Burr-Brown (United States)	Analogue semiconductors	10,235	2.28
Alba	Consumer electronics	9,461	2.10
JSB	Internet control software	9,340	2.08
Alphameric	Computer software and services	8,889	1.98
Anite	Computer software and services	8,285	1.84
Sherwood International	Insurance software	8,269	1.84
NRJ (France)	Commercial radio operator	7,938	1.77
ARM	Design RISC Microprocessors	7,434	1.65
Autonomy	Information search technology	6,932	1.54
Informa	Conference/training/magazines	6,835	1.52
GWR	Commercial radio operator	6,769	1.51
Scottish Radio	Commercial radio operator	6,734	1.50
MRV Communications (United States)	Optical network and switching products	6,663	1.48
Azlan	Electronic component distribution	6,420	1.43
Tempus	Media buying	6,150	1.37
Lynx Holdings	Computer systems	5,996	1.33
Amstrad	Consumer electronics goods	5,525	1.23
Acal	Electronic products distribution	5,367	1.19
Teamtalk	Internet sports site	5,127	1.14
		<u>151,902</u>	<u>33.79</u>

## GEOGRAPHIC SPREAD OF INVESTMENTS

31 December 1999



30 June 2000



## **DIRECTORS, MANAGER AND ADVISERS**

### **DIRECTORS**

Martin Boase (Chairman)  
Timothy George Abell  
Justin Paul Dukes  
Colin Michael McCarthy  
Clive Anthony Parritt

### **SECRETARY**

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### **INVESTMENT MANAGER**

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E-mail: [info@heralduk.com](mailto:info@heralduk.com)

### **COMPANY NUMBER**

2879728 (England and Wales)

### **SOLICITORS**

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London EC4A 1BD

### **AUDITORS**

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Edinburgh EH2 2DZ

### **BANKERS**

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### **STOCKBROKERS**

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### **REGISTRARS**

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