

**HERALD INVESTMENT  
TRUST plc**

**Interim Report**

For the six months ended 30 June 2004

**Investment Policy**

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. 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

The Trust targets the IT, media and communications sectors, which recovered last year from an oversold position. Following the rise in the Trust's fully diluted net asset value of 77% in 2003 this half year has seen a period of wholesome consolidation and more modest progress. Overall the net assets have risen 5.6%. In general progress in the figures reported by the companies in the portfolio has been very strong, but this was in part discounted in the rally last year, and sentiment has been adversely affected by macro concerns such as interest rate and oil price rises in spite of the strong fundamentals. Although the fund was geared throughout last year, it was only 103% invested at the start of 2004, and through profit taking had modest net cash by early February. Encouraged by the strong reporting season the Manager has subsequently not raised further cash, as was originally planned.

### **Total return by geography of the Trust from 31 December 2003 to 30 June 2004**

UK Equities	+11.0%
US Equities	-8.9%
European Equities	+10.5%
Far East Equities	-7.6%

The capital return was 5.6% in the first half. The total return of the HGSCI was +10.6% over the same period, which is similar to the UK portfolio within the Trust, albeit the weighted average of the sectors most relevant to the Trust within the index was up only just by 0.61%. The FTSE-Techmark 100 was +15.3%, but the performance was heavily enhanced by biotechnology and healthcare stocks which Herald does not invest in. In contrast the FTSE-IT index was down 5.2%. The US portfolio decline was similar to the Russell 2000 Technology Index (-6.1% in US\$), which is the most relevant benchmark. The US was a materially lower proportion of the fund than in previous years. Generally trading performances were strong, but the market is nervous that further trading improvements will be more difficult. The European portfolio is small, but performed satisfactorily with local returns of 15.6%, reduced by the weak Euro which reduced the return to 10.5%. The Far East portfolio declined 7.6%; a positive Japanese return had a minor impact due to the low weighting. This reflects the difficulties in analysing small companies in Japan.

As in previous years an interim dividend will not be paid.

Although there have been strong trading improvements in general, there has been a flood of paper offerings from new issues, particularly in the UK, and an unusually small number of takeovers. This reflects a backlog of demand following a period when the market was effectively closed, and the excessive financial incentive brokers have to place new stock versus secondary stock. The quality of many of these offerings is not terribly high, and the flow will abate as investors weary. The regulatory environment in the US and the UK which precludes analysts from operating both sides of the Chinese walls, is leaving many small companies increasingly

## CHAIRMAN'S REVIEW *continued*

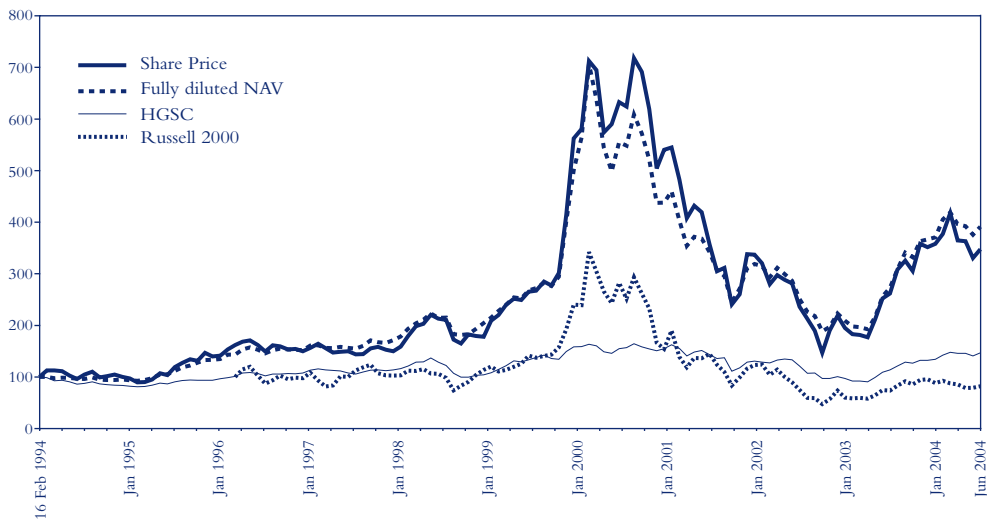
under researched. On balance this will lead to more market inefficiencies which we should be in a good position to exploit. It has become conspicuous that at the current US\$ exchange rate UK executive salaries of the companies in which the Trust invests have become surprisingly high relative to the US, and even more so compared with the Far East. With unemployment low, and house prices high, the UK has become a less competitive place in which to operate. Although the UK has risen to 69% of the net assets, the intention will be to reduce this exposure in the coming months. There is no longer the requirement to have at least 50% of the fund's assets in the UK and Europe.

Enthusiasm for the internet may have become irrational in 2000. Nevertheless usage is showing robust growth as the roll-out of broadband proceeds. Consumer demand has remained robust in the first half utilising most of the world's semiconductor capacity. There has been a strong upturn in capital expenditure in this area, but enterprise software remains, as expected, subdued. More than ever stock selection remains the key. There continue to be interesting small companies thriving in emerging markets.

**Martin Boase**

*22 July 2004*

**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)**



Past performance is no guarantee of future performance.

**STATEMENT OF TOTAL RETURN**  
(Unaudited and incorporating the revenue account\*)

	for the six months ended 30 June 2004		
	Revenue £'000	Capital £'000	Total £'000
Gains on investments	—	17,500	17,500
Unrealised gains on loans	—	215	215
Currency gains	—	174	174
Income	2,375	—	2,375
Investment management fee	(1,905)	—	(1,905)
Other administrative expenses	(129)	—	(129)
<b>Net return before finance costs and taxation</b>	<b>341</b>	<b>17,889</b>	<b>18,230</b>
Finance costs of borrowings	(232)	—	(232)
<b>Return on ordinary activities before taxation</b>	<b>109</b>	<b>17,889</b>	<b>17,998</b>
Tax on ordinary activities	(30)	—	(30)
<b>Return on ordinary activities after taxation</b>	<b>79</b>	<b>17,889</b>	<b>17,968</b>
Ordinary dividend payable (note 2)	—	—	—
<b>Transfer to reserves</b>	<b>79</b>	<b>17,889</b>	<b>17,968</b>
<b>Return per Ordinary share</b> (note 3)			
Basic	<b>0.09p</b>	<b>20.37p</b>	<b>20.46p</b>
Diluted (FRS 14)	—	—	—
Dividend per Ordinary share	—	—	—

\* The revenue column of this statement is the profit and loss account of the Company.  
All revenue and capital items in this statement derive from continuing operations.

**SUMMARY OF PERFORMANCE**

	At inception 16 February 1994	At 31 December 2003	At 30 June 2004	Performance	
				Performance since 31 December 2003	Performance since inception
NAV per share	98.7p	365.4p	<b>385.9p</b>	5.6%	291.0%
Share price	90.9p	325.3p	<b>315.8p</b>	(2.9%)	247.4%
FTSE 100 Index	3,417.7	4,476.9	<b>4,464.1</b>	(0.3%)	30.6%
HGSC Index (ext. cap gains ex. investment companies)	1,750.0	2,346.7	<b>2,560.3</b>	9.1%	46.3%
Russell 2000 (small cap)					
Technology Index (in sterling terms)	83.2*	72.9	<b>67.6</b>	(7.3%)	(18.8%)

\* at 9 April 1996 being the date funds were first available for international investment.  
Past performance is no guarantee of future performance.

**STATEMENT OF TOTAL RETURN**  
(Unaudited and incorporating the revenue account\*)

for the six months ended 30 June 2003			for the year ended 31 December 2003		
Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
—	53,931	53,931	—	136,680	136,680
—	1,021	1,021	—	3,169	3,169
—	—	—	—	100	100
1,772	—	1,772	3,882	—	3,882
(1,069)	—	(1,069)	(2,727)	—	(2,727)
(130)	—	(130)	(259)	—	(259)
573	54,952	55,525	896	139,949	140,845
(282)	—	(282)	(591)	—	(591)
291	54,952	55,243	305	139,949	140,254
(18)	—	(18)	(29)	—	(29)
273	54,952	55,225	276	139,949	140,225
—	—	—	(263)	—	(263)
273	54,952	55,225	13	139,949	139,962
0.32p	64.20p	64.52p	0.32p	161.39p	161.71p
0.32p			0.32p		
—			0.30p		

**SUMMARISED BALANCE SHEET**

(Unaudited)

	30 June 2004 £'000	30 June 2003 £'000	31 December 2003 £'000
Investments at market value	334,088	258,023	331,497
Net current assets	30,874	9,413	18,712
Total assets (before deduction of bank loans)	364,962	267,436	350,209
Bank loans (note 4)	(26,110)	(31,289)	(29,325)
<b>Total net assets</b>	<b>338,852</b>	<b>236,147</b>	<b>320,884</b>
<b>Capital and reserves</b>			
Called-up share capital	21,952	21,952	21,952
Share premium	73,738	73,738	73,738
Capital reserve - realised	195,895	178,134	182,463
Capital reserve - unrealised	45,127	(39,998)	40,670
Revenue reserve	2,140	2,321	2,061
<b>Equity shareholder's funds</b>	<b>338,852</b>	<b>236,147</b>	<b>320,884</b>
<b>Net Asset Value per Ordinary share</b>	<b>385.90p</b>	<b>268.94p</b>	<b>365.44p</b>
<b>Ordinary shares in issue (note 5)</b>	<b>87,807,348</b>	<b>87,807,348</b>	<b>87,807,348</b>

## SUMMARISED CASH FLOW STATEMENT

(Unaudited)

	For six months ended 30 June 2004	For six months ended 30 June 2003	For year ended 31 December 2003
	£'000	£'000	£'000
<b>Net cash inflow from operating activities</b>	240	501	827
<b>Net cash outflow from servicing of finance</b>	(265)	(249)	(580)
<b>Financial investment</b>			
Purchase of investments	(39,020)	(37,145)	(77,543)
Sale of investments	52,993	23,880	74,274
Currency movement	23	—	100
<b>Net cash inflow/(outflow) from financial investment</b>	<b>13,996</b>	<b>(13,265)</b>	<b>(3,169)</b>
<b>Equity dividend paid</b>	<b>(263)</b>	<b>(718)</b>	<b>(718)</b>
<b>Net cash inflow/(outflow) before financing</b>	<b>13,708</b>	<b>(13,731)</b>	<b>(3,640)</b>
<b>Financing</b>			
Issue of Ordinary shares	—	3,332	3,332
Loans drawn down	—	10,000	37,902
Loans repaid	(2,849)	—	(27,718)
<b>Net cash (outflow)/inflow from financing</b>	<b>(2,849)</b>	<b>13,332</b>	<b>13,516</b>
<b>INCREASE/(DECREASE) IN CASH</b>	<b>10,859</b>	<b>(399)</b>	<b>9,876</b>
<b>RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET (DEBT)/FUNDS</b>			
Increase/(decrease) in cash in period	10,859	(399)	9,876
Decrease/(increase) in bank loans	2,849	(10,000)	(10,184)
Exchange movement on loans	366	1,021	3,169
<b>MOVEMENT IN NET (DEBT)/FUNDS IN PERIOD</b>	<b>14,074</b>	<b>(9,378)</b>	<b>2,861</b>
<b>NET DEBT AT 1 JANUARY</b>	<b>(10,686)</b>	<b>(13,547)</b>	<b>(13,547)</b>
<b>NET FUNDS/(DEBT) AT 30 JUNE/31 DECEMBER</b>	<b>3,388</b>	<b>(22,925)</b>	<b>(10,686)</b>

### NOTES

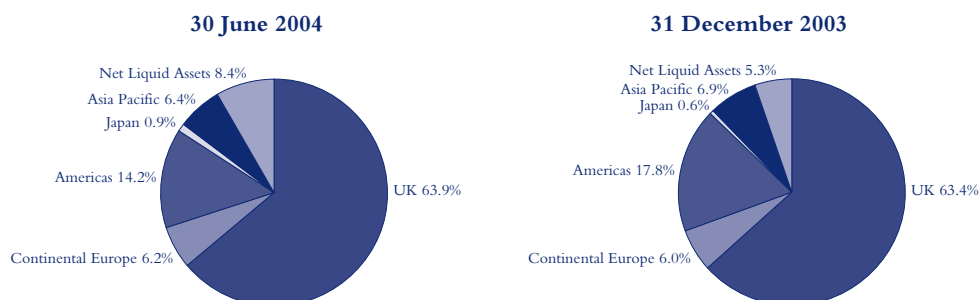
- 1 The Financial Statements for the six months to 30 June 2004 have been prepared on the basis of the accounting policies set out in the Company's Annual Financial Statements at 31 December 2003.  
The Interim Report was approved by the Board on 22 July 2004.  
None of the views expressed in this document should be construed as advice to buy or sell a particular investment.
- 2 No interim dividend will be declared.
- 3 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 2004 the weighted average number of Ordinary shares was 87,807,348 (30 June 2003 - 85,598,153 and 31 December 2003 - 86,711,829).  
There is no dilution effect on the return per ordinary share in the period to 30 June 2004 as all outstanding warrants had been exercised by 30 April 2003. For the periods to 30 June and 31 December 2003, the diluted return per Ordinary share was calculated using the weighted average number of warrants in issue during these periods adjusted by the difference between the average price of the Ordinary shares during the period, 30 June 2003 - 186.9p and 31 December 2003 - 244.3p, and the Subscription price of 100p to give a weighted average of 30 June 2003 - 86,625,581 and 31 December 2003 - 87,358,935 shares.
- 4 The Company has arranged multi-currency loan facilities with The Royal Bank of Scotland plc and ING Bank N.V. The facility with The Royal Bank of Scotland plc comprised a five year £3 million facility which expired on 7 January 2004. The ING Bank N.V. facility comprises a 364 day £30 million facility which expires on 26 October 2004. At 30 June 2004 there were outstanding drawings of US\$47.35 million (30 June 2003 - US\$47.038 million and ¥551.55 million and at 31 December 2003 - US\$47.35 million and ¥551.55 million).
- 5 At the AGM held on 14 April 2004 the Company's authority to buy back shares was renewed in respect of 13,162,321 Ordinary shares (equivalent to 14.99% of its issued share capital at that date). No shares have been bought back during the period and therefore at 30 June 2004 the Company's authority to buy back shares remains unchanged at 13,162,321.
- 6 The financial information for the year ended 31 December 2003 has been extracted from the full accounts which have been filed with the Registrar of Companies and which contain an unqualified Auditors' Report.

## TOP TWENTY EQUITY HOLDINGS

at 30 June 2004

Company	Business	Market value £'000	% of total assets
Amstrad	Consumer electronics designer and manufacturer	14,250	3.9
Northgate Information Solutions	Application software products and services	12,610	3.5
Imagination Technologies	Licenser of semiconductor intellectual property	10,684	2.9
Plasmon	Optical data storage	7,437	2.0
Gresham Computing	Software for real time banking transactions	6,401	1.8
SDL	Multilingual website globalisation	6,100	1.7
SurfControl	Web and e-mail filtering software	5,948	1.6
ACAL	Electronics product distribution	5,093	1.4
Diploma	Distributor	5,054	1.4
Detica	IT services business focused on security and CRM	5,053	1.4
Incisive Media	Magazine publisher	5,014	1.4
Alphameric	Retail and bookmaking software	4,718	1.3
Taylor Nelson Sofres	Market research	4,610	1.3
Marlborough Stirling	Financial software and outsourcing	4,540	1.2
Biotrace International	Rapid hygiene and biological testing	4,375	1.2
Linx Printing Technologies	Manufacturer of continuous inkjet printers	4,286	1.2
Euromoney Institutional Investor	Magazine publisher	4,246	1.2
Alba	Consumer electronics manufacturer and retailer	3,957	1.1
THUS Group	Telecom service provider	3,900	1.1
Microgen	IT services and data management	3,744	1.0
		122,020	33.6

## GEOGRAPHIC SPREAD OF INVESTMENTS



## **DIRECTORS, MANAGER AND ADVISERS**

### **DIRECTORS**

M Boase (Chairman)  
C M Brendish CBE  
J P Dukes  
D C P McDougall OBE  
C A Parritt

### **SECRETARY**

Baillie Gifford & Co.  
Calton Square  
1 Greenside Row  
Edinburgh EH1 3AN  
Tel: 0131 275 2000

### **REGISTERED OFFICE**

12 Charterhouse Square  
London EC1M 6AX

### **COMPANY NUMBER**

2879728 (England and Wales)

### **INVESTMENT MANAGER**

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

### **SOLICITORS**

Macfarlanes  
10 Norwich Street  
London EC4A 1BD

### **AUDITORS**

Ernst & Young LLP  
Ten George Street  
Edinburgh EH2 2DZ

### **BANKERS**

The Bank of New York  
One Canada Square  
London E14 5AL

### **STOCKBROKER**

Cazenove & Co. Ltd  
12 Tokenhouse Yard  
London EC2R 7AN

### **REGISTRARS**

Capita Registrars  
Northern House  
Woodsome Park  
Fenay Bridge  
Huddersfield HD8 0LA  
Tel: 0870 162 3131  
Website: [www.capitaregistrars.com](http://www.capitaregistrars.com)  
E-mail: [shareholder.services@capitaregistrars.com](mailto:shareholder.services@capitaregistrars.com)