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2003

Report & Accounts
to 31 July 2003

Framlington Second Dual Trust PLC



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Introduction

Framlington Second Dual Trust PLC is an investment trust company registered in England and Wales, registered number 3739055.

Objective

The objective of the Trust is to pay the zero dividend preference shareholders 158.6874p per share on 4 August 2005 and to maximise the income and capital entitlement of the ordinary income shareholders by selecting a portfolio of mainly UK listed equities, equity related securities and fixed interest securities.

Capital structure

The Trust has two classes of share capital: ordinary income shares and zero dividend preference shares. The different proportion of each class of share gives the Trust inherent gearing. It also has borrowings in the form of a bank loan which has a face value of £21.5million. The zero dividend preference shares are repayable on 4 August 2005.

Further details of the effects of the Trust's structure and gearing are given on page 12.

Management company

The Trust is managed by Framlington Investment Management Limited, a wholly owned subsidiary of Framlington Group Limited. Framlington Group Limited is ultimately owned by HSBC Holdings plc (51%) and by Munder Capital Management (49%), a US fund management company. As at 31 July 2003, Framlington and its subsidiaries had approximately £2.8billion of assets under management. Details of the management fee arrangements are given on page 14 in the report of the directors.

ISA

As at 31 July 2003 all of the Trust's securities qualified for inclusion in ISAs. The subscription limit for maxi ISAs for 2003/2004 is £7,000.

Year's summary

Framlington Second Dual Trust portfolio relative to FTSE All-Share Index from launch (4/8/99) to 31/7/03

(source: Framlington/FactSet)

Financial highlights

	2003 p	2002 p
Net asset value per*		
Ordinary income share	-	-
Zero dividend preference share	117.39	109.24
Earnings per ordinary income share	3.82	7.25
Dividends	4.00	6.40

* See note 26 on page 35

Total assets

	2003 £000s	2002 £000s
Shareholders' funds	32,365	33,799
Market capitalisation	26,856	22,075

Chairman's statement

The Hon. Nicholas Soames, MP
Chairman

The past year has been another difficult period for investors globally. Volatility has been a feature of all stockmarkets with geo-political events being a contributory factor and investor confidence, already fragile, has had to weather the climate of economic and political uncertainty experienced in the build up to the Iraq conflict. The fall in the UK stockmarket in March 2003, which culminated in an 8 year low being reached, was accompanied by near panic selling, and the level of volatility in 2002 was the highest in 15 years.

There were, of course, other reasons for the market's performance up to March 2003. A number of corporate scandals in the US, investment banking problems, bankruptcies and problems with accounting policies amongst US corporations all served to undermine market confidence.

The sharp rally in share prices that followed the sell off in March has led many commentators to believe that the bear market in the UK may finally have come to an end. Certainly the improvement in the Trust's fortunes since 12 March has been very significant. Not only has the UK market enjoyed a healthy recovery but the smaller and mid cap stocks which make up most of our portfolio have been particularly sought after.

The recovery in the latter months of the Trust's financial year helped the All-Share index to show a total return of 3.4% for the period; with

the FTSE 350 high yield index also achieving a positive return of 2.5%. However, returns from smaller companies were significantly better with a return of 14.2% whilst the mid cap index returned 16.4%. The Trust's equity portfolio returned 18.8% for the financial year whilst the Trust's overall portfolio produced a total return of 10.2%; the difference being explained by the Trust's investment in other asset classes. The net asset value of the zero dividend preference shares rose by 7.5% during the period from 109.2p to 117.4p, still below the zero dividend preference shareholders' final entitlement of 158.69p per share.

The board and the manager have sought to enhance the asset value of the Trust whenever possible. They are agreed that the best way to achieve this is through the continuation of the policy of buying back zero dividend preference shares, that has been in operation for more than two years. In the year to 31 July 2003 the Trust has repurchased 3.4million of its shares at a total cost of £2.1million. These purchases have brought the total number of shares repurchased to 6.9million at a cost of £4.8million. In aggregate, the purchases of zero dividend preference shares, since the commencement of the Trust's repurchase programme, have benefited the net asset value per zero dividend preference share by 8.8%.

Whilst the renewed interest in the

Chairman's statement continued

zero dividend preference share market has made it more difficult to find sellers of these shares it is the board's intention that the company should continue to buyback shares. Accordingly at the annual general meeting of the company to be held on 25 November 2003 shareholders will be asked to renew their authority to continue the buy back. These purchases remain a useful way to improve the net asset value of the Trust and also improve liquidity in the market for those zero dividend preference shareholders who wish to sell.

In my previous reports to shareholders I have mentioned the reduction in income accruing from the Trust's split capital investment trust shareholdings and the impact this has had on the Trust's total earnings. This resulted in the board deciding to reduce the final dividend for 2002 to 1pence per share and to continue to pay quarterly dividends at that level throughout 2002/2003. In discharging their responsibilities the directors have regard to their responsibility for continuing to balance the interests of both sets of shareholders.

The proportion of the company's portfolio invested in the split capital investment company sector continued to fall over the past year. This was due to a combination of share price declines and the sale of some of our holdings. As at 31 July 2003 the company had £2.5million (4.6% of gross assets) invested in the sector compared with

£5.5million (9.9%) at 31 July 2002.

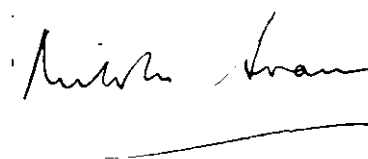
In my interim statement I referred to the resignation of Terry Hitchcock and the decision of the board not to seek a replacement for him. Craig Walton has today also resigned as a director as he has left the management company. The board is most appreciative of the contributions from both Mr Hitchcock and Mr Walton during their tenure as directors of the Trust.

As the Trust still has 2 years of its life to run the directors have decided to appoint a new non-executive independent director. The board is pleased to welcome to the board Arthur Copple who was appointed as a director today. Mr Copple is well known at a senior level within the investment trust industry and the board are confident that he will make a valuable contribution to the running of the Trust.

I have made reference earlier to the declines in market values that took place in the first eight months of the past year. During this period the Trust entered discussions with its bankers, Bank of Scotland, who agreed to a temporary "cash offset" arrangement, whereby cash balances could be netted off against the bank loan for the purposes of the calculation of the banking covenant ratios. At this time the board considered the option of repaying a proportion of the bank loan but concluded that as the market was probably at or near its nadir this

would not prove to be in the interest of shareholders in the longer term. The directors are grateful to the Bank of Scotland for their understanding during this difficult period, and are pleased that the course of action undertaken has proved to be correct, at least in the short term. The investment managers, Framlington, agreed to deduct the amounts of money required for the cash offset arrangement from the gross assets of the Trust when calculating their investment management fee.

Investor confidence remains fragile, but it is now widely believed that the worst of the three year bear market is over. It is clearly difficult to foresee the likely future course of markets, but in contrast to previous prolonged bear markets, the UK economy has continued to produce economic growth, giving grounds for cautious optimism.



The Hon. Nicholas Soames, MP
Chairman

16 September 2003

Investment manager's report

Paul Branigan

Paul Branigan heads the investment management team for Framlington Second Dual Trust PLC.

Economic and Market Background

The past twelve months have witnessed some wild swings in the fortunes of UK equities. The first seven and half months of the Trust's year saw a continuation of the difficult stockmarket conditions that had existed since the time of the launch of the Trust. 2002 was the third consecutive year of negative returns on equities in the UK, Europe, US and Japan. The only UK equity sectors to avoid double digit falls between the end of July and the middle of March 2003 were the tobacco, water, telecom, mining, forestry & paper and household goods & textiles sectors. The better performance of these relatively defensive sectors was mirrored by a better performance from the relatively safe asset classes of cash, gold, bonds, and property.

The third quarter of 2002 was one of the worst quarters for equity investors since the Second World War. Fears of a conflict in the Middle East, a poor macro economic backdrop and disappointing corporate newsflow, all led to investors avoiding risk and therefore equities were heavily sold. This did, however, drive markets down too far globally and buyers returned to produce a fourth quarter of positive returns. During this period, equity markets experienced an unprecedented level of volatility. This was not helped by rumours that insurance companies were close to breaching their solvency levels and were being forced to sell into any short-term strength in the

equity market. One feature that remained consistent was the response of Central Banks to the weak and uncertain conditions. Interest rates stayed low and in the US and Europe half percent cuts were announced.

Corporate activity remained depressed in 2002. In the UK the most noteworthy transactions during the year were the successful bid by US cruise operator Carnival for P&O Princess Cruises, the formation of National Grid Transco from the merger of National Grid and Lattice and HSBC's purchase of Household. Meanwhile Corus and Shire both saw high profile deals fall apart, outcomes which were severely punished by shareholders.

Following a good quarter for equities at the end of 2002, markets returned to the downward trend experienced during the last three years in the first quarter of 2003. Investors continued to be very risk adverse, their reaction to weakening global economic conditions and the uncertainty being created by the conflict in Iraq. Weak economic indicators in stockmarkets, and in particular fears of a slowdown in consumer spending in the major economies, meant that Central Banks maintained their loose monetary policy. They continued to be more fearful of recession than inflation. The start of hostilities in Iraq was preceded by a reasonable rally in markets in the second week of March.

Subsequent to the onset of hostilities in Iraq equity markets have enjoyed

Investment manager's report continued

a very strong rebound, with the second quarter performance of UK equities being the best since 1999. Within this, the best returns were to be found in the mid and small cap indices, both of which rose by more than 25% in the second quarter. A resumption of corporate activity focused on the retail sector with bid approaches for Somerfield, Selfridges, and Debenhams. The total return from the UK equity market of just over 30% between 12th March and the end of the Trust's financial year was sufficient to more than recoup all of the losses that had been incurred in the year up to that point. It is encouraging against this background that the equity portfolio of the Trust produced a total return of some 18.8%, for the year as a whole.

Portfolio Review

Due to the uncertain market conditions and the need to place monies with Bank of Scotland to offset against the banking covenants, the Fund has run high levels of cash throughout the year. In part, the cash was raised as a result of corporate action in three of the stocks within the portfolio in the first half of the year. The contested bid for P&O Princess Cruises, though protracted, benefited performance, whilst the bids for Clydeport and T&S Stores also resulted in a cash inflow for the Fund. The decision that was taken to reinvest the monies from the T&S Stores bid into Safeway was soon rewarded with a flurry of bids for the food retailer. However, Government

intervention and the subsequent Monopolies Commission inquiry have left the situation unresolved.

The major holdings in the portfolio have remained broadly unchanged during the past twelve months. The core holdings of Anglo Irish Bank, Kelda Group, Vodafone, and T Clarke, remain. Crest Nicholson and First Group are still key holdings and further stock purchases of Northgate, Lloyds TSB Group and Headlam have increased their importance within the portfolio.

The search for value and yield in the small and mid cap market has met with reasonable success this year. Purchases of new holdings in such stocks as Senior, Pendragon, Malcolm Group, Chaplethorpe, and Anglo Pacific Group have all added to the portfolio returns. Not only has reasonable capital growth been seen since acquisition but the stocks have all added to the revenue account.

The rebalancing of the income portfolio has continued with further sales in the holdings of split capital investment trusts, and the purchase of more corporate bonds. The split capital sector has seen a significant improvement in its fortunes over the last few months, albeit from an extremely low base. By resisting the temptation to sell these holdings wholesale, some good gains have been achieved from the likes of Premier Pacific Income Fund, Acorn Income Fund and Real Estate Opportunities convertible loan stock. These holdings continue to be a

valuable contributor to the income account.

Economic Outlook

The general assumptions of economists and policy makers worldwide over the past few months have been that rising perceptions of geo-political risk, together with higher oil prices were the primary causes of the lack of economic recovery. These concerns intensified up to the start of the conflict in the Gulf and second quarter GDP numbers confirmed that demand growth has been much weaker than in previous recoveries.

The outcome of the conflict in the Gulf went as well as markets could have hoped for and there has been, to a larger extent, a reversal of the fears leading up to the start of the war. Indeed, it is now assumed that as the geo-political risk falls so will the risk aversion of investors and that economic activity will begin to pick up, partly encouraged by the fall in the oil price.

Nevertheless there are still fundamental problems existing within each individual economy. Consumer confidence and corporate spending is unlikely to pick up sharply and therefore we maintain the view that the major economies will continue with sub-trend growth (a fact of life since 2001) and that inflationary pressures will continue to be virtually non-existent.

Interest rate futures are not predicting any further cuts in the

US, Europe or the UK at the moment. There has been little change in policy from any of the Central Banks and therefore markets are taking a more optimistic view of the recovery going forwards. The fear remains that this optimism may be misplaced and that interest rate cuts are more likely than is currently expected.

In the short term, the Middle East will continue to be an issue, although hopefully one that is reducing in the minds of investors. The oil price will inevitably be a key issue and the reaction of OPEC to the price falls will need to be watched closely. As we go through the reporting season all eyes will be on corporate newsflow which so far appears to be reasonably good. However, earnings estimates for the second half of 2003 are optimistic in many areas and a reduction in expectations must take place. This is perhaps the single biggest risk to markets at the moment.

Market Outlook

Equity markets have begun to improve and most are above their levels at the beginning of 2003, having struggled badly until mid March. The aversion to risk, so prevalent ahead of the Iraq war, has fallen and this is benefiting the more cyclical areas of the economy. The FTSE 100 index, having broken back through the 4000 level appears to be consolidating after the useful gains of the past few weeks.

The valuation of the UK market does not look demanding and corporate activity is beginning to pick up. Whilst poor economic news may hold back certain stocks the expectations of analysts have begun to become more realistic and any clear signs of an economic recovery are likely to send the market higher. The rebuilding of corporate profitability should in turn lead to a resumption of capital investment.

The technical state of the market is encouraging with the sales of equities by pension funds and insurance companies abating. Many other investors who have built up cash are now adopting a less defensive mentality. Setbacks in the market are likely to be met with renewed buying interest and this should underpin markets at these levels.

Framlington Investment
Management Limited

Portfolio analysis

Portfolio breakdown by broad industrial sector

	2003		2002
	2003	2002	
	%	%	
Cyclical services	27.6	28.2	
Financials			
(inc Split Capital Funds)	21.6	27.2	
Non-convertible bonds	12.2	9.3	
Basic industries	12.1	15.9	
Utilities	8.9	8.8	
Non-cyclical			
consumer goods	7.7	3.7	
Cyclical consumer goods	5.1	1.0	
General industrials	3.3	1.1	
Non-cyclical services	1.1	2.9	
Resources	0.4	1.9	

Portfolio breakdown by market capitalisation

	2003		2002
	2003	2002	
	%	%	
FTSE 100	22.8	17.2	
FTSE 250	36.8	38.4	
FTSE SmallCap	15.7	13.0	
FTSE Fledgling	2.9	2.4	
AIM	0.2	0.2	
Miscellaneous equities	4.3	3.0	
Investment companies	5.1	14.8	
Bonds	12.2	11.0	

Valuation

at 31 July 2003

Stock		Holding	Market value £	Fixed assets %
Anglo Irish Bank Corp	€0.32	370,000	2,112,700	4.26
Clarke (T.)	Ord 10p	293,000	1,508,950	3.04
Kelda Group	Ord 15 5/9p	300,000	1,323,750	2.67
Northgate	Ord 5p	250,000	1,306,250	2.63
Vodafone Group	7.5% Nts 19/3/2004	1,190,000	1,217,906	2.45
Lloyds TSB Group	Ord 25p	250,000	1,207,500	2.43
Capital Shopping Centres	5.75% Bds 5/3/2009	1,250,000	1,201,563	2.42
HSBC Holdings	Ord US\$0.50	150,000	1,155,000	2.33
Crest Nicholson	Ord 10p	400,000	1,122,000	2.26
First Group	Ord 5p	400,000	1,096,000	2.21
Top ten holdings			13,251,619	26.70
Headlam Group	Ord 5p	350,000	1,078,000	2.17
Weir Group	Ord 12.5p	400,000	1,070,000	2.16
Gallaher Group	6.625% Bds 21/5/2009	1,000,000	1,068,000	2.15
Safeway	Ord 25p	400,000	1,053,000	2.12
Real Estate Opportunities	7.5% Cnv Uns Ln Stk £1	1,120,000	1,036,000	2.09
Intermediate Capital Group	Ord 20p	100,000	986,000	1.99
Findel	Ord 5p	300,000	883,500	1.78
Rank Group	Ord 10p	300,000	864,000	1.74
AWG	Ord 19 181/201p	160,800	863,496	1.74
P&O	Dfd £1	375,000	862,500	1.74
Top twenty holdings			23,016,115	46.38
Pendragon	Ord 25p	437,500	846,563	1.71
Viridian Group	Ord 25p	150,000	843,750	1.70
RPC Group	Ord 5p	400,000	810,000	1.63
HBOS	Ord 25p	103,182	799,661	1.61
Marshalls	Ord 25p	300,000	799,500	1.61
WH Smith	Ord 55 5/9p	200,000	798,000	1.61
Woolworths Group	8.75% Nts 15/11/2006	750,000	787,500	1.59
Menzies (John)	Ord 25p	240,000	768,000	1.55
Standard Chartered Bank	6.75% Subord Nts 27/4/2009	700,000	760,095	1.53
Scottish Power	Ord 50p	200,000	726,000	1.46
Top thirty holdings			30,955,184	62.38

Valuation continued

Stock		Holding	Market value £	Fixed assets %
Laing (John)	6.4%(Net) Cnv Cum Pref £1	700,000	721,000	1.45
Wolverhampton & Dudley	Ord 29.5p	100,000	711,000	1.43
Balfour Beatty	10.75p Cum Cnv Red Prf 1p	500,000	710,000	1.43
RMC Group	Ord 25p	130,000	706,550	1.42
GlaxoSmithKline	Ord 25p	59,176	705,378	1.42
D.F.S. Furniture Co	Ord 5p	175,000	704,375	1.42
Rexam	Ord 64 2/7p	168,500	694,220	1.40
Premier Farnell	89.2p Cum Cnv Red Prf	50,000	687,500	1.39
Boots Group	Ord 25p	100,000	661,500	1.33
HMV Group	Ord 1p	400,000	660,000	1.33
Top forty holdings			37,916,707	76.40
United Utilities	Ord £1	120,000	657,600	1.33
Heywood Williams Group	Ord 25p	500,000	642,500	1.30
Dairy Crest Group	Ord 25p	150,000	637,500	1.28
Speedy Hire	Ord 5p	175,000	634,375	1.28
Property Acquisition & Management	Ord 10p	1,400,000	623,000	1.26
Merrill Lynch FTSE 100 Stepped Growth & Income	Income 0.01p	645,000	620,813	1.25
Chapelthorpe	Ord 5p	5,000,000	600,000	1.21
Land Securities Group	Ord 10p	70,000	574,350	1.16
Scottish & Newcastle	Ord 20p	150,000	554,250	1.12
Novar	7.25p Cnv Cum Red Prf 16 2/3p	500,000	526,250	1.06
Top fifty holdings			43,987,345	88.65
Avis Europe	Ord 1p	500,000	500,000	1.01
Imperial Tobacco Group	Ord 10p	50,000	489,000	0.99
Senior	Ord 10p	1,250,000	450,000	0.91
McBride	Ord 10p	400,000	392,000	0.79
BT Group	Ord 5p	193,050	377,895	0.76
Premier Pacific Income Fund	Ord Npv	1,000,000	370,000	0.75
Friends Provident	Ord 10p	252,750	346,899	0.70
Acorn Income Fund	Ord 25p	350,000	322,000	0.65
Malcolm Group	Ord 25p	400,000	302,000	0.61
Hitachi Capital (UK)	Ord 25p	134,125	228,683	0.46
Top sixty holdings			47,765,822	96.28

Stock		Holding	Market value £	Fixed assets %
Anglo Pacific Group	Ord 2p	550,000	213,125	0.43
Murray Global Return Trust	Ord 25p	1,250,000	184,375	0.37
Telewest Communications	5.25% Snr Cnv Nts 2007	550,000	176,000	0.35
Blue Chip Value & Income	Ord 12.5p	1,779,592	160,163	0.32
Jupiter Enhanced Income Investment Trust	Income 25p	250,000	160,000	0.32
Jupiter Dividend & Growth Trust	Ord 10p	750,000	151,875	0.31
Henlys Group	Ord 25p	212,500	139,188	0.28
M&G Equity Investment Trust	Income 1p	550,000	137,500	0.28
Martin Currie Enhanced Income Trust	Ord 25p	300,000	111,750	0.23
JP Morgan Worldwide Income Investment Trust	Ord Income 25p	300,000	90,000	0.18
Top seventy holdings			49,289,798	99.35
Investors Capital Trust	Geared Uts(1 Inc & 1 Cap)	300,000	78,000	0.16
Springboard	Ord 10p	111,073	77,751	0.16
ACM European Enhanced Inc Fund	Ord Shs	120,000	70,800	0.14
BFS Asian Assets Trust	Geared Ord Uts(1 Inc & 1 Cap)	655,670	45,897	0.09
BFS Absolute Return	Income 0.1p	550,000	33,000	0.07
Blue Chip Value & Income Fund	Warrants 31/8/2011	195,918	5,388	0.01
Britannic UK Income Trust	Ord 1p	500,000	5,250	0.01
Framlington Global Financial & Income Fund	Ord 25p	750,000	3,788	0.01
American Investment Trust	Ord 1p	1,400,000	1,757	-
Carnival	Ord US\$1.66	1	20	-
Top eighty holdings			49,611,449	100.00
Other (4 stocks)			-	-
Total fixed asset investments			49,611,449	100.00

Structure and gearing

Zero dividend preference shareholders' funds
£32,365,000

Bank loan
£21,541,000

EQUITY	DEBT
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Ordinary income shares as at 31 July 2003

There were 51,697,859 ordinary income shares of 5p each in issue. Ordinary income shares are entitled to all the revenue profits of the Trust by way of a dividend and all the capital assets of the Trust after payment of all debts including the payment to holders of the zero dividend preference shares and the bank loan. The underlying value of assets attributable to the ordinary income shares is geared to the performance of the total assets relative to the rising capital entitlements of the zero dividend preference shares. Ordinary income shareholders will therefore benefit from any outperformance of the total assets relative to the rise in capital entitlements of the zero dividend preference shares, but conversely will suffer from any underperformance. Reference should be made to note 26 of the accounts (page 35).

Zero dividend preference shares as at 31 July 2003

There were 27,571,239 zero dividend preference shares of 5p each in issue. They carry no right to income but have a final entitlement of 158.6874p on 4 August 2005.

Units

A Unit consists of one ordinary income share and one zero dividend preference share. Units were issued under the Framlington Dual Trust PLC scheme of reconstruction. Units are separately quoted on the London Stock Exchange. Shareholders can instruct the registrar to combine a holding of equal numbers of zero dividend preference shares and ordinary income shares into units or to split a unit into its constituent parts.

Bank loan

The Trust has a £21,541,000 bank loan with Bank of Scotland which bears a fixed interest rate of 7.4641% per annum. The loan is due to be repaid on 4 August 2005.

Reconstruction and winding up

The directors are required to consider a scheme of reconstruction pursuant to section 425 of the Companies Act 1985 prior to the repayment date for the zero dividend preference shares - 4 August 2005. If the scheme cannot be implemented prior to this date and the Board is unable to propose some other reconstruction enabling the zero dividend preference shareholders to be repaid on 4 August 2005, then the directors will convene an extraordinary general meeting to wind up the Trust. Both classes of shareholder are entitled to vote at such a meeting. If a scheme of reconstruction is implemented and the zero dividend preference shareholders are repaid, the Trust will have an indefinite life. However, the Board intends to convene a meeting of the ordinary income shareholders prior to 4 August 2005 to consider the future direction of the Trust.

Directors

All the Directors of Framlington Second Dual Trust PLC are non-executive and, with the exception of Mr Walton, who resigned as a director on 16 September 2003, are independent of Framlington and are members of the management engagement and audit committees.

All of the directors were appointed on 4 June 1999, except for Mr Copple who was appointed on 16 September 2003.

The Hon. Nicholas Soames, MP
(Chairman of the Board)

Aged 55.

Nicholas Soames has been a Member of Parliament since 1983. He is the Chairman of the Property Merchant Group Limited, a director of Wiltens (St James's) Limited and a senior vice president of the MMC Group.

Mr Jonathan Carr
(Chairman of the
Audit Committee)

Aged 64.

Jonathan Carr worked in the City of London from 1962 to 1997. He was a director of the investment trust team of Warburg Dillon Read until 1997 when he retired. He is Chairman of Govett Enhanced Income Investment Trust PLC and Royal London UK Equity & Income Trust PLC as well as Talisman First Venture Capital Trust PLC and Galaxy Asset Management Limited. He is also a non-executive director of BFS Income & Growth Trust PLC.

Mr Richard Granville

Aged 65.

Richard Granville worked for Hoare Govett from 1959 to 1986, during which time he became a partner and latterly a director and had responsibility for their investment trust division. He was a member of the Stock Exchange Council from 1981 to 1984 and deputy chairman of Neilson Cobbold from 1988 to 1992. He is a non-executive director of two other investment trust companies, Pennine AIM VCT II PLC and Framlington Income & Capital Trust PLC.

Mr Arthur Copple

Aged 48.

Arthur Copple has more than 25 years experience of working in the world of investment, the majority of it spent specialising in investment trusts. He was a main board director of Smith New Court and, from October 1995 to March 2002, he was a managing director at Merrill Lynch where initially he headed up their Funds Team and latterly directed their Pan European Small and Midcap Service. Presently he acts as a consultant to a number of financial services companies.

Report of the directors

The directors submit their report with the accounts of the Trust for the year to 31 July 2003.

Principal activities

The Trust has directed its affairs so as to enable it to seek approval from the Inland Revenue as an Investment Trust under S.842 of the Income & Corporation Taxes Act 1988. The Trust will be exempt from tax on capital gains on disposal of its investments for each accounting period for which approval is obtained. Investment Trust status is expected to be granted for the accounting year now under review. The Trust is not a close company. The Trust is an investment company within the meaning of Part VIII of the Companies Act 1985

Investment policy

The investment policy of the Trust is set out on page 1 and a general review of the business, together with its prospects are in the Chairman's Statement on pages 3 and 4 and the Investment Manager's Report on pages 5 to 7.

Dividends and retentions

	£000s	£000s
Net revenue from ordinary activities after taxation		1,974
Dividends per ordinary income share		
Paid January: first interim 1.0p	517	
Paid April: second interim 1.0p	517	
Paid July: third interim 1.0p	517	
Payable October: fourth interim 1.0p	517	
		2,068
Net deficit for the year		(94)
Revenue reserve brought forward		650
Revenue reserve carried forward		556

Board of directors

Information on current directors is given on page 13 and the structure of the Board and its committees are set out under the Corporate Governance section of this report.

Management arrangements

Under a management agreement dated 14 June 1999, Framlington Investment Management Limited ("FIM") was appointed as investment manager to manage and advise the Trust including the provision of accounting, secretarial, office and administrative services. The manager is paid a quarterly investment management and administration fee (exclusive of VAT) of 0.2375% of the Trust's gross assets (less any cash deposited under the 'cash offset' arrangement with Bank of Scotland) measured at the end of the relevant quarter. The management fees were allocated 63% to capital and 37% to revenue until 23 April 2002, when the allocation was changed so that management fees are now allocated equally between capital and revenue reserves. The management agreement is terminable on one year's notice. There are provisions for summary termination in certain circumstances including a change of control of the manager.

Craig Walton, who resigned as a director of the Trust on 16 September 2003, was whilst a director of the Trust and throughout the year to 31 July 2003, a director of FIM and an executive director of Framlington Group Limited, the immediate parent company of FIM.

Contracts of significance

Other than the management agreement referred to above, no agreement in which any director of the Trust was materially interested and which was significant in relation to the Trust's business subsisted during the financial year.

Substantial interests

The following holders of ordinary income shares had notifications of their substantial interests, submitted to the Trust in accordance with the Companies Act 1985, outstanding as at 16 September 2003.

Shareholder	Number of shares	% held
Apollo Fund PLC <i>(managed by Hamilton Lunn Asset Management)</i>	5,000,000	9.67
The Carrousel Fund Ltd	5,000,000	9.67
Gartmore Shared Equity Trust PLC	4,900,000	9.48
Aegon UK Plc	3,000,000	5.80
The Investment Trust of Investment Trusts PLC	2,014,000	3.90
Total	19,914,000	38.52

Directors' shareholdings

The interests of the directors, including their family interests, in the issued securities of the Trust were as shown below:

Beneficial interests

as at		31.07.03	31.07.02
The Hon. N Soames	Ord. Inc.	1,800	1,800
	Zero	1,500	1,500
Jonathan Carr	Ord. Inc.	5,000	5,000
	Zero	5,000	5,000
Craig Walton*	Ord. Inc.	2,979	2,979
	Zero	2,979	2,979

* Mr Walton resigned as a director of the Trust on 16 September 2003.

Mr Granville did not hold any interest in the share capital of the Trust at any time during the year under review.

The interests shown above were unchanged at the date of this report.

Individual Savings Accounts ("ISAs")

As at 31 July 2003 the shares of the Trust qualified for inclusion in ISAs.

Savings scheme

Framlington operates an investment trust savings scheme to allow low cost dealings in the Trust's shares. Further information is given on page 40.

CREST

The Trust's share capital is entered into the CREST system of computerised settlement and therefore the holders of the Trust's shares have the choice of maintaining their interests in either electronic or certificated form.

Creditor Payment Policy

It is the policy of the Trust to settle all investment transactions in accordance with the terms and conditions of the relevant markets in which it operates. All other expenses are paid on a timely basis in the ordinary course of business.

Directors' authority to repurchase shares

At the class meeting of zero dividend preference shareholders and the annual general meeting of the Trust, both held on 26 November 2002, shareholders authorised the repurchase of up to 7,749,509 ordinary income shares and 4,614,107 zero dividend preference shares for cancellation. Up to the date of this report, 2,980,780 zero dividend preference shares had been repurchased leaving shareholders' authority for the repurchase of 1,633,327 zero dividend preference shares still valid. No ordinary income shares had been repurchased by the date of this report, leaving the full authority to repurchase 7,749,509 ordinary shares valid.

The Board considers it to be in the best interests of the Trust to renew the authorities and retain flexibility to buy back both ordinary income shares and zero dividend preference shares. The aim of such repurchases would be to increase the net asset value of the ordinary income shares and the cover per zero dividend preference share and to provide an additional source of demand for the shares in the market. Any purchases will be made at the discretion of the Board in the light of prevailing market conditions and within guidelines set from time to time by the Board. Purchases will only be made through the market at prices below the prevailing

Report of the directors continued

net asset value per ordinary income share and zero dividend preference share. Accordingly, resolutions will be proposed at the forthcoming class meeting of zero dividend preference shareholders and the annual general meeting to grant the Trust authority to purchase and cancel up to 7,749,509 ordinary income shares and 8,163,677 zero dividend preference shares, being 14.99% of the ordinary income shares in issue and approximately 30% of zero dividend preference shares in issue.

Auditors

The business of the Trust's former auditors, Deloitte & Touche, was transferred to Deloitte & Touche LLP on 1 August 2003. At the board meeting of the Trust held on 16 September 2003, the board resolved in favour of the transfer of the audit engagement from Deloitte & Touche to Deloitte & Touche LLP. Accordingly, a resolution to re-appoint Deloitte & Touche LLP, Chartered Accountants, as auditors of the Trust will be proposed at the forthcoming annual general meeting.

Corporate governance

Introduction

The directors support The Combined Code (the "Code") issued by the UK Listing Authority, which sets out principles of good governance and a code of best practice. The Board considers that the Trust has complied with Section 1 of the Code (as issued by the Hampel Committee on Corporate Governance in June 1998 and prior to its reissue in July 2003 as a result of the Higgs Review) throughout the accounting year to 31 July 2003 except where otherwise disclosed in the explanation below as to how the Trust has applied the principles of good governance and adopted the code of best practice.

The Board

The Trust currently has four non-executive directors. Information on each of them is set out on page 13 and demonstrates a breadth of investment and commercial experience. The Board normally meets four times a year. In between meetings there is regular contact with the investment manager. Matters specifically reserved for decision by the Board have

been defined and a procedure adopted for directors, in the furtherance of their duties, to take independent professional advice at the expense of the Trust. All the directors have access to the advice and services of the corporate secretary (FIM) through its appointed representative who is responsible to the Board for ensuring that Board procedures are followed and that applicable rules and regulations are complied with.

Each director seeks to bring an independent judgement when considering issues of the Trust's strategy, performance and resources and when considering the appointment of directors and standards of conduct generally.

Owing to the level of experience that would be sought from any new director joining the Board it is unlikely that he would require training on the role of a listed company director. However, any new director appointed will be provided with appropriate information and a suitable induction process would be undertaken.

As the Trust is an investment trust company, the Board does not consider it necessary to identify a senior independent non-executive director to whom concerns can be conveyed, as all of the directors are non-executive and have sufficient expertise to address any concerns conveyed to them.

Board balance

The Board has considered the independence of each of the four non-executive directors and regard each of these as being independent from the investment manager. Mr Craig Walton, who resigned as a director on 16 September 2003, was regarded by the Board as not being independent from the investment manager.

Supply of information

Regular reports are provided by FIM to the directors, keeping them fully informed of investment and financial controls, and other matters that are relevant to the business of the Trust and that should be brought to the attention of the directors. Each of the directors also has direct access to FIM representatives when they wish to make any further enquiries.

Appointments to the Board

The Board does not intend to appoint a nomination committee as, given its size, this function is better performed by the full Board of directors.

Re-election

The Code requires each director to put himself up for re-election at least once every three years. The articles of association satisfy this provision of the Code as the Trust complies with the Code in ensuring that directors put themselves up for re-election at least once every 3 years. The Board therefore does not regard it as necessary for limits to be put on directors' terms of appointment.

In accordance with the articles, Nicholas Soames and Jonathan Carr retire at this year's annual general meeting ("AGM") and being eligible, offer themselves for re-election. Mr Arthur Copple, having been appointed to the Board since the last AGM, will put himself up for election at the AGM.

Management engagement committee

The Trust is not required by the Listing Rules to comply with the Code in relation to directors' remuneration, because there are no executive directors. Consequently, a remuneration committee has not been established. Instead, in accordance with the AITC recommendation, a management engagement committee, consisting of all the independent directors, with defined terms of reference and duties, has been established to review annually the terms of the agreement with the investment manager. Mr Carr is the Chairman of this committee.

Relations with shareholders

The Board recognises the importance of maintaining good relations with all the Trust's shareholders. The investment manager meets with institutional shareholders on a regular basis and reports back to the Board on these meetings. In addition, the Trust's AGM presents the directors with an opportunity to meet and hear the views of shareholders.

The chairmen of the Board, audit committee and management engagement committee are available

at the AGM to answer any questions. At every AGM, each substantial separate issue is dealt with in a separate resolution and where a vote is decided on a show of hands, the Chairman will subsequently report on the number of proxy votes lodged.

Relations with portfolio companies

Generally, the Trust seeks to comply with Section 2 of the Code relating to institutional shareholders. Specifically, the powers to exercise the Trust's voting rights in respect of companies in the portfolio are delegated to the investment manager, who makes considered use of these voting powers. The primary aim of the use of voting rights is to ensure a satisfactory financial return from investments. In the event that the Trust has a controlling share of the votes, the investment manager will refer back to the Chairman before exercising these votes.

Audit committee

The Board has appointed an audit committee with defined terms of reference and duties. All the independent directors are members of the committee, which is chaired by Mr Carr. The duties of the committee are to review the Trust's internal controls, the annual report and accounts and interim report, the auditors' remuneration and engagement, as well as the auditors' independence and the non-audit services provided by them, if any.

Internal control

The directors are ultimately responsible for the Trust's system of internal control and for reviewing its effectiveness. The Code requires directors to conduct at least annually a review of the Trust's system of internal control, covering all controls, including financial, operational and compliance controls and risk management. The directors have reviewed the need for an internal audit function and as an investment trust do not regard it as necessary.

It is important to recognise that a system of internal control can provide only a reasonable, and not an absolute, assurance against material misstatement or loss.

Report of the directors continued

As mentioned earlier in this report, FIM was appointed to manage and advise on the Trust's assets and provide accounting, secretarial, office and administrative services to it. FIM is authorised and regulated by the Financial Services Authority in the conduct of its investment business. FIM's systems of internal control include organisational arrangements with clearly defined lines of responsibility and delegated authority, as well as control procedures and systems which are regularly evaluated and internally monitored.

It is the duty of the audit committee to examine the internal controls on which the Trust is reliant. The audit committee reviews the effectiveness of internal controls semi-annually and reports its findings to the Board. At the request of the audit committee, an annual report is presented on all areas of FIM's internal controls, together with updates relating to the affairs of the Trust during the accounting period. In addition to this, the audit committee also receives FRAG 21 statements on internal controls from HSBC Bank plc, the Trust's custodian bank and Capita Registrars, the Trust's registrars.


Financial reporting - Statement of directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Trust as at the end of the financial year and of the revenue of the Trust for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgements and estimates that 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 a going concern basis unless it is inappropriate to presume that the Trust 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 Trust, enabling them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Trust and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Bearing in mind that the assets of the Trust consist mainly of marketable securities, the directors are of the opinion that, at the time of approving the financial statements, the Trust has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

 *(for Framlington Investment Management Limited)*
By order of the Board

Framlington Investment
Management Limited, Secretary
155 Bishopsgate
London EC2M 3XJ

16 September 2003

Independent auditors' report

We have audited the financial statements of Framlington Second Dual Trust PLC for the year ended 31 July 2003 which comprise the statement of total return, the balance sheet, the reconciliation of movements in shareholders' funds, the cash flow statement, the accounting policies and the related notes 1 to 26. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the part of the directors' remuneration report that is described as having been audited.

This report is made solely to the Trust's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Trust's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Trust and the Trust's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As described in the statement of directors' responsibilities, the Trust's directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards. They are also responsible for the preparation of the other information contained in the annual report including the directors' remuneration report. Our responsibility is to audit the financial statements and the part of the directors' remuneration report described as having been audited in accordance with relevant United Kingdom legal and regulatory requirements and auditing standards.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the directors' remuneration report described as having been audited have been 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 Trust 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 regarding directors' remuneration and transactions with the Trust is not disclosed.

We review whether the corporate governance statement reflects the Trust's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules of the Financial Services Authority, 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 Trust's corporate governance procedures or its risk and control procedures.

We read the directors' report and the other information contained in the annual report for the above year as described in the contents section including the unaudited part of the directors' remuneration report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

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 and the part of the directors' remuneration report described as having been audited. 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 circumstances of the Trust, 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

Independent auditors' report continued

the financial statements and the part of the directors' remuneration report described as having been audited 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 and the part of the directors' remuneration report described as having been audited.

Opinion

In our opinion:

- the financial statements give a true and fair view of the state of affairs of the Trust as at 31 July 2003 and of its total return for the year then ended; and
- the financial statements and part of the directors' remuneration report described as having been audited have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche LLP *Deloitte & Touche LLP*

Deloitte & Touche LLP

Chartered Accountants and Registered Auditors,
London

16 September 2003

Directors' remuneration report

The board of directors of Framlington Second Dual Trust PLC presents its directors' remuneration report in respect of the year ended 31 July 2003.

Remuneration policy

The remuneration policy of the Trust is set by the board of directors, subject to the limit of permissible aggregate remuneration paid in any year to all directors, set by the shareholders.

The remuneration policy of the Trust is to pay its non-executive directors fees that are appropriate for the amount of time spent in discharging their duties, that are broadly in line with those of comparable investment trusts and that are sufficient to attract and retain suitably qualified and experienced individuals. The Chairman is entitled to receive fees at a higher rate than those of the other directors, reflecting his additional duties and responsibilities. The directors' fees are not subject to any performance criteria.

As all directors of the Trust are non-executive and there are no employees, the Trust does not operate any share option or other long-term incentive schemes. In addition, the Trust has not entered into any service contracts with its directors and does not intend to in the future. Therefore, there are no notice

periods or termination provisions that would be operated in the event of the resignation of any director. No pension or other retirement benefits schemes are operated by the Trust for any of its directors.

Trust performance

A graph showing the total shareholder return since launch on 4 August 1999 to 31 July 2003 of the Trust's ordinary income shares against the FTSE All Share Index is shown below.

The directors believe that the FTSE All Share Index is the most appropriate measure of the Trust's performance.

Directors' emoluments

The Trust's articles of association provide that the aggregate annual remuneration of the directors shall not exceed £100,000 but revised limits may be determined from time to time by ordinary resolution of the shareholders in general meeting. The limits exclude any amounts payable in accordance with the articles for extra or special services over the usual non-executive directors' duties. There were no such payments for extra or special services in the year ended 31 July 2003.

Framlington Second Dual Trust PLC - relative performance of ordinary income share price against FTSE All Share, rebased from 4 August 1999

(source: Framlington/FactSet)

Directors' remuneration report continued

The following information is audited:

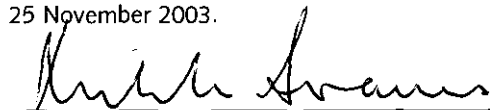
Total fees paid by the Trust in respect of each of the directors' service in the year ended 31 July 2003 were as follows:

The Hon. Nicholas Soames, MP	£15,000
J D Carr	£10,000
R Granville	£10,000
C A Walton*	Nil
T J Hitchcock (to Nov 2002)	£3,192
A T Copple	-

* Director's fee waived (non-independent director)

During the year, no salaries, bonuses, compensation or other payments for loss of office or other benefits were paid to any of the directors or former directors of the Trust. In addition, no reward was received by any director in a form other than cash. None of the directors received any expense reimbursements, either chargeable to UK income tax or in respect of qualifying services.

The approval of this report by the shareholders of the Trust is to be sought by ordinary resolution at the annual general meeting to be held on 25 November 2003.



By order of the Board

Nicholas Soames
Chairman

16 September 2003

*Nicholas Soames
to sign here*

Statement of total return

	Note	Year ended 31 July 2003			Year ended 31 July 2002		
		Revenue £000s	Capital £000s	Total £000s	Revenue £000s	Capital £000s	Total £000s
Realised losses	18	-	(12,095)	(12,095)	-	(8,630)	(8,630)
Unrealised gains/(losses)	17	-	13,906	13,906	-	(12,867)	(12,867)
Income	1/2	3,267	-	3,267	4,886	-	4,886
Investment management fee	3	(270)	(270)	(540)	(294)	(441)	(735)
Other expenses	4	(217)	-	(217)	(198)	-	(198)
Net return before finance costs and taxation		2,780	1,541	4,321	4,394	(21,938)	(17,544)
Interest payable and similar charges	5	(806)	(806)	(1,612)	(648)	(949)	(1,597)
Return on ordinary activities before taxation		1,974	735	2,709	3,746	(22,887)	(19,141)
Taxation on ordinary activities	6	-	-	-	-	-	-
Return on ordinary activities after taxation for the financial year		1,974	735	2,709	3,746	(22,887)	(19,141)
Increase in provision for redemption of zero dividend preference shares	12	-	(2,308)	(2,308)	-	(2,709)	(2,709)
Dividends in respect of ordinary income shares	7(a)	(2,068)	-	(2,068)	(3,310)	-	(3,310)
Transfer (from)/to reserves		(94)	(1,573)	(1,667)	436	(25,596)	(25,160)
Return per ordinary income share	7(b)	3.82p	(3.04p)	0.78p	7.25p	(49.51p)	(42.26p)

The Revenue column of this statement is the profit and loss account of the Trust. All revenue and capital items in this statement derive from continuing operations. No operations were acquired or discontinued in the year.

Balance sheet

as at 31 July

Nicholas Soames

Approved by the board of directors
and signed on their behalf by:

Nicholas Soames

Jonathan Carr

16 September 2003

Jonathan Carr

	Note	2003 £000s	2002 £000s
Fixed asset investments	9		
Listed - Full listing		49,533	49,131
- AIM listing		78	105
		49,611	49,236
Current assets			
Debtors	10	523	1,883
Cash at bank		4,809	5,265
		5,332	7,148
Creditors: amounts falling due within one year			
Creditors	11	520	527
Dividends payable		517	517
		1,037	1,044
Net current assets		4,295	6,104
Total assets less current liabilities		53,906	55,340
Creditors: amounts falling due after more than one year			
Bank loan	11(a)	(21,541)	(21,541)
Net assets		32,365	33,799
Share capital and reserves			
Called up share capital	14(b)	3,963	4,132
Capital reserves			
Share premium account	15	18,086	18,086
Distributable capital reserve	16	55,547	57,622
Capital reserve - unrealised	17	(9,399)	(23,305)
Capital reserve - realised	18	(48,229)	(32,750)
Capital redemption reserve	19	345	176
Redemption reserve for zero dividend preference shares	20	<u>11,496</u>	<u>9,188</u>
		27,846	29,017
Revenue reserve	21	556	650
Shareholders' funds		32,365	33,799
Equity shareholders' funds		-	-
Non-equity shareholders' funds		32,365	33,799
		32,365	33,799
Net asset value per share	26		
Ordinary income shares		-	-
Zero dividend preference shares		117.39p	109.24p

Jonathan Carr

Reconciliation of movements in shareholders' funds

	Year ended 31 July 2003		Year ended 31 July 2002	
	£000s	£000s	£000s	£000s
Net revenue after taxation	1,974		3,746	
Dividends in respect of ordinary income shares	(2,068)		(3,310)	
Net (deficit)/surplus transferred (from)/to reserves	(94)		436	
Other recognised losses	(1,573)		(25,596)	
Transfer to redemption reserve				
for zero dividend preference shares	2,308		2,709	
Repurchase of zero dividend preference shares	(2,075)		(2,741)	
Net reduction to shareholders' funds		(1,434)		(25,192)
Opening shareholders' funds		33,799		58,991
Closing shareholders' funds		32,365		33,799

Cash flow statement

	Note	Year ended 31 July 2003 £000s	Year ended 31 July 2002 £000s
Operating activities			
Investment income received		3,024	4,844
Interest received		221	60
Underwriting commission		-	3
Investment management fee charged to income		(255)	(296)
Fees and expenses paid to and on behalf of directors		(41)	(48)
Other cash payments		(159)	(163)
Net cash inflow from operating activities	23	2,790	4,400
Servicing of finance			
Interest paid		(1,613)	(1,579)
Taxation			
Taxation recovered		177	-
Capital expenditure and financial investment			
Net sales	24	2,628	9,431
Investment management fee charged to capital	24	(295)	(504)
Dividends			
Dividends paid		(2,068)	(4,188)
Net cash inflow before financing		1,619	7,560
Financing			
Repurchase of zero dividend preference shares		(2,075)	(2,741)
Net cash outflow from financing		(2,075)	(2,741)
(Decrease)/increase in cash	25	(456)	4,819

Accounting policies

A summary of the principal accounting policies, all of which have been applied consistently throughout the year, is set out below:

Accounting convention

The financial statements are prepared under the historical cost convention as modified by the revaluation of investments. The accounts have been prepared in accordance with applicable accounting standards and with the Statement of Recommended Practice "Financial Statements of Investment Trust Companies".

Fixed asset investments

Listed investments are valued at mid-market value and unlisted investments at directors' valuation. Dividend income from fixed asset investments is included on the date when the investment is first listed "ex-dividend". Interest on fixed interest securities is accrued on a daily basis.

Taxation

In accordance with Financial Reporting Standard 16 "Current Tax" UK dividends are shown net of attributable tax credits. Overseas dividends and other income that is subject to withholding tax are shown gross.

Revenue and capital reserves

Capital gains and losses arising from the sale and revaluation of investments are dealt with through capital reserves. Investment management fees and administration fees are calculated on the basis set out in the Report of the Directors on page 14. Until 23 April 2002, 63% of management fees and finance costs were charged to capital and 37% to revenue. This allocation was changed so that such fees and costs were split equally between capital and revenue thereafter, following a reassessment of the directors' expectation of the long-term split of returns in the form of capital growth and income. All other expenses are charged to revenue apart from investment transaction costs which are charged to capital reserves.

Notes to the financial statements

at 31 July

1 Income from fixed asset investments

	Franked*	Unfranked	Franked*	Unfranked
	2003	2003	2002	2002
	£000s	£000s	£000s	£000s
Income from investments was derived from:				
Dividends				
Listed investments - United Kingdom				
Full listing	2,259	355	3,375	817
Interest				
Listed investments - United Kingdom	-	421	-	635
	2,259	776	3,375	1,452

* UK dividend income is shown net of its attributable tax credits.

2 Other income

	2003	2002
	£000s	£000s
Deposit and other interest receivable	232	61
Underwriting commission	-	(2)
	232	59

3 Investment management fee

	2003	2002
	£000s	£000s
Management and administration fee	460	626
Irrecoverable VAT thereon	80	109
	540	735
Less amount charged to capital (note 18)	(270)	(441)
	270	294

The investment management fee charged to capital represents 63% of the charge until 23 April 2002 and 50% thereafter.

Details of the management and administration fees are set out in the Report of the Directors on page 14. Other than the disclosed transactions with the investment manager and the information given in the directors' shareholdings section of the Report of the Directors, there are no material related party transactions.

4 Other expenses

	2003	2002
	£000s	£000s
General expenses (including irrecoverable VAT)	162	137
Directors' emoluments (note 8)	41	48
Auditors' remuneration (including irrecoverable VAT)	14	13
	217	198

5 Interest payable

	2003 £000s	2002 £000s
Interest on bank loan	1,612	1,597
Less amount charged to capital (note 18)	(806)	(949)
	806	648

Interest charged to capital represents 63% of the finance costs on the Trust's long-term debt until 23 April 2002 and 50% thereafter.

6 Tax on ordinary activities

a) Analysis of charge in the year

	2003 £000s	2002 £000s
Total current tax for the year (see note 6b)	-	-

b) Factors affecting the current tax charge for the year

The tax assessed for the year is lower than the standard rate of corporation tax in the UK for an investment company (30%) (2002:30%). The differences are explained below:

	2003 £000s	2002 £000s
Return on ordinary activities before taxation	1,974	3,746
Corporation tax at 30%	592	1,124
Effects of:		
Non taxable UK dividends	(678)	(1,013)
Overseas dividends	13	-
Expenses not deductible for tax purposes	10	-
Relief for expenses in capital	(323)	(417)
Stock dividends	(43)	-
Increase in management expenses	429	306
	(592)	(1,124)
Current tax charge for the year (6a)	-	-

Investment companies which have been approved by the Inland Revenue under s842 ICTA 1988 are exempt from tax on capital gains. It has been assumed that the s842 ICTA 1988 criteria will be met in the year and therefore, any capital return is not included in the above reconciliation.

c) Tax losses

The Trust has unrelieved excess tax losses of £5,254,000 (2002: £2,224,000). It is unlikely that the Trust will generate sufficient taxable profits in the future to utilise these losses and therefore no deferred tax asset has been recognised.

7 Dividends and earnings per share

	2003 p	2003 £000s	2002 p	2002 £000s
(a) Ordinary income Shares				
- first interim paid January	1.0	517	1.8	931
- second interim paid April	1.0	517	1.8	931
- third interim paid July	1.0	517	1.8	931
Fourth interim payable October	1.0	517	1.0	517
	4.0	2,068	6.4	3,310

(b) Return per ordinary income share is based on the net revenue after tax of £1,974,000 (2002: £3,746,000) and on 51,697,859 (2002: 51,697,859) ordinary income shares of 5p each in issue throughout the year.

Notes to the financial statements continued

8 Directors' emoluments

	2003 £	2002 £
The Hon. Nicholas Soames, MP	15,000	15,000
J D Carr	10,000	10,000
R Granville	10,000	10,000
T J Hitchcock*	3,192	10,000
C A Walton†	-	-
A T Copple**	-	-
	38,192	45,000
National Insurance	2,760	3,174
	40,952	48,174

* Mr Hitchcock resigned from the Board on 26 November 2002.

† Fees waived. Mr Walton resigned from the Board on 16 September 2003.

** Mr Copple was appointed as a director on 16 September 2003.

9 Fixed asset investments

	Investments £000s
(a) Summary	
Cost	
At 31 July 2002	72,541
Purchases at cost	19,315
Sales - proceeds	(20,751)
Sales - realised losses	(12,095)
Cost at 31 July 2003	59,010
Unrealised depreciation (note 17)	(9,399)
Valuation at 31 July 2003	49,611
Valuation at 31 July 2002	49,236

(b) The thirty largest investments as at 31 July 2003 with a total market value of £30,955,184 (2002: £29,010,504) are shown on page 9. These investments amounted to 62.38% (2002: 58.91%) of total fixed asset investments.

(c) As at 31 July 2003 the Trust had no interest in any company representing more than 3% of a class of equity share capital.

10 Debtors

	2003 £000s	2002 £000s
Amounts due from brokers	-	1,197
Accrued income and other debtors	512	489
Tax recoverable	11	197
	523	1,883

£Nil (2002: £Nil) of the tax recoverable is recoverable after more than one year.

11 Creditors

	2003 £000s	2002 £000s
Amounts falling due within one year		
Management fee accruals*	143	153
General accruals	377	374
	520	527
* Including irrecoverable VAT		
	2003 £000s	2002 £000s
Amounts falling due after more than one year		
Bank loan	21,541	21,541
Repayments due between 2 and 5 years	21,541	21,541

(a) Bank Loan

On 17 August 1999 a loan facility of £30m running from 24 August until 4 August 2005 was taken out with the Bank of Scotland. On 24 August 1999, £21.5m was drawn down under this facility. The facility carried a rate of interest of 7.0841% per annum and included covenants that the ratio of total borrowings to net asset value should not at any time be greater than 0.4:1 and that the ratio of UK quoted assets to borrowings due to Bank of Scotland not less than 3.5:1. From 3 October 2001 the terms of the loan facility were amended so that the ratio of total borrowings to the net asset value should not at any time be greater than 0.66:1 ("borrowing ratio") and the ratio of UK quoted assets to borrowings due to Bank of Scotland should not be less than 2.5:1 ("asset cover"). At the same time, the rate of interest changed to 7.4641% per annum.

On 30 July 2002, the terms were further amended, such that for the period to 31 July 2003 any cash held by the company could be offset against borrowings in calculating the borrowing ratio and added to quoted equities in assessing the asset cover. On 30 June 2003, this amendment was extended until 31 January 2004. As at 31 July 2003, the borrowing ratio was 0.52:1 and the asset cover was 2.97:1.

(b) Interest Rates

The weighted average interest rate on the Sterling fixed rate borrowings shown above is 7.4641% (2002: 7.3975%). The weighted average time for which rates are fixed is two years (2002: three).

12 Increase in provision for redemption of zero dividend preference shares

	2003 £000s	2002 £000s
Provision made during year (notes 14 & 18)	2,308	2,709

13 Financial instruments

The Trust's financial instruments comprise its investment portfolio (see note 9), cash balances, debtors and creditors that arise directly from its operations such as sales and purchases awaiting settlement and accrued income, and the debenture and bank loan used to finance the Trust's operations.

The main risks that the Trust faces arising from its financial instruments are i) interest rate risk; and ii) market price risk, being the risk that the value of investment holdings will fluctuate as a result of changes in market prices caused by factors other than interest rate or currency rate movement. Since the Trust invests primarily in UK equities, any currency risk is not significant.

i) Interest rate risk

The Trust finances its operations through a mixture of retained profits and long-term borrowings. The borrowings have a fixed rate of interest (see note 11).

Notes to the financial statements continued

Financial instruments - continued

The Trust has £5.2m (2002: £5.4m) of fixed interest bearing securities, which have a weighted average interest rate of 6.79% (2002: 6.41%) and a weighted average period to maturity of 4 years (2002: 4.9 years).

ii) Market risk

The Trust's investment portfolio is exposed to market price fluctuations which are monitored by the investment manager in pursuance of the investment objective. Further information on the investment portfolio is set out in the Investment Manager's Report on pages 5 to 7, which is not subject to audit.

The Trust held the following categories of financial instruments at 31 July 2003:

	Book Value £000s	Fair Value £000s
Financial assets		
Investment portfolio	49,611	49,611
Financial liabilities		
Bank loan	(21,541)	(22,421)

The investment portfolio consists of listed investments, which are valued at mid-market price (see note 9).

In the opinion of the directors all assets and liabilities other than the bank loan are stated at their fair value.

The "fair values" of the ordinary income and zero dividend preference shares are based on quoted market prices at 31 July 2003. The fair value of the loan has been estimated according to the discounted value of future cash flows.

The Trust also has an overdraft facility with HSBC Bank plc for £3,500,000 at an interest rate of 1% per annum over base rate. At the balance sheet date none (2002: none) of this facility had been drawn down.

Information regarding the Trust's interest bearing assets are given in the valuation tables on pages 9 to 11 of this report.

14 Called up share capital

	£000s
(a) Authorised	
At 31 July 2002 and 31 July 2003	
300,000,000 ordinary income shares of 5p each	15,000
300,000,000 zero dividend preference shares of 5p each	15,000
Total authorised share capital	30,000
(b) Allotted and fully paid	
Ordinary income shares of 5p	
At 31 July 2002 and 31 July 2003 - 51,697,859 shares	2,585
Zero dividend preference shares of 5p	
At 31 July 2002 - 30,940,239 shares	1,547
Transfer to capital redemption reserve (note 19) - 3,369,000 shares	(169)
At 31 July 2003 - 27,571,239 shares	1,378
Total allotted share capital	3,963

(c) In accordance with the requirements of Financial Reporting Standard No.4, the zero dividend preference shares are defined as "non-equity". 3,369,000 zero dividend preference shares were repurchased in the year at a cost of £2,075,000.

15 Share premium account

	2003 £000s	2002 £000s
At start of year	18,086	78,086
Transfer to distributable capital reserve (note 16)	-	(60,000)
At end of year	18,086	18,086

16 Distributable capital reserve

	£000s
At 31 July 2002	57,622
Repurchase of zero dividend preference shares	(2,075)
At 31 July 2003	55,547

The share premium account was reduced by £60million on 29 May 2002 following approval by the Court and by shareholders. The £60million was credited to the Distributable Capital Reserve to create sufficient reserves from which to repurchase ordinary income and zero dividend preference shares (note 15).

17 Capital reserves - unrealised

	£000s
At 31 July 2002	(23,305)
Net increase in the year	13,906
At 31 July 2003	(9,399)
Surplus arising on valuation of investments:	
- Full listing	(9,101)
- AIM listing	(298)
	(9,399)

18 Capital reserves - realised

	£000s
At 31 July 2002	(32,750)
Realised in the period - Investments	(12,095)
Investment management fee charged to capital (note 3)	(270)
Interest charged to capital (note 5)	(806)
Increase in provision for redemption of zero dividend preference shares (note 12)	(2,308)
At 31 July 2003	(48,229)

19 Capital redemption reserve

	£000s
At 31 July 2002	176
Transfer from share capital (note 14)	169
At 31 July 2003	345

20 Redemption reserve for zero dividend preference shares

	£000s
Balance at 31 July 2002	9,188
Provision for redemption of zero dividend preference shares transferred from capital reserve	2,308
At 31 July 2003	11,496

The redemption reserve for zero dividend preference shares was set up to provide for the repayment entitlement attaching to the zero dividend preference shares which accrues on a daily compound basis to the date of repayment on 4 August 2005.

Notes to the financial statements continued

21 Revenue reserve

	£000s
At 31 July 2002	650
Net deficit for the year	(94)
At 31 July 2003	556

22 Contingent liabilities and other commitments

At 31 July 2003 the Trust had no underwriting commitments and no commitments in respect of holdings of partly paid shares (2002: none).

23 Reconciliation of operating profit to net cash inflow from operating activities

	2003 £000s	2002 £000s
Net revenue from operating activities before interest payable and taxation	2,780	4,394
Decrease in debtors	23	44
Scrip dividends	(20)	(21)
Increase/(decrease) in creditors	7	(17)
Net cash inflow from operating activities	2,790	4,400

24 Gross cash flows

	2003 £000s	2002 £000s
Capital expenditure and financial investment		
Purchases of investments	(19,341)	(29,406)
Sales of investments	21,969	38,837
	2,628	9,431
Capital management fee paid	(295)	(504)
	2,333	8,927

25 Reconciliation of net cash flow to net debt

	2003 £000s
Decrease in cash for the year	(456)
Cash inflow from movement in debt for the period	-
Change in net debt	(456)
Net debt at 31 July 2002	(16,276)
Net debt at 31 July 2003	(16,732)

25 Reconciliation of net cash flow to net debt - continued

Analysis of changes in net debt

	At 31 July 2002 £000s	Cash flows £000s	At 31 July 2003 £000s
Cash at bank	5,265	(456)	4,809
Debt due after one year	(21,541)	-	(21,541)
Net debt	(16,276)	(456)	(16,732)

26 Net asset value and capital return per share

a) The net asset value per share and the net asset values attributable to each class of share at the year end calculated in accordance with the articles of association were as follows:

	Net asset value per share		Net asset value attributable	
	2003 p	2002 p	2003 £000s	2002 £000s
Ordinary income shares	-	-	-	-
Zero dividend preference shares	117.39	109.24	32,365	33,799

The movements during the year of the assets attributable to each class of share were as follows:

	Ordinary income shares £000s	Zero dividend preference shares £000s	Total £000s
Total net assets attributable at start of year	-	33,799	33,799
Total recognised (losses)/gains for the year	401	2,308	2,709
Dividends appropriated in the year	(2,068)	-	(2,068)
Repurchases of zero dividend preference shares	-	(2,075)	(2,075)
Allocation of losses	1,667	(1,667)	-
Total net assets attributable at end of year*	-	32,365	32,365

* Includes provision for redemption of zero dividend preference shares.

Net asset value per ordinary income share is based on net assets attributable to ordinary income shares and on 51,697,859 (2002: 51,697,859) ordinary income shares in issue at the year end.

Net asset value per zero dividend preference share is based on net assets attributable to zero dividend preference shares and on 27,571,239 (2002: 30,940,239) zero dividend preference shares in issue at the year end.

The net asset value per share and net assets attributable to each class of share at the year end, calculated in accordance with FRS 4 were as follows:

	Net asset value per share		Net asset value attributable	
	2003 p	2002 p	2003 £000s	2002 £000s
Ordinary income shares	(7.13)	(5.70)	(3,687)	(2,945)
Zero dividend preference shares	130.76	118.76	36,052	36,744

Differences in net assets attributable to ordinary income shares and zero dividend preference shares calculated on the articles basis and FRS 4 basis arise from the fact that, under the articles, ordinary income shareholders are not liable to make up any shortfall in accrued redemption entitlement to holders of zero dividend preference shares.

Notes to the financial statements continued

Net asset value and capital return per share - continued

b) The capital return values attributable to each class of share calculated in accordance with FRS 4 were as follows:

	Capital return per share	
	2003	2002
	p	p
Ordinary income shares	(3.04)	(49.51)
Zero dividend preference shares	5.75	6.12

Capital return per ordinary income share is based on the net capital loss of £1,573,000 (2002: £25,596,000) and on 51,697,859 (2002: 51,697,859) ordinary income shares of 5p each in issue throughout the year.

Capital return per zero dividend preference share is based on the attributable asset gain of £1,680,000 (2002: £2,081,000) and on 29,211,223 shares (2002: 33,999,581) being the weighted average number of zero dividend preference shares of 5p each in issue during the year.

Notice of class meeting of zero dividend preference shareholders

Notice is hereby given that a Separate Meeting of the holders of zero dividend preference shares of the Trust will be held on 25 November 2003 at 12.25pm at 155 Bishopsgate, London EC2M 3XJ to consider and, if thought fit, pass the following extraordinary resolution:

Extraordinary resolution

THAT the holders of the zero dividend preference shares of 5p each in the capital of the Trust hereby sanction and consent to the passing of resolutions numbers 7 and 8 set out in the notice convening an Annual General Meeting of the Trust for 25 November 2003 as Special Resolutions, contained in the annual report and accounts of the Trust dated 16 September 2003 to the members of the Trust of which the notice of this meeting forms a part and the carrying into effect of such resolutions.

By order of the Board
Framlington Investment Management Limited, Secretary
16 September 2003

Registered office:
155 Bishopsgate, London EC2M 3XJ

Notes:

- 1 A holder of zero dividend preference shares (a "ZDP Shareholder") entitled to attend and vote is entitled to appoint a proxy (or proxies) to attend and, on a poll, vote instead of him. A proxy need not be a ZDP Shareholder of the Trust.
- 2 A blue form of proxy is enclosed for use by ZDP Shareholders. Completion and return of the form of proxy will not prevent a ZDP Shareholder from subsequently attending the ZDP Shareholders' Meeting and voting in person if he so wishes.
- 3 To be effective, the instrument appointing a proxy, and any power of attorney or other authority under which it is signed (or a copy of any such authority certified notarially or in some other way approved by the Directors), must be deposited with the Company's Registrars, not less than 48 hours before the time for holding the meeting or adjourned meeting.
- 4 Pursuant to regulation 41 of the Uncertificated Securities Regulations 2001, the Company has specified that only those ZDP Shareholders registered in the Register of Members of the Trust at 6.00 p.m. on 21 November 2003 shall be entitled to attend and vote at the meeting in respect of the number of ZDP Shares registered in their name at that time. Changes to the Register of Members after 6.00 p.m. on 21 November 2003 shall be disregarded in determining the rights of any person to attend and vote at the meeting.

Notice of annual general meeting

Notice is hereby given that the third Annual General Meeting of the Trust will be held on 25 November 2003 at 12.30 pm at 155 Bishopsgate, London, EC2M 3XJ for the following purposes:

Ordinary resolutions

- 1 To approve the directors' remuneration report for the year ended 31 July 2003.
- 2 To receive the accounts for the year ended 31 July 2003 together with the reports of the directors and auditors.
- 3 To re-elect as a director Mr Soames who retires by rotation.
- 4 To re-elect as a director Mr Carr who retires by rotation.
- 5 To elect as a director Mr Copple.
- 6 To re-appoint Deloitte & Touche LLP as auditors and to authorise the directors to fix their remuneration.

Special resolutions

- 7 THAT subject to the passing of the extraordinary resolution to be proposed at the separate class meeting of the holders of zero dividend preference shares of the Trust convened for 25 November 2003 (or any adjournment of such meeting) the Trust be generally and subject as hereinafter appears be 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 and cancel ordinary income shares of 5p each.

Provided always that

- (i) the maximum number of ordinary income shares hereby authorised to be purchased shall be 7,749,509;
- (ii) the minimum price which may be paid for an ordinary income share shall be 5p;
- (iii) purchases will only be made through the market at prices below the prevailing net asset value of an ordinary income share as calculated by the directors as at the date falling not more than 14 days prior to the date of purchase;
- (iv) the maximum price which may be paid for an ordinary income share shall be an amount equal to 105 per cent of the average of the middle market quotations for an ordinary income share taken from and calculated by reference to the London Stock Exchange Daily Official List for the five business days immediately preceding the date on which the ordinary income share (as the case may be) is purchased;
- (v) the authority hereby conferred shall expire at the conclusion of the annual general meeting of the Trust in 2004 unless the authority is renewed in general meeting prior to such time; and
- (vi) the Trust may make a contract to purchase ordinary income shares under the authority hereby conferred prior to the expiry of such authority which will or may be executed wholly or partly after the expiration of such authority and may make a purchase of ordinary income shares pursuant to any such contract.

- 8 THAT subject to the passing of the extraordinary resolution to be proposed at the separate class meeting of the holders of zero dividend preference shares of the Trust convened for 25 November 2003 (or any adjournment of such meeting) the Trust be generally and subject as hereinafter appears be 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 and cancel zero dividend preference shares.

Provided always that

- (i) the maximum number of zero dividend preference shares hereby authorised to be purchased shall be 8,163,677;
- (ii) the minimum price which may be paid for a zero dividend preference share shall be 5p;
- (iii) purchases will only be made through the market at prices below the prevailing net asset value of a zero dividend preference share as calculated by the directors as at the date falling not more than 14 days prior to the date of purchase;
- (iv) the authority hereby conferred shall expire at the conclusion of the annual general meeting of the Trust in 2004 unless the authority is renewed in general meeting prior to such time; and
- (v) the Trust may make a contract to purchase zero dividend preference shares under the authority hereby conferred prior to the expiry of such authority which will or may be executed wholly or partly after the expiration of such authority and may make a purchase of zero dividend preference shares pursuant to any such contract.

By order of the Board

Framlington Investment Management Limited, Secretary

155 Bishopsgate, London EC2M 3XJ

16 September 2003

Notes:

- 1 A holder of ordinary income shares (an "ordinary income shareholder") entitled to attend and vote is entitled to appoint a proxy (or proxies) to attend and, on a poll, vote instead of him. A proxy need not be an ordinary income shareholder of the Trust.
- 2 A white form of proxy is enclosed for use by ordinary income shareholders. Completion and return of the form of proxy will not prevent an ordinary income shareholder from subsequently attending the annual general meeting and voting in person if he so wishes.
- 3 To be effective, the instrument appointing a proxy, and any power of attorney or other authority under which it is signed (or a copy of any such authority certified notarially or in some other way approved by the directors), must be deposited with the Trust's Registrars, not less than 48 hours before the time for holding the meeting or adjourned meeting.
- 4 Pursuant to regulation 41 of the Uncertificated Securities Regulations 2001, the Trust has specified that only those ordinary income shareholders registered in the Register of Members of the Trust at 6.00pm on 21 November 2003 shall be entitled to attend and vote at the meeting in respect of the number of ordinary income shares registered in their name at that time. Changes to the Register of Members after 6.00pm on 21 November 2003 shall be disregarded in determining the rights of any person to attend and vote at the meeting.

Investor information

Contacts

- **Secretary**
Framlington Investment Management Limited:
020 7374 4100
- **Registrar**
Capita Registrars: 020 8639 2000
- **Select Investment Trust Plan:**
020 7452 1394

Share prices, asset value and performance information sources:

- Financial Times under the Investment Companies section or their website: www.FT.com
- Reuters
 - Ordinary income shares - FDSi.L
 - Zero dividend preference shares - FDS0.L
 - Units - FDS_u.L
- Framlington's website:
www.framlington.co.uk

Annual General Meeting

25 November 2003

Dividends

- First interim - payment in January 2004
- Second interim - payment in April 2004
- Third interim - payment in July 2004
- Fourth interim - payment in October 2004

Results

It is the Trust's aim to announce to the London Stock Exchange interim results for the period to 31 January 2004 in March and to also post out the interim report during that month.

How to invest

The Trust's shares may be purchased through one of the following:

- a stockbroker
- the Framlington Select Investment Trust Plan offers four investment trusts managed by Framlington. Investments can be from £50 per month or lump sums from £500.

For copies of the Select Plan brochure please contact the Framlington 24-hour brochure request line on 0845 702 3138.

All subscriptions for shares are received strictly 'subject to prospectus' (as amended).

Directors, officers and advisers

Directors

The Hon. Nicholas Soames, MP (Chairman)

Mr Jonathan Carr

Mr Richard Granville

Mr Craig Walton (resigned as a director on 16 September 2003)

Mr Arthur Copple (appointed as a director on 16 September 2003)

Registered Office

155 Bishopsgate, London EC2M 3XJ

Tel: 020 7374 4100

Manager and Secretary

Framlington Investment Management Limited

155 Bishopsgate, London EC2M 3XJ

Authorised and regulated by the Financial Services Authority

Registrars

Capita Registrars plc

390-398 High Road, Ilford, Essex IG1 1NQ

Tel: 020 8639 2000

Stockbrokers

UBS Warburg

Auditors

Deloitte & Touche LLP

Chartered Accountants

Solicitors

Stephenson Harwood

Bankers

HSBC Bank plc

Bank of Scotland