

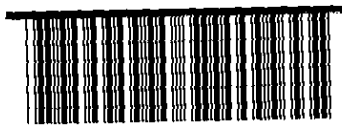
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## Edinburgh Income and Value Trust plc

Annual Report and Accounts 31 May 2000

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**Edinburgh Income and Value Trust plc**

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**Information for Investors**

**Appendix 1**

## Objective

To provide holders of the listed ordinary shares with a high level of income, together with the opportunity for capital and income growth.

<b>Investment manager</b>	Edinburgh Fund Managers plc – Tony Mather
<b>Capital structure</b>	The company has a wholly owned subsidiary, Edinburgh Value Zeros plc. The Group has a capital structure comprising 23,693,875 listed ordinary shares of 1p each and, through its subsidiary, 15,520,000 listed zero dividend preference shares. Each ordinary shareholder is entitled to one vote on a show of hands and, on a poll, to one vote for every share held. The company has a long term loan facility of £11.18m repayable on 27 May 2005. The redemption date of the zero dividend preference shares is 31 May 2005.
<b>Winding up provisions</b>	The company has no fixed duration.
<b>Management fee</b>	0.75% per annum of the gross assets of the group excluding funds managed by Edinburgh Fund Managers plc and 50% of funds managed by other investment managers. The management agreement is terminable on 1 year's notice.
<b>Secretarial fee</b>	£60,000 per annum excluding VAT to be adjusted annually for Retail Price Index.
<b>ISA/PEP status</b>	The company's shares are eligible for Individual Savings Accounts (ISAs), investing in existing general PEPs and PEP transfers.
<b>AITC membership</b>	The company is a member of The Association of Investment Trust Companies and a subscriber to the 'its' advertising campaign.



## Financial Summary

	31 May 2000	8 April 1999 <sup>1</sup>	% change
<b>Performance</b>			
Total assets less current liabilities (£000)	49,847	49,270	+1.2
<b>Capital return</b>			
Net asset value (p)	93.5	97.2 <sup>2</sup>	-3.8
Share price (p)	93.0	100.0	-7.0
<b>Total return</b>			
Net asset value	—	—	+7.1
Share price	—	—	-1.1
Total dividend per share (p)	10.1 <sup>3</sup>	n/a	
Revenue return per share (p)	12.1 <sup>3</sup>	n/a	
<b>(Discount)/premium</b>			
(difference between share price and net asset value)	(0.5)	2.9	
<b>Capital Gearing</b>			
(borrowings over total assets less current liabilities)	56	53	
<b>Expense ratio</b>			
- as % of total assets less current liabilities (annualised)	1.3	n/a	
<b>Year's Highs/Lows</b>			
	<b>High</b>	<b>Low</b>	
Net asset value (p)	130.5	64.7	
Share price (p)	132.5	92.0	
Premium/(discount) (%)	49.3	(7.8)	

<sup>1</sup> First day of listing<sup>2</sup> adjusted for issue expenses<sup>3</sup> for accounting period 10 March 1999 to 31 May 2000

## Chairman's Statement

In this, the first full financial review of the company, I would like to extend a warm welcome to all ordinary and zero dividend preference shareholders. The company's objective is to provide ordinary shareholders with a high level of income together with the opportunity of capital and income growth, and zero dividend preference shareholders with a pre-determined capital entitlement in May 2005.

David Ritchie

The period has been an eventful one during which many investors have seemingly concentrated on technology and internet stocks to the exclusion of everything else. Our own portfolio focus has been quite different. The trust was launched to take advantage of the very polarised nature of the UK stockmarket. Large numbers of primarily medium sized and smaller companies had been neglected by investors and were valued at attractive ratings offering significantly above average yields. This is still the case, and the Managers and Directors continue to see it as an attractive opportunity which will eventually come to be more widely recognised.

### Dividends

The Board has declared a fourth interim dividend of 3.6p which will be paid on 11 August 2000 to shareholders on the register on 4 August 2000. When combined with the other interim dividends already declared and paid, the total dividend paid for the company's first accounting period from 10 March 1999 to 31 May 2000 will amount to 10.1p.

The total dividend for the twelve month period to 31 May 2000 is 9.6p – as intended and outlined in the placing document. At the year-end share price

of 93.5p this resulted in a dividend yield of 10.3%, which compares with a 2.2% yield on the FTSE All-Share Index at that date.

The company's accounting policy is to charge half of the investment management fee and half the loan interest against capital rather than revenue. The revenue return for the initial period was 12.1p.

### Capital

After taking account of initial launch expenses, gross assets less current liabilities rose from £49.3 million to £49.8 million during the period under review. After deducting gearing and the accrual of £1.4 million (6.0p per share) for finance costs on the zero dividend preference shares the net asset value per share has fallen from 97.2p (net of launch expenses) to 93.5p. The share price fell from 100.0p to 93.0p, mirroring the net asset value at 31 May 2000.

The fund is structured with a high level of gearing with bank borrowings and zero dividend preference shares representing 56% of gross assets at 31 May 2000. This leads to a degree of volatility in the trust's net asset value over short time periods.



## Chairman's Statement

The effect of gearing has been adverse to date, but the Board believes that over the lifetime of the gearing it should be beneficial to shareholders.

A consequence of financing the repayment of the zero dividend preference shares out of capital, and also charging to capital part of the interest costs and management expenses, is that growth in gross assets is necessary to ensure that the net asset value per share does not fall. The effect can be determined from the table below. This shows, on projected growth rates which are used here for illustrative purposes only, what the net asset value per share would be on 31 May 2005 given this capital structure.

Annual growth rate (%)	0.0	2.5	5.0	7.5	10.0
Net asset value per ordinary share (p)	47	74	103	136	172

Table 1: Illustrative annual growth rates

### Marketing

The Association of Investment Trust Companies (AITC) launched the 'its' campaign last year. This aims to improve the awareness of potential investors to the attractions of investment trusts. The company, as a member of the AITC, has paid a contribution of £4,900 to the campaign and will pay a further £3,920 in the coming year.

In addition, the Board will promote the company more specifically through the manager's "investment trust initiative" whereby Edinburgh Income and Value Trust participates in the retail product initiatives operated by Edinburgh Fund Managers. These products currently comprise a savings scheme, personal equity plans, individual savings accounts and pension plans. Such products enable investors to make monthly or lump sum investments in the company's shares in a low cost and convenient manner. The company's contribution to this initiative was £15,000.

### Outlook

Recent interest rate increases may constrain UK economic growth, nevertheless the outlook for corporate profits is more encouraging, particularly if we were to see further weakening of sterling against the Euro. Meanwhile the recent stockmarket focus on technology and larger capitalisation stocks continues to leave many sound businesses undervalued and ignored by fund managers. This will not always be so and these remain the focus of the trust's portfolio.

The company's main concentration is on stocks outside the FTSE 100 index and there are many companies offering a good income stream with the potential for growth. As always, stock selection will be the key to achieving the objectives and the focus will remain on the financial health of companies and their ability to grow earnings and dividends on a consistent basis.

### Annual General Meeting

The AGM will be held in Donaldson House, Edinburgh on Wednesday 30 August 2000 at 12 noon. I look forward to welcoming shareholders.

**David Ritchie**

Chairman

20 July 2000



## Manager's Review

In the first full financial year, the net asset value of Edinburgh Income and Value Trust fell from 97.2p (net of expenses) to 93.5p. The company has paid out dividends totalling 10.1p over this period with a payout of 9.6p for the year to 31 May 2000.

### Performance

The fund was launched against a background of falling interest rates, low inflation and improving consumer confidence. Cyclical sectors were the initial beneficiaries of this favourable investment environment and the Trust performed strongly in the early stages.

The period was dominated by a shift in investor sentiment towards "growth", represented by the telecoms, media and technology sectors. The benign inflationary environment contributed to a rerating within this segment of the market. With mega mergers in the FTSE100 Index further concentrating investor focus on a narrow range of sectors, many companies, particularly in the mid and small cap areas of the market, were effectively discriminated against by virtue of the sector they were in. The creation of this two tier market resulted in a polarisation of performance driven solely by market reratings. Subsequently, a derating occurred in the still profitable, but unfashionable, areas of the stock market. This divergence created investment opportunities to capture value in the forgotten stocks and sectors. The net asset value of the trust was significantly boosted in the run up to the year-end as this valuation anomaly began to unwind as evidenced by a stock rotation within the market from high growth technology sectors into undervalued assets as investors sought safety in companies that actually produced profits. Despite the implied valuations accorded by the stock market, traditional companies continued to perform satisfactorily at an operating level thereby providing an income stream to stockholders without compromising their financial position. This has enabled the trust to provide its projected income stream.

Tony Mather

We still believe that attractive investment opportunities exist outside the top tier and continue to target companies with strong cash generation, attractive yields and growth prospects relative to their valuations.

### Portfolio

At the end of the period the portfolio held 55 stocks. The equity split is as follows: 9% of assets invested in FTSE 100 stocks, 45% in mid-250 stocks and 46% invested in small cap stocks. This remains broadly in line with the weightings at the launch of the fund. Within the portfolio itself, one of the major changes was the reduction in exposure to retailers. High operational gearing and price deflation were to cause serious problems, in particular, for the mainstream retailers and during the year holdings in Arcadia, Storehouse and Austin Reed were sold. Other major disposals included Low and Bonar, BPB, and Novara. As a result of the unprecedented polarisation in sector performance prevalent in the UK market, opportunities arose to acquire shares in well-managed, cash generative companies at attractive valuation levels. New holdings were taken in Abbey National, Scottish & Newcastle and Imperial Tobacco. Exposure to more defensive areas was increased with the purchase of Scottish and Southern Energy. Other purchases included Holidaybreak and Christian Salvesen.

Corporate activity has been a key feature during the period with a mix of offers in both paper and cash. Cirqual and Waddington received paper bids while



## Manager's Review

Tarmac and Greenalls completed a return of value through a mix of cash and new shares. Cash bids were received for Burmah Castrol, Partco, Arjo Wiggins, United Biscuits, Ruberoid and James Finlay. This trend is set to continue in response to depressed levels of valuation in certain stocks and sectors.

### Outlook

UK interest rates troughed at 5% in June of last year, but since last September have climbed to the current level of 6%. Inflation remains relatively subdued and economic growth seems set to stabilise around the long term trend level of 2.5% for this year and next. This stable background will mean that UK interest rates are close to, or at, their peak. With European rates set to continue to rise, the recent strength of sterling should unwind and there is already evidence of this. This will ease pressure on the manufacturing sector although the

benefits are unlikely to flow through in the short term. Nevertheless, recovery in Europe and an easing of pressure on manufacturers margins presents a positive outlook for the industrial sectors. The company's exposure to economically sensitive sectors leaves it well placed to benefit from the improved earnings outlook. Furthermore it is likely that depressed levels of valuations will prompt companies to pursue share buybacks, or encourage corporate activity, in an attempt to realise value. Our strategy remains to target stocks with attractive yields and the potential for capital appreciation. The manager continues to seek companies with low to medium risk, good interest and dividend cover and growth relative to their valuations.

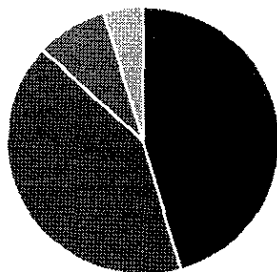
*Edinburgh Fund Managers plc*

20 July 2000

## Analysis of Shareholders

at 31 May 2000

% of ordinary shares held by shareholders



Individuals (45.5%)

Unit and investment trusts (41.3%)

Pension funds (8.5%)

Other institutions (4.7%)





## Distribution of Assets

at 31 May 2000

Sector classification		Market Value £000	%
<b>Basic industries</b>	Chemicals	816	1.6%
	Construction & building materials	4,067	8.2%
		<b>4,883</b>	<b>9.8%</b>
<b>General industrials</b>	Aerospace & defence	753	1.5%
	Electronic & electrical equipment	547	1.1%
	Engineering & machinery	3,764	7.5%
		<b>5,064</b>	<b>10.1%</b>
<b>Cyclical consumer goods</b>	Automobiles	516	1.0%
	Housing goods & textiles	1,449	2.9%
		<b>1,965</b>	<b>3.9%</b>
<b>Non cyclical consumer goods</b>	Food producers & processors	4,978	10.0%
	Packaging	1,449	2.9%
	Personal care & household products	1,128	2.3%
	Tobacco	1,984	4.0%
		<b>9,539</b>	<b>19.2%</b>
<b>Cyclical services</b>	Distributors	2,342	4.7%
	General retailers	3,446	6.9%
	Leisure, entertainment & hotels	2,926	5.9%
	Restaurants, pubs & breweries	2,055	4.1%
	Support services	117	0.2%
	Transport	3,564	7.1%
		<b>14,450</b>	<b>28.9%</b>
<b>Non cyclical services</b>	Food and drug retailer	<b>1,224</b>	<b>2.5%</b>
<b>Utilities</b>	Electricity	1,226	2.5%
	Water	3,565	7.2%
		<b>4,791</b>	<b>9.7%</b>
<b>Financials</b>	Banks	1,334	2.7%
	Insurance	1,739	3.5%
	Life assurance	1,112	2.2%
	Real estate	1,081	2.2%
	Speciality & other finance	810	1.6%
		<b>6,076</b>	<b>12.2%</b>
<b>UK bonds</b>	UK Treasury Stock	<b>18</b>	<b>0.0%</b>
<b>Total investments</b>		<b>48,010</b>	<b>96.3%</b>
<b>Net current assets</b>		1,837	3.7%
<b>Total assets less current liabilities</b>	<b>49,847</b>	<b>100.0%</b>	



## Thirty Largest Investments

at 31 May 2000

Company	Market Value £000	Sector classification
Fine Art Development	1,806	General retailers
James Findlay	1,770	Food producers & processors
Severn Trent	1,463	Utilities
Rexam	1,449	Paper production
Grampian Holdings	1,391	General retailers
Unigate	1,347	Food producers & processors
Abbey National	1,334	Banking
Scottish & Southern Energy	1,226	Utilities
Safeway	1,224	Food retailers
Pendragon	1,221	Distributors
Ten largest investments	14,231	28.6% of total assets less current liabilities
Scottish & Newcastle	1,214	Restaurants, pubs & breweries
Kelda	1,179	Utilities
Arriva	1,173	Transport
Express Dairies	1,137	Food producers & processors
McBride	1,128	Food producers & processors
Hepworth	1,127	Building materials
Britannic	1,112	Insurance
John Mowlem	1,105	Construction & housing
Tops Estates	1,081	Real estate
Kunick	1,068	Leisure, entertainment & hotels
Twenty largest investments	25,555	51.3% of total assets less current liabilities
Tomkins	1,053	Engineering
Imperial Tobacco	1,028	Tobacco
IMI	1,024	Engineering
Royal & Sun Alliance	995	Insurance
Gallaher Group	957	Tobacco
Beazer Group	949	Construction & housing
United Utilities	924	Utilities
Holidaybreak	853	Leisure, entertainment & hotels
Whitbread	841	Leisure, entertainment & hotels
Scapa Group	816	Chemicals
Thirty largest investments	34,995	70.2% of total assets less current liabilities
Other investments represented by 25 holdings	13,015	26.1% of total assets less current liabilities
Total investments	48,010	96.3% of total assets less current liabilities
Net current assets	1,837	3.7% of total assets less current liabilities
Total assets less current liabilities	49,847	100.0% of total assets less current liabilities



## Corporate Information

### Registered Office

Donaldson House  
97 Haymarket Terrace  
Edinburgh EH12 5HD  
Telephone: 0131-313 1000  
website: [www.edfd.com](http://www.edfd.com)

### Manager and Secretary

Edinburgh Fund Managers plc  
Donaldson House  
97 Haymarket Terrace  
Edinburgh EH12 5HD  
Telephone: 0131-313 1000  
Regulated by IMRO and  
the Personal Investment Authority

### Registrar

Lloyds TSB Registrars Scotland  
117 Dundas Street  
Edinburgh EH3 5ED  
Telephone: 0870-601 5366  
website: [www.lloydstsb-registrars.co.uk](http://www.lloydstsb-registrars.co.uk)

### Banker

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

### Auditors

Ernst & Young  
Ten George Street  
Edinburgh EH2 2DZ

### Company Broker

Brewin Dolphin Securities Limited  
5 Giltspur Street  
London EC1A 9BD

### Company Registration Number

SC 194352



## Board of Directors

### **David Ritchie\***

#### *Chairman*

David Ritchie (55), appointed on 11 March 1999, is chairman of Fleming Japanese Investment Trust and a non-executive director of Majedie Investments and Gioma Restaurants. He was executive chairman of Scottish Widows Investment Management and is a fellow of the Faculty of Actuaries.

### **Sir Donald MacKay\***

#### *Director*

Sir Donald MacKay (63), appointed on 11 March 1999, is a founding director of DTZ Pleda Consulting, chairman of Grampian Holdings and Edinburgh Business School and a director of The Scottish Mortgage and Guarantee Trust. He is a former chairman of Scottish Enterprise.

### **Francis Malcolm\***

#### *Director*

Francis Malcolm (56), appointed on 11 March 1999, is a stockbroker and a director of Brewin Dolphin Securities. He is a non-executive director of Close Brothers AIM VCT and Close Brothers Development VCT.

# the board

### **David Simpson\***

#### *Director*

David Simpson (59), appointed on 11 March 1999, is chairman of Martin Currie Capital Return Trust and a non-executive director of Post Office Pensions Trustees, Wickes and Fidelity European Values. He was a general manager and company secretary of The Standard Life Assurance Company and is a fellow of the Faculty of Actuaries.

### **Douglas Smith\***

#### *Director*

Douglas Smith (53), appointed on 11 March 1999, is Scottish chairman of Marsh UK Limited. He is chairman of Heart of Midlothian, an associate of the Chartered Insurance Institute and a fellow of the Institute of Directors.

\*Member of the audit and management engagement committee.



## Directors' Report

### Introduction

The company was incorporated as a public limited company on 10 March 1999 and commenced business on 8 April 1999.

### Business and status

The company carries on business as an investment trust for the purpose of the Income and Corporation Taxes Act 1988. The company has conducted its affairs so as to enable it to seek such approval. The close company provisions of the Act do not apply to the company.

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

### Share capital

The authorised share capital on incorporation was £50,000, divided into 5,000,000 ordinary shares ('shares') of 1p each of which two shares were issued nil paid. On 29 March 1999 the authorised share capital was increased to £315,918 by the creation of 26,591,800 shares.

Following the placing on 31 March 1999, 23,693,875 shares were admitted to the official list and dealings in the shares commenced on 8 April 1999.

### Review of activities

During the period the company followed the normal activities of an investment trust. Details of these are given in the Chairman's Statement and the Manager's Review.

### Dividends

Details of dividends paid during the period to 31 May 2000 and amounts transferred to revenue reserves are shown in notes 6 and 18 to the financial statements.

### Directors

The names of the directors who served throughout the period and their holdings in the company's shares are shown in Table 1 opposite.

The company has not been notified of any other changes in the directors' holdings between 31 May 2000 and 20 July 2000.

In accordance with the Articles of Association, all directors retire from office. Messrs Ritchie, Malcolm, Simpson and Smith and Sir Donald MacKay will be proposed for election.

Brewin Dolphin Securities, of which Mr Malcolm is a director, were the sponsors and placing agents of the company and received a fee of £0.5million. No other contract or arrangement subsisted during the period in which any of the directors was materially interested. No director had a service contract with the company.

### Payments Policy

The company's payment policy is to ensure settlement of suppliers' invoices in accordance with the stated terms. In certain circumstances, settlement terms are agreed prior to business taking place.

### Year 2000

The year 2000 compliance project was successfully implemented by Edinburgh Fund Managers plc, the company's manager and ensured that its systems and services continued to operate over the millenium. All costs of the project were met by the manager.

### Corporate Governance

#### Compliance

The company is committed to high standards of corporate governance. The board is accountable to the company's shareholders for good governance and this statement describes how the company applies the principles identified in the Combined Code appended to the Listing Rules of the Financial Services Authority.

	Ordinary shares	
	31 May 2000	Nature of interest
David Ritchie	15,000	Beneficial
Sir Donald MacKay	5,000	Beneficial
Francis Malcolm	20,000	Beneficial
David Simpson	14,000	Beneficial
Douglas Smith	—	—

Table 1 Directors and their holdings in the company



## Directors' Report

The board believes that the company has complied throughout the accounting period with the provisions set out in Section 1 of the Code except for the provision which relates to the combination of the roles of the chairman and chief executive. This provision does not apply as the company has no executive directors.

### Directors

The board has overall responsibility for the company's affairs. It delegates, through an investment management agreement and through specific instructions, the day to day management of the company to the manager, Edinburgh Fund Managers plc. The company has no executives or employees.

The board presently consists of five non-executive directors, one of whom is chairman.

The majority of the directors are considered by the board to be independent of management and free from any business or other relationship which could materially interfere with the exercise of their independent judgement. Mr Malcolm is a director of Brewin Dolphin Securities, the company's broker and is deemed not to be independent.

Biographies of the directors appear on page 10 of this report. Each director has the requisite business and financial experience which enables the board to provide effective strategic leadership and proper governance of the company. The senior independent director is Sir Donald MacKay.

The board meets at least four times each year. There is an annual cycle of board meetings which is designed to address, in a systematic way, overall strategy, review of investment policy, investment performance, marketing achievements, budgets, dividend policy and communication with shareholders.

Appointments of new directors are considered by the whole board taking into account the need to maintain a balanced board. When a new director is appointed to the board, he or she is provided with all relevant information regarding the company and their duties as a director.

A director appointed during the year is required to retire and seek election by shareholders at the next annual general meeting. All directors are required to submit themselves for re-election at least every three years.

There is a procedure for directors to take independent professional advice, if necessary, at the company's expense. This is in addition to the access which every director has to the advice and services of the company secretary, Edinburgh Fund Managers plc, which is responsible to the board for ensuring that board procedures are followed and that applicable rules and regulations are complied with.

### Communication with shareholders

The directors place great importance on communication with the company's shareholders. The company also carries out a programme of regular dialogue and individual meetings with institutional shareholders.

At the annual general meeting all shareholders have the opportunity to put questions to the board and a presentation from the manager covers the investment performance and strategy during the financial year and the outlook for the year ahead. The board hopes that as many shareholders as possible will be able to attend the meeting. Shareholders have direct access to the manager at any time through the freephone shareholder information service.

### Accountability and audit

The company has adopted the transitional approach for the Combined Code set out in the letter from the London Stock Exchange to listed companies at the end of September 1999 and reports as follows:

The board confirms that, as at 31 May 2000, it had established the procedures necessary to implement the guidance Internal Control: Guidance for Directors on the Combined Code. The board will continue to consider management and internal control on a regular basis during the year and there will be a full risk and control assessment before reporting on the year ending 31 May 2001.



## Directors' Report

The board has overall responsibility for ensuring that there is in place a system of internal financial control for the safeguarding of assets, the maintenance of proper accounting records and the reliability of financial information. During the year the board has reviewed the effectiveness of the systems. Any system of internal financial control can only provide reasonable and not absolute assurance of meeting the internal control objectives.

The manager is responsible for the design, implementation and maintenance of controls and procedures to safeguard the assets of the company and to manage its affairs properly. The system extends to operational and compliance controls and risk management. Clear lines of accountability have been established between the board and the manager and regular reports on controls and compliance issues are provided to the board. In carrying out its review, the board has had regard to the activities of the manager, the manager's internal audit function and the external auditors.

The audit and management engagement committee, of which David Simpson is chairman, meets at least twice a year and considers reports from the internal and external auditors, as well as from the manager. The audit and management engagement committee keeps the scope and effectiveness of the external audit under review. The independence and objectivity of the external auditors are also considered on a regular basis. Shareholders have the opportunity at each annual general meeting to vote on the election of the external auditors for the forthcoming year.

### Going concern

The directors believe that the company 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 accounts.

### Corporate Governance and Socially Responsible Investment Policy

The company's manager actively encourages companies to adhere to best practice in the area of

Corporate Governance and Socially Responsible Investing.

They believe that this can best be achieved by entering into a dialogue with company management to encourage them, where necessary, to improve their policies in both areas.

Their ultimate objective however is to deliver superior investment return for their clients. Accordingly, whilst they will seek to favour companies which pursue best practice in these areas this must not be to the detriment of the return on the investment portfolio.

In order to monitor company policies effectively they subscribe to the Proxy Voting and Environmental Screening service offered by Manifest, an organisation which provides specialist research information on both areas.

### Substantial share interests

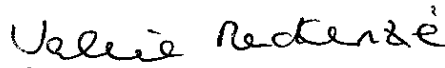
As at 20 July 2000, the substantial interests in the ordinary share capital had been notified to the company are shown in Table 2.

Holder	No. of ordinary Shares	%
Exeter Asset Management	2,800,000	11.8%
Martin Currie Investment Management	2,515,000	10.6%
HL Income & Growth Trust	1,946,000	8.2%
Gartmore Split Capital Opportunities Trust	1,070,000	4.5%
Aberdeen Asset Managers	770,000	3.2%

Table 2 Substantial share interests

### Auditors

The company's auditors, Ernst & Young, are willing to continue in office and resolutions will be proposed at the annual general meeting to appoint them and to authorise the directors to fix their remuneration.

By order of the board,  
  
**Edinburgh Fund Managers plc**  
 Secretary

Edinburgh, 20 July 2000



## 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 company and of the revenue of the company for that period. In preparing those financial statements, the directors are required to:

- ~ select suitable accounting policies and then 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 financial statements;

The directors are responsible for ensuring that proper accounting records are kept which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and to detect fraud and other irregularities.





## Auditors' Report

### To the shareholders of

#### Edinburgh Income and Value Trust plc

We have audited the financial statements on pages 16 to 26, which have been prepared under the historical cost convention, as modified by the revaluation of fixed asset investments, and the accounting policies set out on page 19.

#### Respective responsibilities of directors and auditors

The directors are responsible for preparing the Annual Report. As described on page 14, this includes responsibility for preparing the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, the Listing Rules of the Financial Services Authority and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit or if information specified by law or the Listing Rules regarding directors' remuneration and transactions with the group is not disclosed.

We review whether the statement on pages 11 to 13 reflects the company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules and we report if it does not. We are not required to consider whether the board's statements on internal controls cover all risks and controls or form an opinion on the effectiveness of either the group's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report, including the corporate governance statement, and consider whether it is consistent with the audited financial statements. We 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 Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

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

#### Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company and of the group as at 31 May 2000 and of the return of the group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

*Ernst & Young*

**Ernst & Young**  
Registered Auditor

Edinburgh, 20 July 2000



## Group Statement of Total Return

for the period 10 March 1999 to 31 May 2000

	Notes	Revenue £000	Capital £000	Total £000
Realised gains on investments	8	—	3,371	3,371
Unrealised losses on investments	17	—	(2,697)	(2,697)
<b>TOTAL GAINS ON INVESTMENTS</b>		<b>—</b>	<b>674</b>	<b>674</b>
Investment income	2	3,622	—	3,622
Interest receivable		136	—	136
Other Income		12	—	12
Investment management fee	3	(254)	(254)	(508)
Administrative expenses	4	(260)	—	(260)
<b>NET RETURN BEFORE FINANCE</b>				
<b>COSTS AND TAXATION</b>		<b>3,256</b>	<b>420</b>	<b>3,676</b>
Interest payable		(377)	(377)	(754)
<b>RETURN ON ORDINARY ACTIVITIES</b>				
<b>BEFORE TAXATION</b>		<b>2,879</b>	<b>43</b>	<b>2,922</b>
Taxation	5	(3)	3	—
<b>RETURN ON ORDINARY ACTIVITIES</b>				
<b>AFTER TAXATION</b>		<b>2,876</b>	<b>46</b>	<b>2,922</b>
Non- equity minority interests		—	(1,416)	(1,416)
<b>RETURN ATTRIBUTABLE TO</b>				
<b>MEMBERS OF THE PARENT COMPANY</b>		<b>2,876</b>	<b>(1,370)</b>	<b>1,506</b>
Dividends in respect of equity shares	6	(2,393)	—	(2,393)
Transfer to/(from) reserves		483	(1,370)	(887)
<b>BASIC RETURN PER ORDINARY SHARE</b>	<b>7</b>	<b>12.14p</b>	<b>(5.78p)</b>	<b>6.36p</b>

The revenue column of this statement represents the consolidated profit and loss account of the group.  
All revenue and capital items in the above statement derive from continuing operations.



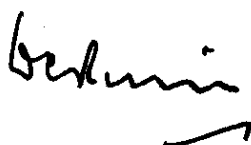
## Balance Sheets

as at 31 May 2000

	Notes	Group £000	Company £000
FIXED ASSETS			
Investments	8	48,010	47,992
Investment in subsidiary	9	—	—
		<u>48,010</u>	<u>47,992</u>
CURRENT ASSETS			
Debtors	11	594	603
Cash and short term deposits	21	2,955	2,955
		<u>3,549</u>	<u>3,558</u>
CREDITORS: AMOUNTS FALLING			
DUE WITHIN ONE YEAR	12	1,712	1,702
NET CURRENT ASSETS		<u>1,837</u>	<u>1,856</u>
TOTAL ASSETS LESS CURRENT LIABILITIES		49,847	49,848
CREDITORS: AMOUNTS FALLING			
DUE AFTER MORE THAN ONE YEAR	13	11,180	28,144
		<u>38,667</u>	<u>21,704</u>
CAPITAL AND RESERVES			
Ordinary share capital	14	237	237
Other reserve	15	22,381	22,381
Capital reserve – realised	16	1,327	1,276
Capital reserve – unrealised	17	(2,697)	(2,696)
Revenue reserve	18	483	506
EQUITY SHAREHOLDERS' FUNDS		<u>21,731</u>	<u>21,704</u>
NON EQUITY MINORITY INTERESTS	19	16,936	
		<u>38,667</u>	
NET ASSET VALUE PER SHARE			
Ordinary shares	23	93.47p	

The financial statements on pages 16 to 26 were approved by the board on 20 July 2000 and were signed on its behalf by:

D RITCHIE, Chairman




## Group Cashflow Statement

for the period 10 March 1999 to 31 May 2000

	Notes	Group	
		£000	£000
NET CASH INFLOW			
FROM OPERATING ACTIVITIES	20		2,566
RETURN ON INVESTMENT AND			
SERVICING OF FINANCE			
Interest paid			(673)
TAXATION			—
CAPITAL EXPENDITURE AND			
FINANCIAL INVESTMENT			
Purchase of investments		(74,045)	
Sale of investments		27,290	
NET CASH OUTFLOW FROM CAPITAL EXPENDITURE			
AND FINANCIAL INVESTMENT			(46,755)
EQUITY DIVIDENDS PAID			(1,540)
FINANCING			
Issue of preference shares to minority shareholders		15,520	
Issue of ordinary share capital		23,694	
Expenses of share issue		(1,037)	
Loan repayable on 27 May 2005		11,180	
NET CASH INFLOW FROM FINANCING			49,357
INCREASE IN CASH	21		2,955



## Notes to the Accounts

### 1 Accounting policies

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

(a) **Basis of Accounting** – The accounts have been prepared under the historical cost convention, modified to include the revaluation of fixed asset investments. The accounts have been prepared in accordance with applicable accounting standards, with the Statement of Recommended Practice 'Financial Statements of Investment Trust Companies' on the assumption that approval as an investment trust will be granted.

(b) **Group accounts** – On 8 April 1999 the company purchased the entire ordinary share capital of Edinburgh Value Zeros plc, making this a wholly-owned subsidiary. The group accounts consolidate the combined assets, liabilities and results of the company and its subsidiary. The company has taken advantage of s230 of the companies Act 1985 in not presenting the company's own Statement of Total Return.

(c) **Investment income and interest receivable** – Dividends are included in revenue by reference to the date on which the investment is quoted ex-dividend. In accordance with Financial Reporting Standard 16 'Current Tax' dividends receivable are recognised net of the attributable tax credits. Interest on investments and other interest receivable are dealt with on an accruals basis.

(d) **Investments** – Investments are valued at middle market prices.

(e) **Investment in subsidiary undertaking** – The company's investment in Edinburgh Value Zeros plc is carried on the company's accounts at market value.

(f) **Capital reserve**

**Realised** – Gains and losses on realisation of investments of a capital nature are dealt with in this reserve. 50% of the investment management fee, along with the associated irrecoverable VAT and of interest payable are charged to this reserve. The associated tax relief is credited to this reserve.

**Unrealised** – Unrealised depreciation/appreciation of investments is accounted for in this reserve.

(g) **Expenses** – All expenses are accounted for on an accruals basis and are charged through the revenue account except where (i) they directly relate to the acquisition or disposal of an investment, in which case, they are added to the cost of the investment or deducted from the sale proceeds, and (ii) expenses are charged to capital reserve – realised where a connection with maintenance or enhancement of the value of investments can be demonstrated.

In this respect, the investment management fee and interest payable has been allocated 50% to capital reserve – realised and 50% to the revenue account.

(h) **Taxation** – Deferred taxation is provided on all timing differences to the extent that liabilities are likely to arise in the foreseeable future.

(i) The amount ultimately repayable to the non equity minority shareholders is to be spread over the life of the trust and is treated as an appropriation from capital reserve - realised.

Group  
Period 10 March 1999  
to 31 May 2000  
£000

### 2 Investment income

Franked investment income	3,511
Unfranked investment income	22
Interest from UK investments	89
	<u>3,622</u>



## Notes to the Accounts

Group  
£000  
Period 10 March 1999  
to 31 May 2000

**3 Investment management fee**

Investment management fee (including VAT)	508
Charged to capital	(254)
	<u>254</u>

The management fee of 0.75% per annum payable to Edinburgh Fund Managers plc is calculated on the gross assets of the company and any subsidiary less (i) the value of any investment funds managed by Edinburgh Fund Managers plc and (ii) 50% of the value of any investment funds managed or advised by investment managers other than Edinburgh Fund Managers plc. 50% of the management fee has been charged to the capital reserve – realised (see note 16).

The management agreement between the company and Edinburgh Fund Managers plc is terminable by either party on one year's notice.

Edinburgh Fund Managers plc also received fees of £60,000, excluding VAT, in connection with the launch of the company, which are included in the expenses of the share issue (note 15).

**4 Administrative expenses**

Directors' fees	55
Auditors' remuneration - statutory audit	8
- initial accounts	13
Secretarial fee	69
Investment Trust Initiative - marketing expenditure	13
Printing and stationery	21
Registrars' fees	25
Other	56
	<u>260</u>

Directors' fees comprise the chairman's fees of £12,000 per annum and fees of £8,000 per annum paid to each other director.

Brewin Dolphin Securities, of which Mr Malcolm is a director, received a fee of £0.5million as sponsors and placing agents of the company.

The secretarial fee is paid to Edinburgh Fund Managers plc and is adjusted annually in line with the Retail Prices Index.

The contribution to the Investment Trust Initiative of £15,000 per annum was paid to Edinburgh Fund Managers plc in respect of marketing and promotion of the company.

The auditors received additional non-audit fees of £35,000, excluding VAT, in connection with the launch of the company, which are included in the expenses of the share issue (note 15).

**5 Taxation**

Corporation tax charge	<u>—</u>
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## Notes to the Accounts

Company  
£000  
Period 10 March 1999  
to 31 May 2000

**6 Dividends on equity shares**

Initial interim dividend of 0.5p per share paid on 30 July 1999	118
First interim dividend of 2.0p per share paid on 30 October 1999	474
Second interim dividend of 2.0p per share paid on 4 February 2000	474
Third interim dividend of 2.0p per share paid on 30 April 2000	474
Fourth interim dividend of 3.6p per share payable on 11 August 2000	853
	<u>2,393</u>

**7 Basic return per ordinary share**

The return per ordinary share is based on the following figures:

	Period 10 March 1999 to 31 May 2000
Revenue return	£2,876,000
Capital return	(£1,370,000)
Average number of ordinary shares in issue	23,693,875

No diluted return per share is required as there are no potentially dilutive shares.

**8 Investments**

	Fixed Interest £000	Equities £000	Total £000
(a) Group			
Additions at cost	1,128	73,498	74,626
Sales – proceeds	—	(27,290)	(27,290)
– realised gains	—	3,371	3,371
Closing book cost	1,128	49,579	50,707
Closing unrealised depreciation	(29)	(2,668)	(2,697)
Closing market value	1,099	46,911	48,010
(b) Company			
Additions at cost	1,109	73,498	74,607
Sales – proceeds	—	(27,290)	(27,290)
– realised gains	—	3,371	3,371
Closing book cost	1,109	49,579	50,688
Closing unrealised depreciation	(28)	(2,668)	(2,696)
Closing market value	1,081	46,911	47,992

All investments are listed on the London Stock Exchange.



## Notes to the Accounts

Group  
£000  
Period 10 March 1999  
to 31 May 2000

### 9 Investment in subsidiary

Additions at cost	1,467
Amount written off	(1,467)
Closing book cost	—
Closing unrealised appreciation	—
Closing market value	—

On 8 April 1999, 50,000 Edinburgh Value Zeros ordinary shares were purchased and a further 128,091 were subsequently purchased under the subscription agreement (see note 24) for a total consideration of £1,466,778. The company owns the whole of the ordinary share capital of Edinburgh Value Zeros plc.

### 10 Risk management, financial assets and liabilities

The following information is given in accordance with Financial Reporting Standard 13, 'Derivatives and Other Financial Instruments'.

#### Risk management

The major risks associated with the company are market, liquidity and interest rate risk. The company has established a framework for managing these risks which is evolving continually as the company's investment activities change in response to market developments. The directors have provided the manager with guidelines and limits for the management of gearing, investments and financial instruments.

Market risks arises from changes in interest rates, valuations accorded to equities, movements in prices and the liquidity of financial instruments. Market price risk is managed through investment guidelines agreed by the board with the manager and is discussed at each board meeting. It is the company's policy to increase its exposure to equity market price risk through the investment of borrowings, thus increasing the opportunity for growth of assets in rising markets but also the risk when markets fall. The downside risk may be reduced by increasing the level of cash balances through the sale of equities.

The company's long term loan is at a fixed rate which exposes the company's to changes in the market value in the event that the debt is repaid before maturity.

As all the financial assets and liabilities are denominated in sterling, the company is not open to currency risk.

The group's financial instruments comprise securities, other investments, cash balances and debtors and creditors that arise directly from its operations, for example, in respect of sales and purchases awaiting settlement and debtors for the accrued income. The disclosures below exclude short term debtors and creditors.

#### Financial assets

Fixed asset investments (see note 8) are valued at middle market prices which equate to their fair values.

At the balance sheet date the group held a fixed interest investment with a market value of £1,099,000. These earn a weighted average rate of return of 7.5% and have a weighted average period to maturity of 20.3 years.

Cash and short term deposits are held in floating rate accounts. The benchmark that determines the interest received or paid on balances, is the bank base rate, which was 6.00% at 31 May 2000.





## Notes to the Accounts

**10 Financial assets and liabilities-cont'd****Financial liabilities**

The company's principal financial liabilities are detailed in note 13 and 19.

The company has entered into an interest rate swap agreement to fix the interest rate cost of the Flemings loan. At 31 May 2000, the company had an outstanding interest rate swap agreement with a notional principal value of £11,180,000 maturing on 27 May 2005. Under this agreement the company pay 5.37% per annum and receive LIBOR, producing an effective fixed rate of 5.97%. There also exists an interest free loan from Edinburgh Value Zeros plc for £15,497,000 and an irrevocable undertaking under the subscription agreement detailed in note 24.

The fair value of the zero dividend preference shares at the period end was £16,800,000. The fair value of the interest rate swap based on market values, at the period end was £565,000 and the book value was nil.

	Group £000	Period 10 March 1999 to 31 May 2000 Company £000
<b>11 Debtors: amounts due within one year</b>		
Dividends and interest receivable	566	565
Taxation recoverable	18	18
Sundry debtors	10	20
	<u>594</u>	<u>603</u>
<b>12 Creditors: amounts falling due within one year</b>		
Amounts due to brokers	581	581
Investment management fee	125	125
Sundry creditors	33	23
Loan interest	81	81
Dividend payable	853	853
Share issue expenses	39	39
	<u>1,712</u>	<u>1,702</u>
<b>13 Creditors: amounts falling due after more than one year</b>		
Amount due to Robert Fleming	11,180	11,180
Amount due to Edinburgh Value Zeros plc	—	15,497
Amount due in respect of purchase of shares in subsidiary	—	1,467
	<u>11,180</u>	<u>28,144</u>

On 15 April 1999 a floating rate term loan of £11,180,000 was drawn down from Robert Fleming & Co Limited. Edinburgh Income and Value Trust has also entered into an interest rate swap which means that interest is paid quarterly at an effective fixed rate of 5.97% per annum. This loan is repayable on 27 May 2005.

On 15 April 1999, £15,497,000 was borrowed from Edinburgh Value Zeros plc, a wholly owned subsidiary of the company. This is an interest free loan which is due to be repaid on 31 May 2005.



## Notes to the Accounts

Group  
and Company  
£000  
Period 10 March 1999  
to 31 May 2000

**14 Ordinary share capital**

Authorised	
31,591,800 ordinary shares of 1p each	316
Authorised, issued and fully paid	
23,693,875 ordinary shares of 1p each	237

Following the placing on 31 March 1999 23,693,875 ordinary shares of 1p each were issued at 100p per share to finance the initial investments of the company. A consideration of £23,693,875 was received.

The Directors intend to distribute substantially all of the income after expenses and tax to the ordinary shareholders on a quarterly basis. Repayment of the bank loan and the loan from Edinburgh Value Zeros plc will take priority over either income or capital returns to the ordinary shareholders.

**15 Other reserve**

Premium arising on issue of ordinary shares	23,457
Expenses of share issue	(1,076)
Closing balance	22,381

Court approval was granted on 13 September 1999 for the premium arising on issue of ordinary shares to be regarded as distributable.

**16 Capital reserve – realised**

	Group £000	Company £000
Realised gain on sale of investments	3,371	3,371
Management fee charged to capital (including VAT)	(254)	(254)
Interest paid charged to capital	(377)	(377)
Non equity minority interests	(1,416)	—
Investment in subsidiary written off (see note 9)	—	(1,467)
Tax relief	3	3
Closing reserve	1,327	1,276

**17 Capital reserve – unrealised**

Movement in unrealised depreciation on investments	(2,697)	(2,696)
Closing reserve	(2,697)	(2,696)



## Notes to the Accounts

	Group £000	Period 10 March 1999 to 31 May 2000 Company £000
<b>18 Revenue reserve</b>		
Movement for the period	483	506
Closing reserve	483	506

	Group and Company £000
<b>19 Non-equity minority interests</b>	Period 10 March 1999 to 31 May 2000
Initial issue of zero dividend preference shares	15,520
Accrued finance costs (see note 24)	1,416
Closing balance	16,936

**20 Reconciliation of net return before finance costs and taxation  
to net cash inflow from operating activities**

Net return before finance costs and taxation	3,256
Increase in dividends and interest receivable	(566)
Increase in sundry debtors	(10)
Increase in sundry creditors	158
Management fees charged to capital reserve	(254)
Tax on unfranked investment income included within income from UK companies	(18)
	<u>2,566</u>

**21 Analysis of changes in net debt during the period**

	Cashflows £000	At 31 May 2000 £000
Cash and short term deposits	2,955	2,955
Debt due after more than one year	(11,180)	(11,180)
	<u>(8,225)</u>	<u>(8,225)</u>

**22 Reconciliation of movement in shareholders' funds**

Revenue for the period	2,876
Recognised capital loss for the period	(1,370)
Total recognised gain for the period	1,506
Dividends in the period	(2,393)
Issue of shares	22,618
Closing shareholders' funds	<u>21,731</u>



## Notes to the Accounts

### 23 Net asset value per equity share

Total shareholders' funds have been calculated in accordance with the provisions of Financial Reporting Standard 4 'Capital Instruments'. The analysis of non equity shareholders' funds on the face of the balance sheet does not, under the articles of association, reflect the rights of the preference shareholders on a return of assets. These rights are reflected in the net asset value per non equity shareholder at the year end, adjusted to reflect the deduction of accrued finance costs. A reconciliation between the two sets of figures is given below:-

	31 May 2000
Total equity shareholders' funds	£21,731,000
Adjusted net assets	£22,146,000
Number of ordinary shares in issue at the year end	23,693,875
Total equity shareholders' funds per share	91.72p
Add accrued finance costs	1.75p
Adjusted net asset value per equity share	93.47p

The net asset value adjusted to reflect the market value of the financial liabilities and preference shares is 97.01p.

### 24 Commitments and contingencies

Edinburgh Income and Value Trust plc ('EIVT') has entered into a subscription agreement with Edinburgh Value Zeros plc ('EVZ') in which EIVT has agreed, subject to certain conditions, to subscribe in aggregate for sufficient ordinary shares in EVZ and at such prices, that will result in the assets of EVZ being sufficient to satisfy the capital entitlement on 31 May 2005 of 159.63p per share of 15,520,000 EVZ zero dividend preference shares (or the capital entitlement accrued prior to that date).



## Notice of Meeting

Notice is hereby given that the first Annual General Meeting of Edinburgh Income and Value Trust plc will be held at Donaldson House, on 30 August 2000 at 12 noon, for the following purposes:

### ORDINARY BUSINESS

1. To receive the Report of the Directors and the Accounts for the period to 31 May 2000;
2. To elect David Ritchie as a director of the company;
3. To elect Sir Donald MacKay as a director of the company;
4. To elect Francis Malcolm as a director of the company;
5. To elect David Simpson as a director of the company;
6. To elect Douglas Smith as a director of the company;
7. To appoint Ernst & Young as auditors of the company; and
8. To authorise the directors to fix the remuneration of the auditors for the year to 31 May 2001.

### Notes:

1. Holders of ordinary shares are entitled to attend and vote at the meeting.

Members must be entered on the company's register of members 48 hours before the time appointed for the meeting. If the meeting is adjourned for more than 48 hours then, for members to be entitled to vote, they must be entered on the company's register of members 48 hours prior to the time fixed for the adjourned meeting. Any such holder may appoint another person (whether a member of the company or not) as his proxy to attend and vote on a poll in his stead. Proxies must be lodged at the company's registrar, Lloyds TSB Registrars Scotland, 117 Dundas Street, Edinburgh EH3 5ED not less than 48 hours before the time appointed for the meeting. Completion of a form of proxy will not prevent a holder of ordinary shares from attending or voting in person should he so wish.

2. There are special arrangements for holders of shares through The Edinburgh Fund Managers Investment Trust Savings Plan, Investment Trust ISA/PEP and Investment Trust Pension. These are explained in the 'Letter of Directions' which such holders will have received with this report.

By order of the board

*Valerie Mackenzie*

**Edinburgh Fund Managers plc**

Secretary

28 July 2000

Registered office:

Donaldson House, 97 Haymarket Terrace,  
Edinburgh EH12 5HD



## Financial Calendar

Announcements, ordinary share dividend payments and the issue of the annual and interim reports may normally be expected in the following months:

**July**– Preliminary figures and fourth interim dividend for year announced. Annual report and accounts published.

**August**– Fourth interim dividend paid. Annual General Meeting.

**October**– First interim dividend paid.

**January**– Interim figures announced and second interim dividend paid. Interim report for half-year to 30 November published.

**April**– Third interim dividend paid.

This year's Annual General Meeting will be held at Donaldson House, 97 Haymarket Terrace, Edinburgh on Wednesday 30 August at 12 noon followed by a buffet lunch. Shareholders are asked to reply on the enclosed card if they will be attending the meeting.



The Company is a member of The Association of Investment Trust Companies.

