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## **EDINBURGH SMALL COMPANIES TRUST**

Edinburgh Small Companies Trust plc, the investment trust with an investment objective to achieve long term capital growth by investing in small UK quoted companies mainly with a market capitalisation below £150 million, announces its preliminary results for the year ended 30 June 2002.

### **PRELIMINARY RESULTS FOR THE YEAR ENDED 30 JUNE 2002**

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*Please note that past performance is not necessarily a guide to the future and that the value of investments and the income from them may fall as well as rise. Investors may not get back the amount they originally invested.*

## **EDINBURGH SMALL COMPANIES TRUST**

### **CHAIRMAN'S STATEMENT**

The environment for investing in small companies has been extremely difficult throughout the period under review. In particular the fall in the share prices of a number of companies operating in the technology, media and telecoms (TMT) sectors has continued unabated for the second year running. Weakness has not been confined solely to TMT companies and concerns over the sustainability of long term earnings projections of other types of growth companies has resulted in an erosion of valuations. These factors would have had a negative impact on sentiment, but when combined with the volatility in markets following the terrorist attacks in the US and more recently the fallout from the financial scandals involving Enron and WorldCom, the impact on share prices of small UK growth companies has been severe.

#### **Performance**

The trust has a policy of investing in small companies which are chosen for their ability to produce above average long term growth in earnings per share. A significant percentage of the portfolio has been exposed to the TMT sector and other stocks which are regarded as growth companies. Whilst the policy has achieved above average returns on a number of occasions unfortunately it has not been successful over the past two years. The board has confidence that the policy will produce attractive returns to shareholders in the future.

Against this very difficult environment the gross assets of Edinburgh Small Companies have fallen by 36.2% from £157.3 million to £100.4 million. The company's policy of utilising long term gearing has led to a fall of 46.3% in the net asset value from 170.60p to 91.65p. In contrast our more broadly based benchmark, the extended Hoare Govett Smaller Companies Index, excluding investment trusts, declined by 15.6%.

The fall in the value of the company's assets not only reflects the portfolio's historically high exposure to the TMT sector and its strong bias towards growth sectors but also the above average weighting in other stocks in the financial sector which are very sensitive to the performance of stockmarkets. The portfolio has only a limited exposure to companies operating in mature industries which have proved to be more defensive in the current environment.

#### **Gearing**

The company's gearing is in the form of a £40 million long term debenture repayable in 2023. With cash and other types of short term interest bearing securities, totalling £27.2

million, net debt of £12.8 million at the end of June 2002 represented 26.3% of shareholder funds.

Throughout the year the level of net debt has fluctuated between 21.1% and 53.5%. The average level of gearing for the year was 34.3% and its use has contributed to a reduction of 19.6p in the net asset value.

At the beginning of the period gearing represented 29.4% of shareholder funds. Following the sharp falls in equity markets shortly after the terrorist attack on the US gearing rose to 53.5% due to the fall in shareholder funds. The lack of liquidity in many of our investments made it impossible to raise cash quickly while it was also not desirable to have to sell shares with good prospects. As a result the board agreed a strategy with the manager to raise cash over a period of time to return gearing to below 25%.

Whilst the board continue to believe that gearing can enhance returns to ordinary shareholders over the longer term the sharp fall in the value of assets during September pushed the gearing ratio to uncomfortable levels. The board has reviewed its policy on gearing and has agreed various controls which, in the absence of extreme circumstances, are designed to try to reduce the likelihood of gearing rising to excessive levels in future.

#### Revenue Account

Investment income has fallen from £2.343 million to £1.922 million due mainly to several dividend cuts. A number of expenses are also below the previous year's, which partly compensates for the fall in revenue. The principal reduction is the lower management fee payable to Edinburgh Fund Managers which has fallen from £2.166 million to £1.302 million to reflect the lower value of investments. Half of this fee is chargeable against revenue received. For the year, the loss per share is 0.49p compared to a loss of 0.34p for the previous year.

The board is proposing to pay an unchanged dividend of 0.75p from accumulated revenue reserves. If approved the final dividend will be paid on 25 October 2002 to shareholders on the register at close of business on 4 October 2002.

Following the payment of the dividend the company will have revenue reserves of 1.19p.

### Share and Warrant Buybacks

During the year 2.2m shares were bought back for cancellation at a discount of 24.6% to the underlying net asset value. The transaction enhanced the net asset value by approximately 1.2p per share. No warrants were purchased by the company during the year.

The board is seeking permission from shareholders to renew the authority to purchases up to 14.99% of the shares in issue.

### Marketing Initiatives

The board continues to promote the company through the Edinburgh Fund Managers Investment Trust Initiative which provides a range of savings products, including ISA, Pension Scheme and PEP Transfers in a cost effective manner. Shareholders can receive up to date information on recent performance and the trust's strategy on the manager's website, [www.edfd.com](http://www.edfd.com).

### Prospects

The volatility in stockmarkets has continued into the new financial year with the UK stockmarket in particular falling to a six year low before staging a recovery.

The prospects for the UK stockmarkets are very much dependent on global events and in particular a sustained recovery in the US economy. Whilst the financial scandals involving Enron and WorldCom have clearly shaken confidence signs are emerging that the US economy is beginning to respond to the easing of interest rates throughout last year.

After over two years of falling share prices the valuations of many of the small companies in our portfolio have fallen to levels which do not reflect their longer term growth prospects. Provided these growth prospects are realised the recovery potential of many of these companies is likely to be substantial.

## STATEMENT OF TOTAL RETURN

<b><u>for the year ended 30 June 2002</u></b> (audited)	<b>Revenue £000</b>	<b>Capital £000</b>	<b>Total £000</b>
Realised net losses on investments	-	(8,683)	(8,683)
Unrealised net losses on investments	-	(42,654)	(42,654)
<b>TOTAL CAPITAL LOSSES ON INVESTMENTS</b>		<b>(51,337)</b>	<b>(51,337)</b>
Investment Income	<b>1,922</b>	-	<b>1,922</b>
Interest receivable	<b>205</b>	-	<b>205</b>
Other income	<b>21</b>	-	<b>21</b>
Investment management fee	<b>(651)</b>	<b>(651)</b>	<b>(1,302)</b>
Administrative expenses	<b>(305)</b>	-	<b>(305)</b>
<b>Net return before finance costs and taxation</b>	<b>1,192</b>	<b>(51,988)</b>	<b>(50,796)</b>
Interest payable and similar charges	<b>(1,524)</b>	<b>(1,524)</b>	<b>(3,048)</b>
<b>Return on ordinary activities before taxation</b>	<b>(332)</b>	<b>(53,512)</b>	<b>(53,844)</b>
Taxation	-	-	-
<b>Return on ordinary activities after taxation</b>	<b>(332)</b>	<b>(53,512)</b>	<b>(53,844)</b>
Dividends in respect of equity shares	<b>(489)</b>	-	<b>(489)</b>
Transfer from reserves	<b>(821)</b>	<b>(53,512)</b>	<b>(54,333)</b>
Return per ordinary share	<b>(0.49p)</b>	<b>(78.74p)</b>	<b>(79.23p)</b>
Diluted return per ordinary share	<b>(0.49p)</b>	<b>(78.74p)</b>	<b>(79.23p)</b>
Dividends per ordinary share	<b>0.75p</b>	-	<b>0.75p</b>

**STATEMENT OF TOTAL RETURN****for the year ended 30 June 2001 (audited)**

	<b>Revenue £000</b>	<b>Capital £000</b>	<b>Total £000</b>
Realised net gains on investments	-	<b>14,282</b>	<b>14,282</b>
Unrealised net losses on investments	-	<b>(68,440)</b>	<b>(68,440)</b>
<b>TOTAL CAPITAL LOSSES ON INVESTMENTS</b>		<b>(54,158)</b>	<b>(54,158)</b>
Investment Income	<b>2,343</b>	-	<b>2,343</b>
Interest receivable	<b>220</b>	-	<b>220</b>
Other income	<b>10</b>	-	<b>10</b>
Investment management fee	<b>(1,083)</b>	<b>(1,083)</b>	<b>(2,166)</b>
Administrative expenses	<b>(276)</b>	<b>(2)</b>	<b>(278)</b>
<b>Net return before finance costs and taxation</b>	<b>1,214</b>	<b>(55,243)</b>	<b>(54,029)</b>
Interest payable and similar charges	<b>(1,449)</b>	<b>(1,421)</b>	<b>(2,870)</b>
<b>Return on ordinary activities before taxation</b>	<b>(235)</b>	<b>(56,664)</b>	<b>(56,899)</b>
Taxation	<b>(2)</b>	-	<b>(2)</b>
<b>Return on ordinary activities after taxation</b>	<b>(237)</b>	<b>(56,664)</b>	<b>(56,901)</b>
Dividends in respect of equity shares	<b>(522)</b>	-	<b>(522)</b>
Transfer from reserves	<b>(759)</b>	<b>(56,664)</b>	<b>(57,423)</b>
Return per ordinary share	<b>(0.34p)</b>	<b>(81.43p)</b>	<b>(81.77p)</b>
Diluted return per ordinary share	<b>(0.33p)</b>	<b>(79.88p)</b>	<b>(80.21p)</b>
Dividends per ordinary share	<b>0.75p</b>	-	<b>0.75p</b>

**BALANCE SHEET**  
**(audited)**

	At 30 June 2002 £000	At 30 June 2001 £000
<b>Fixed assets</b>		
Investments	78,032	153,601
<b>Current assets</b>	30,290	8,905
<b>Current liabilities</b>	6,548	3,763
<b>Net current assets</b>	23,742	5,142
	101,774	158,743
<b>Creditors: amounts falling due after more than one year</b>	41,405	41,474
	60,369	117,269
<b>Capital and reserves</b>		
Called up share capital	16,851	17,400
Reserves	43,518	99,869
<b>Total equity shareholders' funds</b>	60,369	117,269
Adjusted net asset value per share	<u>91.65p</u>	<u>170.60p</u>
Fully diluted net asset value per share	<u>N/A</u>	<u>167.66p</u>

**CASHFLOW STATEMENT**  
**(audited)**

	For the year ended 30 June 2002 £000	For the year ended 30 June 2001 £000
Net cash inflow from operating activities	522	190
Net cash outflow from servicing of finance	(3,100)	(2,737)
Total tax paid	-	-
Net cash inflow from capital expenditure and financial investment	24,360	(1,871)
Equity dividend paid	(505)	(522)
Management of Liquid Resources	(23,967)	-
Net cash outflow from financing	(2,567)	10,645
 DECREASE IN CASH	 <u>(5,257)</u>	 <u>5,705</u>

**NOTES:**

1. The accounts are prepared under the same accounting policies used for the year to 30 June 2001.
2. The financial information for the year ended 30 June 2001 has been extracted from the Annual Report and Accounts of the company, which have been filed with the Registrar of Companies and contained an unqualified auditors' report. The statutory accounts for 2002 are unqualified and will be delivered to the Registrar of Companies following the company's Annual General Meeting which will be held at the registered office of the company, Donaldson House, 97 Haymarket Terrace, Edinburgh, EH12 5HD on Thursday 24 October 2002 at 11.00am.
3. The statement of total return (incorporating the revenue account) and balance sheet set out above do not represent full accounts in accordance with Section 240 of the Companies Act 1985.
4. The investment management fee in each case includes irrecoverable VAT calculated at 17.5%.
5. The final dividend, subject to shareholder approval, will be paid on 25 October 2002 to shareholders on the register at the close of business on 4 October 2002. The ex-dividend date is 2 October 2002.
6. The Annual Report will be posted to shareholders on 12 September 2002 and copies will be available from the registered office of the company.

For Edinburgh Small Companies Trust plc  
Edinburgh Fund Managers plc, Secretary  
Amanda Fraser  
Company Secretary  
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