

HERALD INVESTMENT TRUST plc

REPORT & ACCOUNTS

31 December 2004

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COMPANY SUMMARY

COMPANY DATA AT 31 DECEMBER 2004

Total assets†	Shareholders' funds	Market capitalisation
£361m	£337m	£283m

† before deduction of bank loan.

Policy and Objective Herald's objective is to achieve capital appreciation through investments in smaller quoted companies, in the areas of communications and multi-media. Investments will be made throughout the world. The business activities of investee companies will include information technology, broadcasting, printing and publishing and the supply of equipment and services to these companies.

Benchmark The portfolio benchmark against which performance is measured is $\frac{2}{3}$ Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies) and $\frac{1}{3}$ Russell 2000 (small cap) Technology Index (in sterling terms).

Management Details Herald Investment Management Limited ('HIML') is the appointed investment manager to the Company. The management contract can be terminated at twelve months' notice. Administration of the Company and its investments is contracted by HIML to Baillie Gifford & Co., who also act as Company Secretary.

Capital Structure The Company's share capital consists of 87,556,010 ordinary shares of 25p each which are issued and fully paid.
The Company has been granted authority to buy back a limited number of its own Ordinary shares for cancellation. During the year the Company bought back 251,338 shares for cancellation.

Management Fee Herald Investment Management Limited's annual remuneration is 1.0% of the Company's net asset value, calculated on a monthly basis payable in arrears.

Wind-Up At the Annual General Meeting of the Company held in April 2004 shareholders voted in favour of the Company continuing to operate as an investment trust. The next continuation vote is in 2007 and every third year thereafter.

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

None of the views expressed in this document should be construed as advice to buy or sell a particular investment.

Investment trusts are UK public listed companies and are not authorised or regulated by the Financial Services Authority.

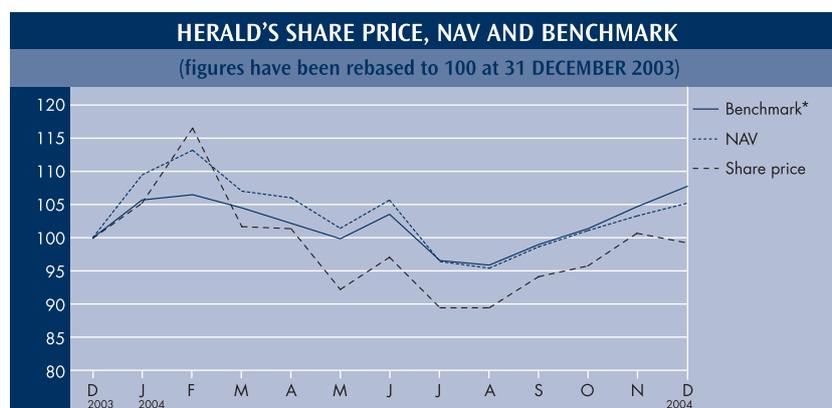
YEAR'S SUMMARY

	31 December 2004	31 December 2003	% change
Total assets (before deduction of bank loans)	£361.2m	£350.2m	
Bank loans	£24.7m	£29.3m	
Equity shareholders' funds	£336.6m	£320.9m	4.9
Net asset value per ordinary share	384.4p	365.4p	5.2
Share price	322.8p	325.3p	(0.8)
FTSE 100	4,814.3	4,476.9	7.5
FTSE All-Share	2,410.8	2,207.4	9.2
FTSE Small Cap	2,758.2	2,475.1	11.4
Hoare Govett Smaller Companies Index <small>(extended capital gains ex. investment companies)</small>	2,752.2	2,346.7	17.3
Russell 2000 (small cap) Technology Index <small>(in sterling terms)</small>	65.1	72.9	(10.7)
Benchmark composite index			7.5
Dividend per ordinary share	0.30p	0.30p	–
Earnings per ordinary share	0.34p	0.32p	6.3
Expense ratio	1.20%	1.20%	
Discount	(16.0%)	(11.0%)	

	Year to 31 December 2004		Year to 31 December 2003	
Year's high and low (on month end values)	High	Low	High	Low
Share price	379.5p	291.0p	325.5p	160.5p
Net asset value	413.2p	348.6p	366.0p	193.4p
Discount	(8.2%)	(19.0%)	(8.1%)	(15.4%)

	31 December 2004	31 December 2003
Total return per ordinary share		
Revenue	0.34p	0.32p
Capital	18.68p	161.39p
Total	19.02p	161.71p

Past performance is no guarantee of future performance.



Source: Thomson Financial Datastream.

*2/3 Hoare Govett Smaller Companies Index (extended capital gains ex. investment companies) and 1/3 Russell 2000 (small cap) Technology Index (in sterling terms).

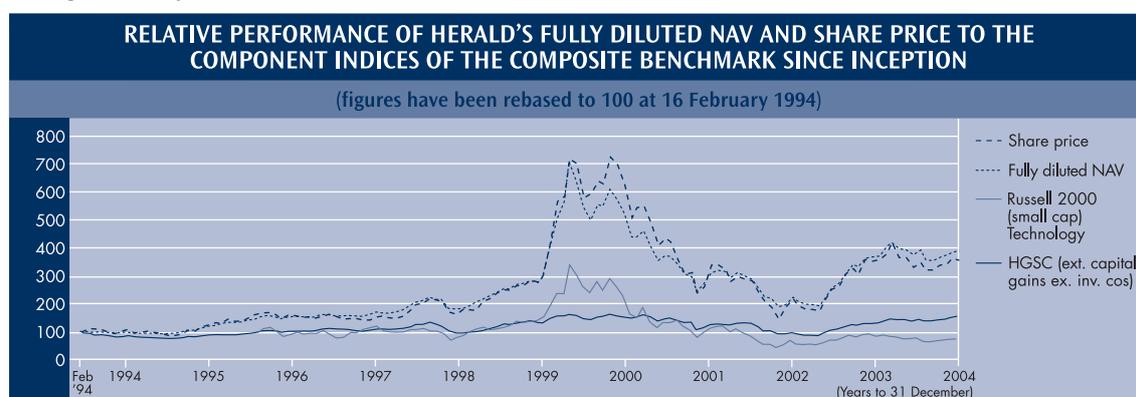
Dividends are not reinvested.

LONG TERM PERFORMANCE SUMMARY

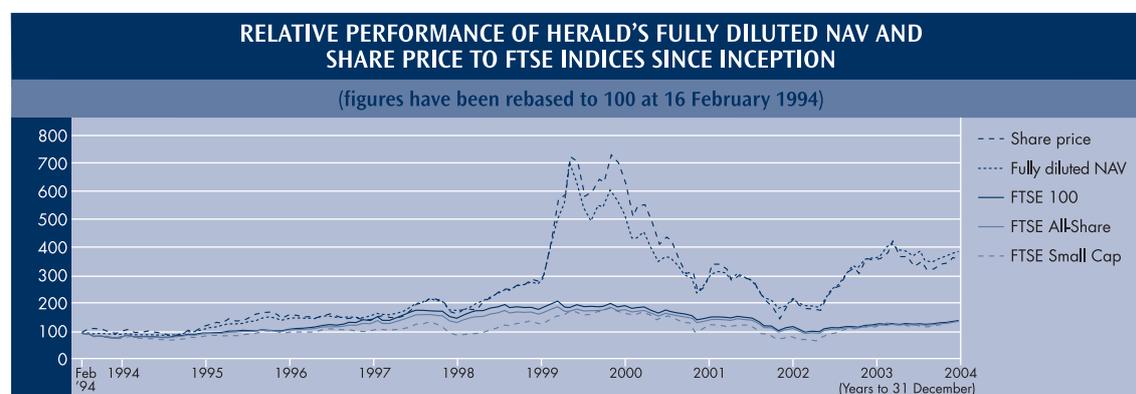
The following charts indicate how an investment in Herald has performed relative to its comparative indices (applied retrospectively) and its underlying fully diluted net asset value over the period since inception of the Company.

	31 December 2004	Inception 16 February 1994	% change
Net asset value per ordinary share	384.4p	98.7p	289.5
Share price	322.8p	90.9p	255.1
Hoare Govett Smaller Companies Index <small>(extended capital gains ex. investment companies)</small>	2,752.2	1,750.0	57.3
Russell 2000 (small cap) Technology Index <small>(in sterling terms)</small>	65.1	83.2*	(21.8)
FTSE 100	4,814.3	3,417.7	40.9
FTSE All-Share	2,410.8	1,717.8	40.3
FTSE Small Cap	2,758.2	2,076.1	32.9

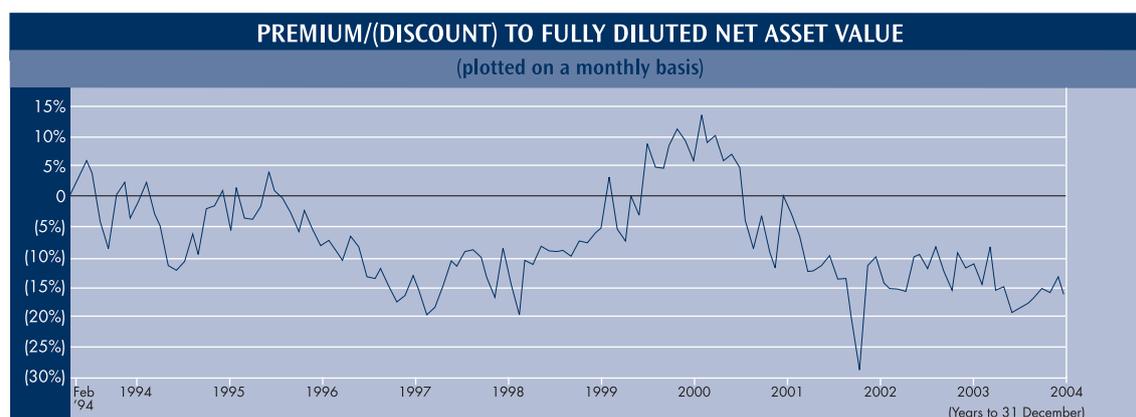
* at 9 April 1996, being the date funds were first available for international investment.



Source: Thomson Financial Datastream



Source: Thomson Financial Datastream



Source: Thomson Financial Datastream

The premium/(discount) is the difference between Herald's quoted share price and its underlying fully diluted net asset value.

DIRECTORS, MANAGER AND ADVISERS

Directors

Martin Boase, MA, FIPA (Chairman), aged 72, was appointed to the Board on 11 January 1994 and is Chairman of the Audit Committee and the Nomination Committee. He formed advertising agency Boase Massimi Pollitt plc in 1968 which was floated on the London Stock Exchange in 1983. He was chairman of the Advertising Association from 1987 to 1992 and is currently chairman of The Maiden Group plc, The Investment Trust of Investment Trusts PLC and Jupiter Dividend and Growth Investment Trust PLC.

Clay Brendish, CBE, aged 57, was appointed to the Board on 23 July 2001. He has been Non-Executive Chairman of Beacon Investment Fund since 1995 and Echo Research Limited since July 2003. He is a trustee of the Economist Newspapers Limited together with the Foundation for Liver Research and became a council member of the City University of London in July 2000. Clay's other Non-Executive Directorships are of British Telecommunications plc, Elexon Limited, the Defence Logistics Organisation (DLO) and the Defence Communication Services Agency (DCSA) Owners Advisory Board. He has been in the computer systems environment and high technology industry for over 30 years. He was formerly Executive Chairman of Admiral plc and, in turn, Deputy Chairman of CMG plc when the companies merged. He has also held a number of Government advisory posts.

Tim Curtis, aged 62, was appointed to the Board on 22 July 2004. He was Chief Executive of Zetex plc (formerly Telemetrix PLC) and is Non-Executive Chairman of RaceCourse Technical Services Ltd. Former Non-Executive Directorships were with TVS Entertainment plc, Dobson Park Industries plc, Bournemouth & West Hampshire Water Co., and Pace Micro Technology plc. Tim was previously a Director of Unitech plc and Director and Chairman of Metrologie UK.

Justin Dukes, aged 63, was appointed to the Board on 11 January 1994. He is chairman of ECIC Management Limited and Intelfax Limited and is a director of VTR plc. He was the founding managing director of Channel Four Television and joint managing director of the Financial Times Group. He is a former president of the Institute of Information Scientists and is a Companion of the Institute of Management.

Douglas McDougall, OBE, aged 60, was appointed to the Board on 13 February 2002 and is the senior independent director. He has extensive experience in the fund management industry and is a former senior partner of Baillie Gifford & Co. He is chairman of The Law Debenture Corporation plc, Foreign & Colonial Eurotrust PLC, The Independent Investment Trust PLC, The Scottish Investment Trust PLC and 3i Bioscience Investment Trust plc and is a director of The Monks Investment Trust PLC and Pacific Horizon Investment Trust PLC. He is a former chairman of IMRO, of the Association of Investment Trust Companies and of the Fund Managers' Association.

Clive Parritt, FCA, FIIA, aged 61, was appointed to the Board on 10 December 1993. He is a chartered

accountant with over 25 years' experience of providing strategic, financial and commercial advice to medium sized businesses. He has a particular interest in the multi-media arena having led the media team at Baker Tilly, Chartered Accountants. Until February 2001 he was also chairman of Baker Tilly having been its national managing partner for ten years until June 1996. He is a member of the Council of the Institute of Chartered Accountants in England and Wales, chairman of Baronsmead VCT2 plc and BETon SPORTS plc. Previously he has been a director of a number of investment trusts, VCTs and media businesses.

All Directors are members of the Audit and Nomination Committees.

Secretary

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

Registered Office

12 Charterhouse Square
London EC1M 6AX

Company Number

2879728 (England and Wales)

Manager

Herald Investment Trust plc is managed by Herald Investment Management Limited (HIML). The senior director of HIML with prime responsibility for the management of Herald Investment Trust is Katie Potts.

Katie Potts

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CHAIRMAN'S STATEMENT

2004 has seen modest progress with the net asset value per share rising 5.2%. Somewhat disappointingly, the performance has lagged the FTSE 100, which rose 7.5% and the Hoare Govett Smaller Companies Index, which grew 17.3%. However, over the history of the Trust the net asset value has grown 289.5% over a period when the FTSE 100 rose only 40.9%. In this context, to have underperformed the FTSE by 2.3% is not unsatisfactory in a year when Herald's target sectors have performed poorly. The FTSE Information Technology Index, which is central to the portfolio, attained wooden spoon status by appearing bottom of the All Share Index table with a decline of 8.4%. The relevant sectors in the Hoare Govett showed a weighted average total return of 1.38%. The market in the US has been more difficult with the Russell 2000 Technology Index declining 4.3%, which translated to £ is a decline of 10.7%.

The most encouraging outcome of 2004 has been the outstandingly strong trading performance in the portfolio's companies. The aggregate increase in earnings in the portfolio in 2004, according to consensus estimates, was 90.4%. This far exceeds the return on the portfolio this year, but the strong performance in 2003 was clearly anticipating much of this growth. Consensus forecasts suggest similar profits growth of 67.6% in 2005. By value, more than two thirds of the portfolio has been consistently trading profitably. The P/E of these stocks in 2004 was 18.4x falling to 14.9x in 2005. A further 13.1% of the value of equities in the portfolio at the year-end is expected to have moved from losses in 2003 to profits in 2004. Expectations are for these profits to rise dramatically by 127.6% in 2005. Against this background, prospects for progress in 2005 are exceptionally promising.

In spite of the growth orientation of the portfolio, a fully invested position and a significant proportion of the portfolio not paying dividends, the Trust has remained profitable. This is after passing all expenses through the income account as always. Capital appreciation remains the primary objective.

The Trust became geared in 2002. These borrowings were rolled forward again in US\$ at a rate of 2.62% in October, but for much of the year similar levels of cash have been held in £. This has provided a useful currency hedge for the US\$ element of the portfolio.

The market for new issues re-emerged with a vengeance in the first half after two years of inactivity. The market was swamped by July, and the second half has been more sober in stock market terms in the sector. This, combined with cash withdrawals from the sector, such as the steady redemptions in specialist open-ended funds, has contributed to the de-rating during the year. Positively the speculators have moved on to the mining sector! Some acquisition activity has countered this at substantial premiums. More bid activity is expected in 2005. There continues to be favourable macro trends including the dramatic adoption of broadband Internet access by the consumer, albeit tempered by price competition in many parts of the sector. Economic growth is still expected in 2005 albeit at a more modest rate than 2004. More than ever this is a stock pickers market.

Clive Parritt and Justin Dukes have both served as Directors since the Trust was launched in 1994. Pressured by the regulatory environment and the Combined Code of Corporate Governance with the incumbent restrictions on Directors' tenure they have decided to stand down. I would like to thank them for their efforts over the years. I welcome Tim Curtis to the Board. He has recently retired as Chief Executive of Zetex, and brings an international knowledge in the semiconductor and telecommunications equipment sector. Shareholders will be asked to vote on his appointment at the Annual General Meeting.

Overall there has been a dichotomy this year between depressing macroeconomic and political news, which has understandably preyed on investors' minds, and exceptionally strong profits performance in the underlying portfolio. Happily this does provide an extremely solid base with which to look forward to 2005, as ever in the absence of unforeseen shocks.

Martin Boase

Chairman

17 February 2005

INVESTMENT MANAGER'S REPORT

Having enjoyed a return of 77.4% in 2003, the outcome for 2004 seems a little dull. The increase in net assets was only 5.2%. The widening of the discount led to an even duller return. Fortunately that masks very strong progress in a number of investee companies, with their aggregate forecast earnings per share effectively rising over 90%. I am surprised that this has not been reflected to a greater degree in share prices.

The 90%+ growth in earnings per share is a robust claim which requires explanation. The portfolio may be broken into four groups as follows:

Market value as % of total equities	UK	US	Europe	Far East	Total
Companies profitable in 2003 and 2004	47.7%	10.5%	5.9%	7.2%	71.3%
Companies unprofitable in 2003 profitable in 2004	8.6%	2.9%	1.4%	0.2%	13.1%
Companies unprofitable in 2003 and 2004	9.2%	1.6%	0.9%	–	11.7%
Missing Data (no available forecast)	2.0%	0.6%	0.4%	0.9%	3.9%
Total	67.5%	15.6%	8.6%	8.3%	100.0%
Earnings growth %					
2004: Companies always profitable (2003 and 2004)	13.5%	11.3%	48.6%	38.0%	18.8%
2005: Companies always profitable (2003 and 2004)	17.5%	22.7%	11.2%	21.4%	18.1%
2005: Companies unprofitable in 2003 and profitable in 2004	140.6%	113.4%	121.9%	(51.9%)	127.6%
Earnings growth %					
Total portfolio 2004*	73.1%	N/A	181.7%	49.1%	90.4%
Total portfolio 2005*	72.9%	83.1%	159.0%	20.3%	67.6%
P/E profitable stocks with estimates only					
2004	18.0x	32.6x	21.1x	10.6x	18.4x
2005	14.5x	24.0x	18.3x	8.7x	14.9x
P/E of all stocks with estimates					
2004	25.9x	59.4x	47.5x	10.6x	26.2x
2005	15.0x	29.6x	18.3x	8.7x	15.6x

*The calculation for 2004 and 2005 earnings growth is based only on companies with data available in each of the respective years.
Source: JCF Group and Company Brokers estimate

In all cases earnings growth is the growth of the aggregate earnings attributable to our holdings. The p/e is the market value of the holdings divided by the aggregate earnings. It should be noted that the overall growth is flattered by the number of companies which have moved from loss to profit, hence these companies have been shown separately. Some of the best returns have been achieved in these stocks. No companies in the portfolio are forecast to have gone from profit to loss.

The strong profits growth in 2004 reflects a return to more traditional business disciplines of cost control and cash generation. Profits growth will be harder to achieve now that those easy gains have been made, the labour market in the UK is tightening, the weak US\$ will adversely impact exporters and those with US\$ revenues, and it is difficult to see such strong growth in consumer spending in 2005. Nevertheless, economic growth continues, and a number of companies in the portfolio benefit from new products and immature markets.

Unfortunately I do not have historic data to quantify the proportion of the portfolio that was unprofitable in the past. The exercise to quantify it now was driven by awareness that there is an uncharacteristically high number of loss making shares in the portfolio, albeit less than a year ago. This is a direct result of many companies floating in the millennium bubble at an embryonic stage. Then many of the companies went into a valuation tailspin as investors extrapolated losses, but for a number sufficient cash was raised to see them to profitability. Positions in a number of these stocks were acquired in 2002. Furthermore there was a change in business attitude around the millennium where land grab and revenue growth was the business agenda for many companies. It is the companies which are just breaking into profit which can offer the greatest returns. This has been the case in 2004. The highest % returns have been from Thomson Intermedia (+405%), Group NBT (+181%), Nordic Semiconductor (+161%), RIT Technologies (+120%), Retail Decisions

INVESTMENT MANAGER'S REPORT *continued*

(+111%), DataCash (+106%) and Silicon Image (+105%). Retail Decisions and Silicon Image broke even in 2003 while the other five were loss making. The portfolio contains more stocks than it has in the past. We contend that these returns justify the proliferation of small holdings in higher risk situations. In particular the Trust owned 10% stakes in both Thomson Intermedia and NetBenefit (now Group NBT), which were at one stage trivial holdings, but have now both delivered worthwhile returns. It is at the smallest end of the market that inefficiencies appear, and it remains our aim to exploit these opportunities.

PERFORMANCE ATTRIBUTION (in sterling terms)									
Equity markets	Benchmark allocation		Herald asset allocation		Performance*		Contribution to relative return %	Contribution attributable to:	
	01.01.04 %	31.12.04 %	01.01.04 %	31.12.04 %	Herald %	Benchmark %		Stock selection %	Asset allocation† %
	UK	66.7	66.7	69.2	65.3	9.3		20.7	(6.4)
Europe ex. UK	–	–	6.5	7.1	21.1	–	0.5	–	0.5
Americas	33.3	33.3	19.4	15.9	(7.1)	(10.7)	4.0	0.6	3.3
Japan	–	–	0.7	0.8	(17.5)	–	(0.2)	–	(0.2)
Asia Pacific ex. Japan	–	–	7.5	7.5	(9.0)	–	(1.3)	–	(1.3)
Cash	–	–	5.8	10.7	4.2	–	(0.6)	–	(0.6)
Loans	–	–	(9.1)	(7.3)	(5.0)	–	1.2	–	1.2
Total	100.0	100.0	100.0	100.0	6.4	9.6	(3.0)	(6.0)	3.1

Past performance is no guarantee of future performance.

Source: HSBC.

*The above returns are calculated on a total return basis with net income reinvested. Dividends and interest are reinvested on a cash basis, unlike the NAV calculation where income is recognised on an accruals basis, relative performance may differ as a result.

Contributions cannot be added together, as they are geometric; for example, to calculate how a return of 6.4% (against a benchmark of 9.6%) translates into a relative return of (3.0%), divide the portfolio return of 106.4 by the benchmark return of 109.6 and subtract one.

† Asset allocation includes the contribution attributable to currency movements.

UK

The UK return was 9.3%. This was poor relative to the Hoare Govett Smaller Companies Index (extended) of 20.7%. However in 2004 the Trusts target sectors underperformed as follows:-

	Total return %	Weight in index	Weighted return %
Electronic and Electrical Equipment	10.4	2.45	1.75
Media and Entertainment	4.9	4.91	1.65
Telecommunication Services	(22.2)	1.11	(1.69)
Information Technology	(0.8)	6.09	(0.33)
Total		<u>14.56</u>	<u>1.38</u>

As already explained the feature of 2004 was the de-rating against a background of strong profits growth. In monetary terms the most profitable stocks were Thomson Intermedia, Linx Printing, which sadly was taken over after nine years of continuous ownership, Amstrad, SDL and ICM. The Trust's stakes in these companies were 9.6%, 9.7%, 8.1%, 9.1% and 6.1% respectively. The telecommunications exposure, though small overall, proved expensive.

AIM has been a source of new issues. There are now c1,000 companies of which about a quarter operate within Herald's defined remit. We view this as an opportunity, but warn that many of these companies are early stage with minimal controls. There will be many disappointments so stock selection is more key than ever in this market.

INVESTMENT MANAGER'S REPORT *continued*

US

The US exposure is smaller than it has been. This reflects the less attractive valuations in the US. Although there are far more strong companies, in an economy which has continued to outperform, there are far more enthusiasts for growth companies than there are in the UK, which means paying higher prices. The management strengths in US companies remain awesome. The respect for intellectual property both in legal terms and in investment valuation terms places the US well for continuing to innovate.

The portfolio was flat in US\$ terms, which was around 4% ahead of our benchmark index the Russell 2000 Technology Index.

Europe

The small European portfolio has contributed usefully this year, +21%. This reflects the particularly strong return in Nordic Semiconductor and a useful contribution from ICOS Vision, a Belgian company and is the more pleasing when European returns have been minimal in the Herald remit. The Bloomberg European Biotechnology index – a sector in which Herald does not invest – grew by 22.6%. In contrast the European semiconductor index declined 29.7%. It will be difficult for € based companies to compete with such a weak US\$. The European Media Index grew 12.9%.

Far East

The Far East portfolio has declined by around 7% in local currency, and worse in £ (-10.2%). There have been some useful returns on JASDAQ, but Japan is not our focus. The Tiger economies have been pressured by the weakness of the US\$. Korea has interesting technologies, but valuations are low reflecting corporate governance issues. The p/e of the Far East portfolio is lower, but companies generally are manufacturers who do not have the pricing power or leverage associated with higher margin software and media businesses more prevalent in the West, so we do not consider this anomalous.

Sarbanes-Oxley has been an immense drag on the corporate sector in the US this year. It is not uncommon for small companies to incur US\$1m of costs. In the orbit of small companies the regulatory environment is putting an immense burden on companies in both the US and to a slightly lesser extent the UK. It seems the environment has forgotten the primary purpose of trying to build strong companies. Instead too much energy is directed towards cutting the cake up fairly and not actually making it. The companies that need regulatory control are not the ones you want to invest in anyway!

Outlook

In an environment of low interest rates, and relatively low growth, the valuations in our sector look attractive, particularly in the UK. European exporters will be pressured by the strength of the Euro against the US\$, but as always stock selection is the key.

17 February 2005

INVESTMENT CHANGES (£'000)				
	Valuation at 31 December 2003	Net acquisitions (disposals)	Appreciation (depreciation)	Valuation at 31 December 2004
Equities*:				
UK	221,987	(19,565)	16,961	219,383
Continental Europe	21,012	(1,306)	4,048	23,754
Americas	62,419	(5,360)	(2,996)	54,063
Japan	2,139	1,088	(584)	2,643
Asia Pacific	23,940	4,207	(2,822)	25,325
Total investments	331,497	(20,936)	14,607	325,168
Net liquid assets	18,712	17,382	(29)	36,065
Total assets	350,209	(3,554)	14,578	361,233

The figures above for total assets comprise assets less current liabilities before deduction of bank loans.

*Equities includes convertibles, preference stock and warrants.

TOP TWENTY HOLDINGS

A brief description of the twenty largest holdings in companies is as follows:

Northgate Information Solutions

A leading supplier of applications and outsourcing solutions to the public sector, HR and corporate markets, with over 1,000 customers and 30 years' experience. Headquartered in Hemel Hempstead, Northgate has over 900 staff operating throughout the UK and in California, USA. In January 2004 Northgate announced the acquisition of the complementary Rebus HR Group for £150 million.

Country	United Kingdom
Valuation	£12,513,000
% of total assets	3.5
% of issued share capital held	3.9

Amstrad

Designs and manufactures consumer electronic products, notably the 'e-m@iler' and set-top satellite decoders for Sky including the new Sky Plus box. The 'e-m@iler' combines the functionality of a telephone with e-mail access. The new Sky Plus box targets the growth area of Personal Video Recorders (PVR). Its products are sold primarily in the UK.

Country	United Kingdom
Valuation	£10,745,000
% of total assets	3.0
% of issued share capital held	8.1

Imagination Technologies Group

The company develops 2D/3D graphics, digital signal processing, video and audio technologies and licenses this IP (Intellectual Property) to global semiconductor and system companies. These technologies are used in multimedia devices. Imagination has been a pioneer in developing Digital Audio Broadcasting Technology (DAB).

Country	United Kingdom
Valuation	£7,756,000
% of total assets	2.1
% of issued share capital held	6.4

Detica Group

A specialty provider of business consulting, systems design and implementation services. The Company focuses on helping organizations harness technology to identify, attract, develop and retain customers through effective integration with business processes. The Company is also a provider of information and systems security services, notably in the UK National Security market. Detica aims to combine independent advice with the design and delivery of effective solutions.

Country	United Kingdom
Valuation	£6,759,000
% of total assets	1.9
% of issued share capital held	3.9

SDL

Provides multilingual website globalisation software in addition to support databases, training and translation services. Its 'Realtime' and 'Workflow' are leading solutions in this field. Its comprehensive and integrated offerings include multilingual content management solutions, real-time translation technologies, translation memory and a full range of internationalization and localization services.

Country	United Kingdom
Valuation	£6,700,000
% of total assets	1.9
% of issued share capital held	8.9

Plasmon

Provides the industry's most comprehensive line of automated storage libraries, optical drives, disks, library storage management software and associated support services. Technologies include 5.25" Magneto Optical (MO), 12-inch TrueWORM, LTO-Ultrium/AIT Tape and 120mm DVD/CD technology. Plasmon has developed Ultra Density Optical (UDO) the next generation 5.25" professional optical storage technology, released during the latter stages of 2003. It is a convergent technology that delivers the performance of 5.25" MO, the longevity of 12-inch WORM, and the cost effectiveness of DVD.

Country	United Kingdom
Valuation	£6,461,000
% of total assets	1.8
% of issued share capital held	5.8

Diploma

A group of specialised distribution businesses serving industries with long-term growth potential and with the opportunity for sustainable superior margins through the quality of customer service, depth of technical support and value-adding activities. The three divisions are life sciences, seals and components, and interconnect.

Country	United Kingdom
Valuation	£5,751,000
% of total assets	1.6
% of issued share capital held	4.0

Incisive Media

A business-to-business magazine publisher in the financial, insurance and photography sectors. Titles include 'Investment Week', 'Risk', 'Insurance Age' and 'Waters'. Incisive also have a strong events business, enhanced by their May 2003 acquisition of Risk Waters.

Country	United Kingdom
Valuation	£5,476,000
% of total assets	1.5
% of issued share capital held	4.1

TOP TWENTY HOLDINGS *continued*

SurfControl

Its principal activity is the development of web and e-mail filtering and content management software. Its main brands were SurfControl Superscout which was sold to the corporate market and CyberPatrol which was directed at the education and home markets. SurfControl is now the single brand for all server based web and e-mail filtering products sold into the corporate and education markets. CyberPatrol is the brand for client-based products sold into the home market.

Country	United Kingdom
Valuation	£5,362,000
% of total assets	1.5
% of issued share capital held	3.2

ICM Computer Group

Offers a combination of IT solutions, IT support and Business Continuity services. It achieved public listing on the London Stock Exchange in May 1998. The Company has since grown from strength to strength, both organically and through acquisition. Operating from a network of support centres, strategically located throughout the UK, ICM has an impressive resource of skills and expertise and an excellent reputation for quality of service.

Country	United Kingdom
Valuation	£5,248,000
% of total assets	1.5
% of issued share capital held	6.1

Gresham Computing

Provides software for real time banking transactions and storage management. 'Real Time Nostro', jointly developed with Cable and Wireless, offers secure access to Nostro account information, providing real-time information that banks need to improve their liquidity management, reduce settlement risk and deliver value-added services. 'Real Time Integrated Banking' (RIBS) is a full-featured, end-to-end application providing complete transaction and customer self-service solutions for financial services providers. In addition to software products, Gresham provides bespoke software and consultancy services to over four hundred customers.

Country	United Kingdom
Valuation	£5,106,000
% of total assets	1.4
% of issued share capital held	3.7

Euromoney Institutional Investor

The Group's principal activity is business publishing that focuses primarily on international finance. It publishes more than 100 magazines, newsletters and journals as well as surveys, directories, books and maps. It also runs conferences, seminars and training courses and provides electronic business information through its capital market databases and emerging markets information services. Financial publishing accounted for 37% of fiscal 2003 revenues, conferences and seminars 22%, business publishing 20%, training 13% and databases and information services 9%.

Country	United Kingdom
Valuation	£4,718,000
% of total assets	1.3

Thomson Intermedia

Founded in 1997, as a response to a growing need by companies for a creative monitoring system that linked directly to expenditure. Driven by market requirements and their own desire to push forward the boundaries of media monitoring technology, the company grew at a phenomenal rate, floating on the stock exchange as an AIM listed company in 2000. To date, Thomson Intermedia Plc boasts over 500 of the UK's major advertisers as clients. Their media monitoring systems now cover Press, Television, Radio, Cinema, Direct Mail, Door Drops, Outdoor, and Internet-creative and expenditure-across all business sectors, making their systems the most comprehensive and technologically advanced in the world.

Country	United Kingdom
Valuation	£4,697,000
% of total assets	1.3
% of issued share capital held	9.6

Alphameric

The company is engaged in the supply of solutions to retail, leisure and financial organizations worldwide. With skills in a wide range of areas including consultancy, software development, business intelligence, project management, installation, support services and help desks, the Company provides solutions to organizations throughout Europe and the United States. Alphameric Retail offers products that can form part of a fully integrated system or operate independently in the areas of head office, in-store and business intelligence. Alphameric Leisure and Bookmaking supplies integrated systems and services covering the operational requirements of United Kingdom Licensed Betting Offices, including centrally controlled Display, Slip Capture and EPoS Systems. Alphameric Finance provides solutions covering the digital distribution of corporate information via satellite to the provision of private television networks for financial organizations.

Country	United Kingdom
Valuation	£4,441,000
% of total assets	1.2
% of issued share capital held	4.7

TOP TWENTY HOLDINGS *continued*

Linx Printing Technologies

Linx has leading global positions in the two main non-contact coding and marking technologies: continuous inkjet printing and laser coding. Linx continuous inkjet printers operate at extremely high production-line speeds, directing 80,000 drops of fast-drying ink per second on all sorts of surfaces, e.g. Linx continuous inkjet printers can print a sell-by date on up to 2,000 beverage cans per minute. As it is permanent, laser coding is favoured by makers of prestige products, such as champagne, where it helps protect against counterfeiting.

Country	United Kingdom
Valuation	£3,999,000
% of total assets	1.1
% of issued share capital held	4.7

Scottish Radio Holdings

Founded in 1973, Scottish Radio Holdings has become the leading Scottish broadcaster, and also enjoys a high profile in Northern Ireland. It partly or wholly owns 16 radio stations, including Radio Clyde, Radio Forth, Carlisle Radio and Today FM. And that is not all – the group also runs the press agency Score Press, which publishes various weekly newspapers (33 in all), such as Bute Newspaper, the Leitrim Observer and the Montrose Review. Then there is Score Outdoor, which manages a total of 4,000 advertising boards, rented out to advertisers. Aware of the rapidly-evolving technological landscape, Scottish Radio Holdings Plc has kept up with change. It has thus developed a website for each of its radio stations, providing news, programmes and soundtracks, among other things.

Country	United Kingdom
Valuation	£3,838,000
% of total assets	1.1

Acal

A leading value-added distributor providing specialist design-in, sales and marketing services for international suppliers in the fields of Electronic Components, IT Products, IT Parts Services and Industrial Controls. The Group, which has 24 principal trading companies, eleven in Continental Europe, eleven in the UK, one in the USA and one in Australia, employs approximately 980 people with particularly strong technical sales and marketing expertise.

Country	United Kingdom
Valuation	£3,780,000
% of total assets	1.0
% of issued share capital held	4.0

Taylor Nelson Sofres

Following the acquisition of NFO in July 2003 for \$425m, TNS is the third largest market information group in the world. It operates an international network in more than 50 countries and provides market information services in over 80 countries to national and multi-national organisations. Its principal areas of activity are Consumer, Media, Business Services, Healthcare and IT/Telecoms. Approximately half of TNS' revenue is derived from continuous research projects and access panels, bolstered by the NFO acquisition, with the balance derived from customised research.

Country	United Kingdom
Valuation	£3,764,000
% of total assets	1.0

Alterian

A global provider of Database Marketing and Customer Insight solutions which help blue-chip organizations to improve the effectiveness of their marketing activity. Alterian provides innovative software and a unique business relationship to Marketing Service Providers which enables them to deliver closed loop Database Marketing solutions to their clients. With 80 employees and international headquarters in Bristol, UK, and North American headquarters in Chicago, Alterian has a further four satellite offices in Boston, New York, Salt Lake City and Toronto. Alterian also has a Master Reseller based in Barcelona. Alterian's network of over 50 partners include: infoUSA, Carlson Marketing, Omnicom Group, CFM Direct, CC3, Experian, GB Group, DataForce Group and Euro RSCG Worldwide, which all deliver industry leading database marketing solutions based on Alterian technology.

Country	United Kingdom
Valuation	£3,536,000
% of total assets	1.0

Nordic Semiconductor

Formerly Nordic VLSI ASA, is a semiconductor company specialising in design solutions at the microchip level in the areas of wireless communication and multimedia. The company is a world leader in high-speed data converters and short-range radio communication.

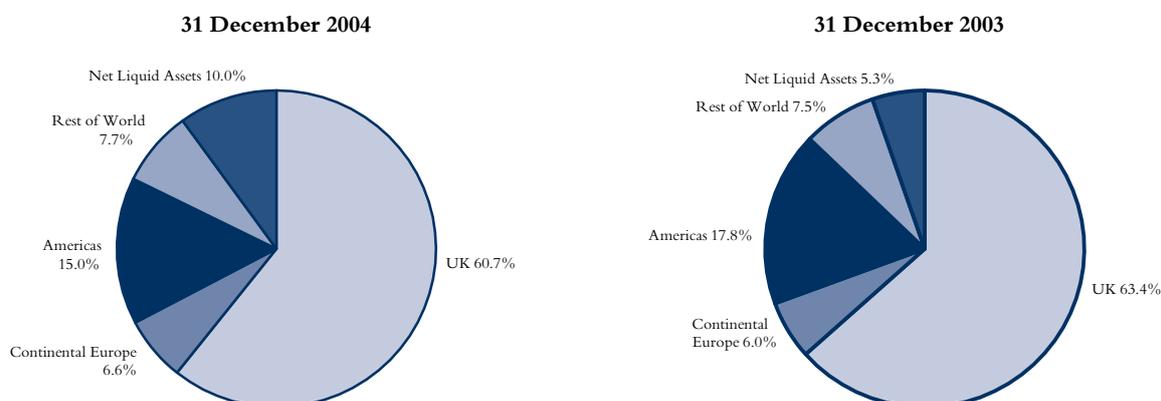
Country	Norway
Valuation	£3,405,000
% of total assets	0.9

Note: A figure is presented for % of issued share capital held only if greater than 3%.

CLASSIFICATION OF INVESTMENTS

Classification	Continental					2004 Total %	2003 Total %
	UK %	Europe %	Americas %	Japan %	Asia Pacific %		
EQUITIES: (including convertibles, preference stock and warrants)							
INDUSTRIALS	6.8	0.8	1.7	0.6	3.7	13.6	12.0
Chemicals	–	–	–	0.1	–	0.1	–
Electronic and electrical equipment	6.8	0.8	1.7	0.3	2.7	12.3	12.0
Engineering and machinery	–	–	–	0.2	1.0	1.2	–
CONSUMER GOODS	0.8	–	0.2	–	–	1.0	1.3
Healthcare and pharmaceuticals	0.8	–	0.2	–	–	1.0	1.3
SERVICES AND UTILITIES	25.2	2.6	2.1	–	1.3	31.2	31.4
Distributors	4.2	–	0.2	–	0.3	4.7	5.0
Leisure and hotels	0.5	–	0.1	–	–	0.6	1.0
Media and entertainment	15.5	2.5	1.3	–	1.0	20.3	19.5
Support services	4.0	0.1	0.5	–	–	4.6	4.0
Telecommunication services	1.0	–	–	–	–	1.0	1.9
FINANCIALS	0.1	0.1	–	–	–	0.2	0.2
Speciality and other finance	0.1	–	–	–	–	0.1	0.1
Investment companies	–	0.1	–	–	–	0.1	0.1
INFORMATION TECHNOLOGY	27.8	3.1	11.0	0.1	2.0	44.0	49.8
Information technology hardware	6.2	2.2	5.4	0.1	1.6	15.5	18.3
Software and computer services	21.6	0.9	5.6	–	0.4	28.5	31.5
TOTAL EQUITIES (including convertibles, preference stock and warrants)	60.7	6.6	15.0	0.7	7.0	90.0	
Total equities – 2003 (including convertibles, preference stock and warrants)	63.4	6.0	17.8	0.6	6.9		94.7
NET LIQUID ASSETS	10.0	–	–	(0.1)	0.1	10.0	5.3
TOTAL ASSETS (before deduction of bank loans)	70.7	6.6	15.0	0.6	7.1	100.0	
Total assets – 2003	68.6	6.0	17.8	0.6	7.0		100.0
BANK LOANS	–	–	(6.8)	–	–	(6.8)	(8.4)
EQUITY SHAREHOLDERS' FUNDS	70.7	6.6	8.2	0.6	7.1	93.2	
Equity shareholders' funds – 2003	68.6	6.0	10.2	(0.2)	7.0		91.6
Number of equity investments (including convertibles, preference stock and warrants)	119	23	73	5	33	253	243

GEOGRAPHICAL SPREAD OF INVESTMENTS



DETAILED LIST OF INVESTMENTS

AT 31 DECEMBER 2004

Classification	Name	Market value £'000	%
UNITED KINGDOM			
Electronic and electrical equipment	Alba	3,136	
	Amstrad	10,745	
	†Andor Technology	273	
	†Bright Things	417	
	†Innovision Research & Technology	2,728	
	Intelek	581	
	Linx Printing Technologies	3,999	
	†OMG	1,098	
	†TRL Electronics	1,778	
		24,755	6.8
Healthcare and pharmaceuticals Distributors	Biotrace International	2,765	
	Abacus Group	1,579	
	Acal	3,780	
	Deltron Electronics	1,049	
	Diploma	5,751	
	†Netcentric Systems Northamber	15 2,928	
		15,102	4.2
Leisure and hotels Media and entertainment	†ukbetting	1,903	
		2,160	0.5
	Aegis Group	268	
	†Alibi Communications	1,079	
	Applied Optical Technologies	3,030	
	Bloomsbury Publishing	89	
	†Campus Media	660	
	Capital Radio	2,514	
	Chime Communications	1,588	
	†Eckoh Technologies	4,718	
	Euromoney Institutional Investor	927	
	†Expomedia Group	5,476	
	Incisive Media	504	
	Independent Media Distribution	505	
	†Independent Media Support Group	1,355	
	Johnston Press	2,032	
	†Local Radio Company	426	
	†M & C Saatchi	2,258	
	Metal Bulletin	279	
	Music Choice Europe	895	
	Pinewood Shepperton	3,214	
	§Quarto Group	3,838	
	Scottish Radio Holdings	412	
	†Screen Fx	546	
	†SP Holdings	878	
	SPG Media	2,643	
	T & F Informa	3,764	
	Taylor Nelson Sofres	1,875	
	†Ten Alps Communications	845	
†Touch Group	1,549		
†UBC Media Group	1,328		
†WILink	3,394		
Wilmington Group	894		
†Yoomedia	16		
†Zyzygy	55,959	15.5	
Support services	†Group NBT	1,678	
	Harvey Nash Group	783	
	†hotgroup	745	
	Lorien	971	
	†Maintel Holdings	579	
	Mice Group	987	
	‡†Mondas	732	
	†Moneybox	2,010	
	PSD Group	406	
	†Thomson Intermedia	4,697	
	†United Clearing	648	
†Xpertise Group	155		
		14,391	4.0

DETAILED LIST OF INVESTMENTS *continued*

AT 31 DECEMBER 2004

Classification	Name	Market value £'000	%
Telecommunication services	Easynet Group	1,463	
	THUS Group	2,175	
		3,638	
Speciality and other finance	*Herald Investment Management Ltd	207	1.0
	*Herald Venture 2	300	
	*HIML Jersey Ltd	–	
		507	0.1
Information technology hardware	CML Microsystems	900	6.2
	CSR	1,170	
	E2V Technologies	868	
	†ID Data	107	
	‡*ID Data 7%	1,000	
	Imagination Technologies Group	7,756	
	Plasmon	6,461	
	Roxboro Group	1,243	
	*UbiNetics	788	
	Zetex	2,220	
		22,513	
Software and computer services	Alphameric	4,441	21.6
	Alterian	3,536	
	†Atlantic Global	125	
	†Attentiv Systems Group	1,527	
	†Clarity Commerce Solutions	787	
	Clinical Computing	134	
	†Corpora	190	
	‡*Culver Holdings 8%	36	
	†DataCash Group	1,080	
	†Dealogic	864	
	Detica Group	6,759	
	Electronic Data Processing	1,476	
	†Empire Interactive	320	
	†Fayrewood	514	
	Gresham Computing	5,106	
	†Harrier Group	449	
	ICM Computer Group	5,248	
	†IDOX	1,632	
	†IMS Maxims	34	
	†INCAT International	801	
	Intec Telecom Systems	794	
	†InTechnology	513	
	†Intelligent Environments Group	625	
	†Interactive Digital Solutions	312	
	†IQ-Ludorum	58	
	†Manpower Software	766	
	Marlborough Stirling	2,538	
	†Matrix Communications Group	744	
	†Maxima Holdings	548	
	Northgate Information Solutions	12,513	
	†OneClickHR	251	
	†Patsystems	784	
	Phoenix IT Group	2,740	
	Retail Decisions	1,496	
	RM	1,171	
	SDL	6,700	
	ServicePower Technologies	493	
	†Smart Approach Group	479	
	†Statpro Group	536	
	SurfControl	5,363	
Trace Group	717		
†Zoo Digital Group	2,650		
	77,850	21.6	
	219,383	60.7	
TOTAL UNITED KINGDOM EQUITIES			

DETAILED LIST OF INVESTMENTS *continued*

AT 31 DECEMBER 2004

Classification	Name	Market value £'000	%
CONTINENTAL EUROPE			
Electronic and electrical equipment	Logitech International	2,865	0.8
Media and entertainment	Evs Broadcasting Equipment	732	
	Impresa SGPS	1,232	
	NRJ Group	2,836	
	PubliGroupe	1,117	
	Roularta Media Group	920	
	United Internet	2,260	
		9,097	2.5
Support services	Teleplan International	410	0.1
Investment companies	Inspire Investments	276	0.1
Information technology hardware	ICOS Vision Systems	2,578	
	LPKF Laser & Electronics	212	
	Nera	973	
	Nordic Semiconductor	3,405	
	SEZ	386	
	Suess Microtec	397	
		7,951	2.2
Software and computer services	*Atex Media Solutions	–	
	Ementor ASA	342	
	Horizon Technology Group	380	
	Iona Technolgies	789	
	Isra Vision System	545	
	Plaut	174	
	SkillSoft	118	
	Unit 4 Agresso	807	
		3,155	0.9
	TOTAL EUROPEAN EQUITIES	23,754	6.6
AMERICAS			
Electronic and electrical equipment	M-Systems Flash Disk Pioneers	1,541	
	Netgear	946	
	Pemstar	283	
	Power Integrations	206	
	Quantum Fuel Systems Technologies Worldwide	235	
	Remec	1,235	
	‡Reptron Electronics	142	
	Silicon Image	600	
	Sipex	402	
	Varian	534	
			6,124
Healthcare and pharmaceuticals	SonoSite	707	0.2
	Distributors	536	
	Jaco Electronics	187	
		723	0.2
Leisure and hotels	Pegasus Solutions	394	0.1
Media and entertainment	Emmis Communications	400	
	Harris Interactive	1,234	
	Hearst-Argyle Tv	1,374	
	Multivision Communications	1	
	SBS Broadcast	629	
	Scholastic	963	
		4,601	1.3
Support services	Computer Horizons	258	
	First Consulting Group	636	
	Wireless Facilities	737	
		1,631	0.5

DETAILED LIST OF INVESTMENTS *continued*

AT 31 DECEMBER 2004

Classification	Name	Market value £'000	%
Information technology hardware	Actel	1,122	
	Adaptec	988	
	Advanced Digital Information	1,044	
	Anadigics	586	
	Artisan Components	391	
	Asyst Technologies	504	
	ATMI	235	
	Brooks Automation	359	
	Ceva	465	
	Credence Systems	477	
	McData	310	
	Micros Systems	1,016	
	Moog	3,189	
	MRV Communications	1,797	
	Nova Measuring Instruments	289	
	On Track Innovations	721	
	Powerwave Technologies	795	
	Rimage	251	
	RIT Technologies	452	
	Safenet	1,148	
	Simpletech	839	
	Skyworks Solutions	982	
	Spectralink	591	
Stratex Networks	259		
Supertex	904		
		19,714	5.4
Software and computer services	Advent Software	1,067	
	At Road	504	
	Borland Software	608	
	Carreker	571	
	Centra Software	548	
	Datastream Systems	325	
	EPIQ Systems	1,068	
	HPL Technologies	15	
	I-many	402	
	INVU	936	
	Kronos	1,398	
	Macrovision	1,742	
	Manhattan Associates	398	
	Mentor Graphics	398	
	PDF Solutions	797	
	Pegasystems	444	
	Retalix	1,502	
	RSA Security	2,090	
	Seachange International	500	
	Serena Software	563	
	Sonic Solutions	1,753	
Sourcecorp	398		
THQ	657		
Vitria Technology	296		
Websense	1,189		
		20,169	5.6
	TOTAL AMERICAN EQUITIES	54,063	15.0
JAPAN			
Chemicals	Soken Chemical	443	0.1
Electronic and electrical equipment	Yamaichi Electronics	689	
	Yokowo	509	
		1,198	0.3
Engineering and machinery	Towa	543	0.2
Information technology hardware	Enplas	459	0.1
	TOTAL JAPANESE EQUITIES	2,643	0.7

DETAILED LIST OF INVESTMENTS *continued*

AT 31 DECEMBER 2004

Classification	Name	Market value £'000	%	
ASIA PACIFIC				
Electronic and electrical equipment	Action Asia	Singapore	211	
	Advantech Co	Taiwan	820	
	IDT International	Hong Kong	658	
	† Kingboard Chemicals Holdings	Hong Kong	882	
	Kiryung Electronics	Korea	448	
	LG Electronics	Korea	276	
	† Man Yue	Hong Kong	560	
	Merry Electronic	Taiwan	495	
	MFS Technology	Singapore	943	
	Norelco Centreline	Singapore	617	
	Phoenix PDE	Korea	642	
	Richtek Technology	Taiwan	569	
	Solomon Systech	Hong Kong	643	
	Starlight International	Hong Kong	395	
	Sunningdale Precision Industries	Singapore	1,687	
		9,846	2.7	
Engineering and machinery	First Engineering	Singapore	887	
	Hi-P International	Singapore	1,126	
	Meiban Group	Singapore	982	
	Taiwan Green Point Enterprise	Taiwan	618	
		3,613	1.0	
Distributors	Jadason Enterprises	Singapore	899	
Media and entertainment	Oriental Press Group	Hong Kong	950	
	Star Publications	Malaysia	2,600	
		3,550	1.0	
Information technology hardware	Gemtek Technology	Taiwan	1,146	
	GES International	Singapore	477	
	Globetronics Technology	Malaysia	652	
	Hana Microelectronics	Thailand	850	
	Huan Hsin Holdings	Singapore	671	
	KH Vatec	Korea	625	
	Simmtech	Korea	437	
	† Surface Mount Technology	Singapore	983	
			5,841	1.6
Software and computer services	Catuity	Australia	88	
	Infomedia	Australia	579	
	Reckon	Australia	909	
		1,576	0.4	
	TOTAL ASIA PACIFIC EQUITIES		25,325	7.0
	Value of equity stocks	322,763		
	Convertible preference stocks having an element of equity	605		
	Convertible loan stocks having an element of equity	1,724		
	Warrants having an element of equity	76		
	TOTAL EQUITY INVESTMENTS	325,168	90.0	
	NET LIQUID ASSETS	36,065	10.0	
	TOTAL ASSETS AT MARKET VALUE (before deduction of bank loan)	361,233	100.0	

(† denotes holding listed on AIM)

(* denotes unlisted security)

(‡ denotes holding wholly or partly in convertible loan stock)

(§ denotes holding wholly or partly in preference loan stock)

(¶ denotes holding wholly or partly in warrants)

TEN YEAR RECORD

CAPITAL								
At 31 December	Total assets £'000	Bank loans £'000	Equity shareholders' funds £'000	Net asset value per share p	Diluted net asset value per share† p	Share price p	Warrant price p	(Discount)/premium‡ %
1994	60,823	—	60,823	93.57	93.57	91.00	38.00	(2.7)
*1995	89,689	—	89,689	137.98	132.36§	127.00	55.00	(4.0)
1996	130,055	—	130,055	156.89	150.88§	136.00	61.00	(9.9)
1997	147,424	—	147,424	177.84	171.80	136.00	60.50	(20.8)
1998	170,982	—	170,982	206.25	201.70	161.50	77.50	(19.9)
1999	432,620	(3,343)	429,277	517.44	494.22	511.00	411.00	3.4
2000	378,607	(3,233)	375,374	447.55	431.43	491.00	382.50	13.8
2001	275,624	(2,892)	272,732	322.94	314.53	306.00	212.50	(2.7)
2002	199,900	(22,310)	177,590	210.23	206.68	177.00	79.00	(14.4)
2003	350,209	(29,325)	320,884	365.44	365.44	325.25	—	(11.0)
2004	361,233	(24,663)	336,570	384.41	384.41	322.75	—	(16.0)

* Restated for change in accounting policy to account for income on an xd basis.

† The diluted net asset value per ordinary share figures have been calculated in accordance with FRS14.

‡ (Discount)/premium is the difference between Herald's quoted share price and its underlying diluted net asset value (FRS14).

§ The diluted net asset values at 31 December 1995 and 1996 have been restated with the adoption of FRS14. The previously reported fully diluted net asset values were 131.65p and 149.45p respectively.

REVENUE						GEARING RATIOS	
Period to 31 December	Gross revenue £'000	Available for ordinary shareholders £'000	Earnings per ordinary share net** p	Dividend per ordinary share net p	Expense ratio†† %	Actual gearing‡‡	Potential gearing§§
1994	1,286	439	0.68	0.50	0.82	85	100
*1995	1,968	780	1.20	0.65	1.32	92	100
1996	2,897	1,035	1.32	0.81	1.46	89	100
1997	3,185	1,118	1.35	0.85	1.29	92	100
1998	3,845	1,134	1.37	0.90	1.36	94	100
1999	3,658¶	717	0.86	0.85	0.95	93	101
2000	6,508	778	0.93	0.85	1.40	86	101
2001	4,728	1,145	1.36	0.85	1.07	84	101
2002	3,539	627	0.74	0.85	1.21	108	113
2003	3,882	276	0.32	0.30	1.20	103	109
2004	4,776	301	0.34	0.30	1.20	97	107

* Restated for change in accounting policy to account for income on an xd basis.

** The calculation of earnings per ordinary share is based on the revenue from ordinary activities after taxation and the weighted average number of ordinary shares in issue (see note 8, page 35).

†† Ratio of total operating costs against average shareholders' funds.

‡‡ Total assets (including all debt used for investment purposes) less all cash and fixed interest securities (excluding convertibles) divided by shareholders' funds.

§§ Total assets (including all debt used for investment purposes) divided by shareholders' funds.

¶ Restated for the adoption of FRS16 "Current Tax".

CUMULATIVE PERFORMANCE (taking 1994 as 100)								
At 31 December	Diluted net asset value per share†	Share price	Benchmark	Hoare Govett Smaller Cos Index	Russell 2000 Technology Index	Earnings per ordinary share	Dividend per ordinary share net	Retail price index
1994	100	100	100	100	—	100	100	100
1995	141	140	112	112	100¶¶	176	130	103
1996	161	149	129	129	98	194	162	106
1997	184	149	149	136	103	199	170	110
1998	216	177	146	125	113	201	180	113
1999	528	562	251	190	240	126	170	115
2000	461	540	221	186	154	137	170	118
2001	336	336	186	157	123	200	170	119
2002	221	195	123	116	60	109	170	122
2003	391	357	174	161	88	47	60	126
2004	411	355	187	189	78	50	60	130

Compound Annual Returns

5 year	(4.9)%	(8.8)%	(5.8)%	(0.1)%	(20.1)%	(16.9)%	(18.8)%	2.6%
10 year	15.2%	13.5%	6.5%	6.6%	(2.7)%	(6.7)%	(5.0)%	2.7%

¶¶ Index at 9 April 1996, being the first date funds were first available for international investment.

Past performance is no guarantee of future performance.

DIRECTORS' REPORT

The Directors present their report and accounts for the year ended 31 December 2004.

Business Activity

The Company carries on business as an investment trust. It was approved by the Inland Revenue as an investment trust under Section 842 of the Income and Corporation Taxes Act 1988 for the year ended 31 December 2003, subject to any matters that may arise from any subsequent enquiry by the Inland Revenue into the Company's tax returns. In the opinion of the Directors the Company has conducted its affairs so as to enable it to continue to obtain such approval and it will continue to seek approval under Section 842 of the Income and Corporation Taxes Act 1988 each year.

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

Investment Policy and Objectives

The objective of the Company's management is to secure an attractive level of overall return for its shareholders primarily from capital growth but also from income over the life of the Company. The Company spreads its risks across a diversified portfolio of quoted securities in smaller companies which specialise in products, services or applications in the communications and multimedia sectors. The Company has certain specific investment guidelines, including that investee companies will have an equity market capitalisation of up to approximately £750 million at the time of initial investment. Securities acquired by the Company will normally be quoted on the Official List (which includes the Alternative Investment Market) of the London Stock Exchange or equivalent markets overseas.

At the Annual General Meeting held on 16 April 2003 shareholders approved the amendment to the Articles of Association of the Company increasing the maximum level of gearing from 20% to 30% of total capital and reserves. At 31 December 2004 borrowings comprised US\$47,350,000 (£24.7 million).

The Company's policy is to adopt a long-term approach to investment.

Continuation of the Company

The Directors consider it desirable that shareholders be given the opportunity to consider the future of the Company at regular intervals. Accordingly, an ordinary resolution was passed at the Annual General Meeting of the Company in 2004 to the effect that the Company should continue as an investment trust. The next continuation vote will be in 2007 and every third year thereafter. If such resolution is not passed, the Directors will prepare and submit to shareholders (for approval by special resolution) proposals for the unitisation or other reconstruction of the Company. If these proposals are not approved the Company will be wound up.

Results and Dividend

The net revenue after tax for the period was £301,000 (2003 – £276,000).

The Directors recommend a dividend of 0.30p per Ordinary share for the year ended 31 December 2004, which, if approved at the Annual General Meeting, will be payable on 19 April 2005 to holders registered on 29 March 2005. The payment will amount to £263,000 and the transfer to reserves will therefore be £38,000.

The net asset value (NAV) of the Company at 31 December 2004 represented a value of 384.41p per Ordinary share. This represented an increase of 5.2% during the year and a rise of 289.5% since the date of committal of funds (16 February 1994) after allowing for launch expenses of 1.3p per share.

Investment Report and Outlook

The Chairman's Statement and the Investment Manager's Report incorporate a review of the highlights of the year to 31 December 2004, and the outlook for the Company.

DIRECTORS' REPORT *continued*

The Board

The Directors at the year end, and their interests in the Company, all of which are beneficially owned, were as follows:

Name	Number of Ordinary Shares	
	2004	2003
Martin Boase	50,000	50,000
Clay Brendish	14,700	–
Timothy Curtis (appointed 22 July 2004)	–	– †
Justin Dukes	1,158	1,158
Douglas McDougall	200,000	200,000
Clive Parritt	9,649	9,649

†Holding at date of appointment

Mr T M Curtis was appointed to the Board on 22 July 2004. His appointment falls to be confirmed at the Annual General Meeting.

Mr D C P McDougall retires by rotation and, being eligible, offers himself for re-election.

In accordance with the Combined Code on Corporate Governance Mr M Boase, who is 72 and who has served on the Board for more than nine years, retires and offers himself for re-election.

The Board has reviewed the performance of Messrs Boase, Curtis and McDougall. Their performance continues to be effective and each remains committed to the Company. Their contribution to the Board is valued highly and the Board recommends their re-election to shareholders.

Mr J P Dukes and Mr C A Parritt will retire from the Board at the conclusion of the Annual General Meeting.

Mr C M McCarthy retired from the Board on 14 April 2004.

Mr T M Curtis acquired 2,000 shares on 14 February 2005. There have been no other changes intimated in the Directors' interests up to 16 February 2005.

Management and Administration

For the entire year under review the management of the Company was contracted to Herald Investment Management Limited (HIML). HIML is authorised and regulated by the Financial Services Authority.

The management contract is subject to 12 months' notice. The senior director of HIML with prime responsibility for the management of Herald Investment Trust is Katie Potts, who is also a substantial shareholder of HIML. HIML is remunerated at a monthly rate of 0.08333% of the Company's net asset value. Compensation fees would only be payable in respect of this 12 month period if termination were to occur sooner.

At 31 December 2004 the Company was the beneficial owner of 12.89% of the Ordinary share capital of HIML.

Administration of the Company and its investments is contracted by HIML to Baillie Gifford & Co., who also act as Company Secretary.

Custody of investments is contracted to The Bank of New York.

The Board considers the Company's investment management and secretarial arrangements for the Company on an ongoing basis and a formal review is conducted annually. The Board considers, amongst others, the following topics in its review: investment performance in relation to the investment policy and strategy; the continuity of personnel managing the assets and reporting to the Board; the level of service provided in terms of the accuracy and timeliness of reports to the Board and the frequency and quality of both verbal and written communications with shareholders. Following the most recent review the Board is of the opinion that the continued appointment of Herald Investment Management Limited as investment manager, on the terms agreed, is in the interests of shareholders due to the experience of the manager, the past performance and the quality of information provided to the Board.

DIRECTORS' REPORT *continued*

Significant Shareholdings

At 16 February 2005 the Directors have been notified of the following shareholdings comprising 3% or more of the issued share capital of the Company:

Name	Ordinary Shares	% of issue
Newton Investment Management Limited	8,256,701	9.4
The Royal Bank of Scotland plc	4,170,520	4.8
Legal & General Group plc	2,731,180	3.1

Payment of Suppliers

It is the Company's payment policy to obtain the best possible terms for all business. The Company negotiates with its suppliers the terms on which business will take place and abides by such terms.

The Company did not have any trade creditors at 31 December 2003 or 2004.

Auditors

The Auditors, Ernst & Young LLP, are willing to continue in office and in accordance with sections 385 and 390A of the Companies Act 1985 resolutions concerning their reappointment and remuneration will be submitted to the Annual General Meeting.

Annual General Meeting

At the Annual General Meeting of the Company to be held on 13 April 2005 the following resolution will be proposed as a special resolution.

Authority to Repurchase the Company's Ordinary Shares

At the Company's Annual General Meeting held on 14 April 2004 it was resolved that the Company be authorised to purchase in the market up to 13,162,321 Ordinary shares (14.99% of its Ordinary share capital in issue at that time). During the year to 31 December 2004, the Company bought back 251,338 Ordinary shares (nominal value £62,835 which comprised 0.29% of the issued share capital at 1 January 2004); on the London Stock Exchange for cancellation. The total consideration for these shares was £742,567. Between 1 January 2005 and the date of this report, no further shares have been bought back. The Board continues to believe, however, that the ability of the Company to purchase its own Ordinary shares in the market will potentially benefit all shareholders of the Company. The repurchase of Ordinary shares at a discount to the underlying net asset value ("NAV") should enhance the NAV per Ordinary share of the remaining shares and may also enable the Company to address more effectively any imbalance between supply and demand for the Company's Ordinary shares.

Accordingly, the Directors are now recommending in Resolution 9 that this authority to purchase the Company's own Ordinary shares should be renewed and should now expire at the Company's Annual General Meeting to be held in 2006. Authority will be sought to purchase up to 14.99% of the Company's Ordinary shares in issue at the date of the passing of the resolution (the maximum permitted under the Listing Rules of the UK Listing Authority) at a price that is not less than 25p per share (the nominal value of each share) and not more than 5% above the average middle-market quotation for the five business days preceding the day of purchase. The authority being sought, the full text of which can be found in Resolution 9 in the Notice of Annual General Meeting, will last until the date of the Annual General Meeting in 2006. The decision as to whether the Company repurchases any shares will be at the absolute discretion of the Board and will only be considered when it is in the interests of the Company and its shareholders as a whole. It is the intention that purchases will only be made at a discount to net asset value.

The Directors consider that the implementation of the facility to repurchase the Company's own Ordinary shares is in the interests of shareholders as a whole and unanimously recommend all holders to vote in favour of the resolution by completing and returning the enclosed form of proxy. The proxy form should be returned to the Company's Registrar as soon as possible but in any event so as to arrive no later than 48 hours before the time of the Annual General Meeting.

By order of the Board

Baillie Gifford & Co.

Secretaries

17 February 2005

DIRECTORS' REMUNERATION REPORT

Directors' Remuneration Report

The Board has prepared this report, in accordance with the requirements of Schedule 7A to the Companies Act 1985. An ordinary resolution for the approval of this report will be put to the members at the forthcoming Annual General Meeting.

The law requires the Company's auditors to audit certain of the disclosures provided. Where disclosures have been audited, they are indicated as such. The auditors' opinion is included in their report on pages 28 and 29.

Remuneration Committee

The Company has six Directors, all of whom are non-executive (see page 4). There is no separate remuneration committee and the Board as a whole considers changes to Directors' fees from time to time. The Company Secretary, Baillie Gifford & Co, provides advice when the Board considers the level of Directors' fees.

Policy on Directors' fees

The Board's policy is that the remuneration of Directors should be set at a reasonable level that is commensurate with the duties and responsibilities of the role and consistent with the requirement to attract and retain Directors of the appropriate quality and experience. It should also reflect the experience of the Board as a whole, be fair and comparable to that of other investment trusts that are similar in size. It is intended that this policy will continue for the year ended 31 December 2005 and subsequent years.

The fees for the non-executive Directors are determined within the limits set out in the Company's Articles of Association. Shareholders' approved an increase of the aggregate limit to £100,000 at the Annual General Meeting held on 14 April 2004. Non-executive Directors are not eligible for bonuses, pension benefits, share options, long-term incentive schemes or other benefits.

The Board carried out a review of the level of Directors' fees in 2002, and concluded that the fees should be increased from £13,200 to £15,000 for the Chairman and from £9,900 to £11,000 per Director.

Directors' service contracts

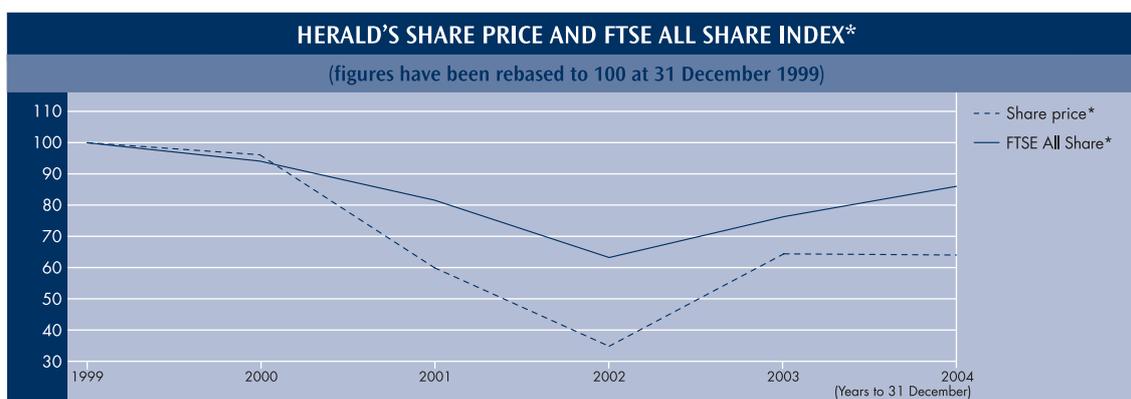
It is the Board's policy that none of the Directors have a service contract. All of the Directors have been provided with revised appointment letters dated 10 November 2004. The terms of their appointment provide that a Director shall retire and be subject to re-election at the first Annual General Meeting after their appointment. Directors are thereafter obliged to retire by rotation, and, if they wish, to offer themselves for re-election, at least every three years after that. There is no notice period and no provision for compensation upon early termination of appointment.

	Date of appointment	Due date for re-election
Martin Boase	11 January 1994	AGM April 2005
Clay Brendish	23 July 2001	AGM in 2006
Timothy Curtiss	22 July 2004	elected AGM April 2005
Justin Dukes	11 January 1994	retires AGM April 2005
Douglas McDougall	13 February 2002	AGM April 2005
Clive Parritt	10 December 1993	retires AGM April 2005

DIRECTORS' REMUNERATION REPORT *continued*

Company performance

The graph below compares, for the five financial years ending 31 December 2004, the total return (assuming all dividends are reinvested) to ordinary shareholders compared to the total shareholder return on a notional investment made up of shares in the component parts of the FTSE All-Share Index. This index was chosen for comparison purposes, as it is the best measure of performance for UK listed companies.



Past performance is no guarantee of future performance.

Directors' emoluments for the year (audited)

The Directors who served in the year received the following emoluments in the form of fees:

	Fees 2004 £	Fees 2003 £
Directors who served during the year:		
Martin Boase (Chairman)	15,000	15,000
Clay Brendish	11,000	11,000
Timothy Curtis (appointed 22 July 2004)	4,912	–
Justin Dukes	11,000	11,000
Colin McCarthy (retired 14 April 2004)	3,165	11,000
Douglas McDougall	11,000	11,000
Clive Parritt	11,000	11,000
	<u>67,077</u>	<u>70,000</u>

Sums paid to third parties (audited)

The Directors' fees payable to Mr C M Brendish and Mr J P Dukes were paid to Technology Management Services and ECIC Management Limited respectively. For the year to 31 December 2003, 50% of Mr C A Parritt's fee was paid to The Business Exchange PLC. The payments were for making their services available as Directors of the Company.

Approval

The Directors' Remuneration Report on pages 22 and 23 was approved by the Board of Directors on 10 February 2005 and signed on its behalf by

Clay Brendish
Director

CORPORATE GOVERNANCE

Compliance

The Board has considered the principles set out in the revised Combined Code on Corporate Governance (the “Code”) and the AITC Code on Corporate Governance (the “AITC Code”) both of which were published in July 2003.

The Board believes that the Company’s current practice, given the special circumstances of an investment trust company, is in all material respects consistent with the principles of the Code. The Company has complied throughout the year under review, unless otherwise stated below, with the provisions set out in Section 1 of the Code which are relevant to it.

The Board is also adhering to the principles of the AITC Code in all material respects.

The Board

The Board has overall responsibility for the Company’s affairs. It has a number of matters reserved for its approval including strategy, investment policy, borrowings, gearing, treasury matters, dividend and corporate governance policy. Full and timely information is provided to the Board to enable the Board to function effectively and to allow directors to discharge their responsibilities. The Board also reviews the financial statements, investment transactions, revenue budgets and performance.

The Board currently comprises six Directors all of whom are non-executive and are considered by the Board to be independent of the managers and free of any business or other relationship which could interfere with the exercise of their independent judgement. The executive responsibilities for investment management and administration have been delegated to Herald Investment Management Limited (HIML) and Baillie Gifford & Co respectively, and in the context of a Board comprised entirely of non-executive Directors, there is no chief executive officer. Mr D C P McDougall is the senior independent director.

The Directors all have appropriate business and financial experience to enable the Board to provide effective leadership and proper governance of the Company. Information about the Directors, including their relevant experience, can be found on page 4.

Mr C M McCarthy who had been a Director since 1994 retired during the year and both Mr C A Parritt and Mr J P Dukes, who have been Directors for eleven years, will retire at the forthcoming Annual General Meeting. Mr T M Curtis was appointed during the year.

There is an agreed procedure for Directors to seek independent professional advice if necessary at the Company’s expense. The Company also maintains Directors’ and Officers’ Liability insurance.

Chairman

The Chairman, Martin Boase, was independent at the date of his appointment and, notwithstanding that Mr Boase holds 5.6% of the ordinary share capital of the investment management company, the Board has concluded that he continues to be independent. The Board believes that Mr Boase’s shareholding has not, in the past, given rise to a conflict of interest or affected his independent judgement, nor is it expected to do so in the future. As Mr Boase has been a Director for eleven years, he has agreed to offer himself for re-election annually. The Board takes the view that Mr Boase’s independence has not been compromised by his length of service. The Board considers that none of his other commitments interferes with the discharge of his responsibilities to the Company and is satisfied that he makes sufficient time available to serve the Company effectively. There has been no significant change to the Chairman’s other commitments during the year.

Meetings

The number of meetings of the Board, the Audit Committee and the Nomination Committee held during the year and the attendance of the individual directors at those meetings is shown in the following table.

Name	Board	Audit Committee	Nomination Committee
Number of meetings	4	2	2
Martin Boase	4	2	2
Clay Brendish	2	2	2
Timothy Curtis (appointed 22 July 2004)	1	–	1
Justin Dukes	3	2	1
Colin McCarthy (retired 14 April 2004)	2	1	1
Douglas McDougall	4	2	2
Clive Parritt	4	2	1

Mr C M McCarthy attended all the meetings up to the date of his retirement and Mr T M Curtis attended all the meetings held since his appointment.

CORPORATE GOVERNANCE *continued*

Nomination Committee

The Nomination Committee consists of all the Directors and the Chairman of the Board is Chairman of the Committee. The Committee meets on annual basis and at such other times as may be required. The Committee has written terms of reference which include reviewing the Board, identifying and nominating new candidates for appointment to the Board, Board appraisal, succession planning and training. The terms of reference are available for inspection on request.

Following the retirement of Mr C M McCarthy the composition of the Board was reviewed and it was agreed that the appointment of a director with experience in the technology industry would strengthen the Board. Mr T M Curtis, who has extensive knowledge of the semiconductor and telecommunications equipment sector, was appointed to the Board on 22 July 2004. The Directors were able to identify Mr T M Curtis as an appropriate candidate for appointment to the Board without incurring the cost of either an external search consultant or an open advertisement.

Performance Evaluation

An appraisal of the Chairman, each Director and a performance evaluation and review of the Board as a whole and its committees was carried out during the year. The performance of each Director was appraised by the Chairman in individual interviews and the Chairman's performance was appraised in his absence by the other Directors and the results communicated to him. The appraisals and evaluations considered amongst others, the balance of skills of the Board, the contribution of individual Directors and the overall effectiveness of the Board. The performance of each Director, the Chairman, the Board and its Committees continues to be effective and each Director and the Chairman remain committed to the Company.

Terms of Appointment and Re-election

Letters which specify the terms of appointment, are issued to new Directors. The letters of appointment are available for inspection on request.

Training for new Directors is tailored to the particular circumstances of the individual appointee. Directors receive other relevant training as necessary.

A Director appointed during the year is required, under the provisions of the Company's Articles of Association, to retire and seek election by shareholders at the next Annual General Meeting. The Articles also require that one third of the Directors retire by rotation each year and seek re-election at the Annual General Meeting. In addition, all Directors are required to submit themselves for re-election at least every three years. The Board is of the view that length of service will not necessarily compromise the independence or contribution of Directors of an investment trust company, where continuity and experience can add significantly to the strength of the Board.

The names of the Directors retiring and offering themselves for re-election together with the reasons why the Board supports the re-elections are set out on page 20.

Remuneration

Since all the Directors are non-executive, a Remuneration Committee is considered unnecessary and Directors' fees are considered by the Board as a whole. The Company's policy on remuneration is set out in the Directors' Remuneration Report on pages 22 and 23.

Internal Controls and Risk Management

The Directors acknowledge their responsibility for the Company's system of internal controls and for reviewing its effectiveness. The system of internal controls is designed to manage rather than eliminate risk and can only provide reasonable but not absolute assurance against material misstatement or loss. The Directors confirm that they have reviewed the effectiveness of the system and they have procedures in place to review its effectiveness on a regular basis.

The Board confirms that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Company, in accordance with the guidance "Internal Control: Guidance for Directors on the Combined Code."

CORPORATE GOVERNANCE *continued*

The practical measures to ensure compliance with regulation and company law, and to provide effective and efficient operations and investment management, have been delegated to HIML and Baillie Gifford & Co, as detailed in the Directors' Report. The Board acknowledges its responsibilities to supervise and control the discharge by the managers and secretaries of their obligations.

The managers are responsible for the design, implementation and maintenance of control policies and procedures to safeguard the assets of the Company and to manage its affairs properly. This responsibility also extends to maintaining effective operational and compliance controls and risk management.

The Company's investments are segregated from the investment and administration functions through the appointment of The Bank of New York as independent custodian of the Company's investments.

The managers have a compliance function in accordance with the Financial Services Authority regulations. The managers' compliance function provides the Board with a report on monitoring procedures on a regular basis. In addition, Baillie Gifford & Co conducts an annual review of its system of internal controls which is documented within an internal controls report. This report is independently reviewed by Baillie Gifford & Co's auditors. A copy of the internal controls report is submitted to the Board. The Baillie Gifford & Co heads of business risk & internal audit and regulatory risk provide the Board with regular reports on Baillie Gifford & Co's monitoring programmes as they relate to the secretarial and administrative function.

A detailed risk map is prepared which identifies the significant risks faced by the Company and the key controls to manage these risks are confirmed as in place and operating effectively.

These procedures ensure that consideration is given regularly to the nature and extent of the risks facing the Company and that they are being actively monitored. Where changes in risk have been identified during the year they also provide a mechanism to assess whether further action is required to manage the risks identified. The Board confirms that these procedures have been in place throughout the Company's financial year, are operating effectively and continue to be in place up to the date of approval of this Report.

Internal Audit

The Board has reviewed the need for an internal audit function and has decided that the compliance and internal control systems in place within the Investment Managers and Company Secretaries provide sufficient assurance that a sound system of internal control, which safeguards shareholders' investment and the Company's assets, is maintained. An internal audit function, specific to the trust, is therefore considered unnecessary.

Accountability and Audit

The respective responsibilities of the Directors and the auditors in connection with the Financial Statements are set out on pages 27 to 29.

The accounts have been prepared on the going concern basis as it is the Directors' opinion that the Company has adequate resources to continue in operational existence for the foreseeable future.

An Audit Committee has been established in compliance with the Combined Code consisting of all the non-executive Directors, all of whom are considered to be independent. Its authority and duties are clearly defined within its written terms of reference which are available on request. The Chairman of the Board is Chairman of the Audit Committee. The Committee's responsibilities include:

- monitoring and reviewing the integrity of the financial statements, the internal financial controls and the independence, objectivity and effectiveness of the external auditors;
- making recommendations to the Board in relation to the appointment of the external auditors and approving the remuneration and terms of their engagement;
- developing and implementing policy on the engagement of the external auditors to supply non audit services;
- reviewing the arrangements in place within HIML whereby their staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters insofar as they may affect the Company;

CORPORATE GOVERNANCE *continued*

- reviewing the terms of the Investment Management Agreement; and
- considering annually whether there is a need for the Company to have its own internal audit function.

Relations with Shareholders

The Company's managers meet regularly with institutional shareholders and report to the Board. The Chairman is available to meet with shareholders as appropriate. Shareholders wishing to communicate with the Chairman or any other Director may do so by writing to him at the address of the registered office of the Company shown on page 4. The Company's Annual General Meeting provides a forum for communication with all shareholders and the Board announces the level of proxies lodged. The notice period for the Annual General Meeting is at least twenty working days.

Voting Policy and Socially Responsible Investment

The Company has given discretionary voting powers to the investment managers, HIML. The Managers vote against resolutions they consider may damage shareholders' rights or economic interests. HIML give consideration to socially responsible investment when making investment decisions, but their overriding objective is to produce good investment returns for shareholders. The managers' policy has been reviewed and endorsed by the Board.

On behalf of the Board

Clay Brendish

Director

17 February 2005

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RELATION TO THE FINANCIAL STATEMENTS

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 as at the end of the year and of the surplus or deficit for the year. In preparing the financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates which are reasonable and prudent; and
- 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 enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

INDEPENDENT AUDITORS' REPORT

TO THE MEMBERS OF HERALD INVESTMENT TRUST plc

We have audited the Company's financial statements for the year ended 31 December 2004 which comprise the Statement of Total Return, Balance Sheet, Cash Flow Statement and the related notes 1 to 21. These financial statements have been prepared on the basis of the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the Company'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 Company's members those matters that 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 Company and the Company'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

The directors are responsible for preparing the Annual Report, including the financial statements which are required to be prepared in accordance with applicable United Kingdom law and accounting standards as set out in the Statement of Directors' Responsibilities in relation to the financial statements.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements, United Kingdom Auditing Standards and the Listing Rules of the Financial Services Authority.

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 to be 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 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 Company is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the 2003 FRC 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 Company's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. This other information comprises the Company Summary, Year's Summary, Long Term Performance Summary, Directors, Manager and Advisers, Chairman's Statement, Investment Manager's Report, Top Twenty Holdings, Classification of Investments, Geographical Spread of Investments, Detailed List of Investments, Ten Year Record, Directors' Report, unaudited part of the Directors' Remuneration Report, Corporate Governance Statement, Notice of Annual General Meeting and Further Shareholder Information. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes an 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 to be 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 Company's circumstances, consistently applied and adequately disclosed.

INDEPENDENT AUDITORS' REPORT *continued*

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 and the part of the Directors' Remuneration Report to be 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 to be audited.

Opinion

In our opinion:

- the financial statements give a true and fair view of the state of affairs of the Company as at 31 December 2004 and of its net revenue for the year then ended; and
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985.

ERNST & YOUNG LLP

Registered Auditor

Edinburgh

17 February 2005

STATEMENT OF TOTAL RETURN

(incorporating the revenue account)

FOR THE YEAR ENDED 31 DECEMBER 2004

		2004			2003		
	Notes	Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
Gains on investments	9	–	14,607	14,607	–	136,680	136,680
Exchange difference on loans		–	1,813	1,813	–	3,169	3,169
Currency (losses)/gains		–	(29)	(29)	–	100	100
Income	2	4,776	–	4,776	3,882	–	3,882
Investment management fee	3	(3,671)	–	(3,671)	(2,727)	–	(2,727)
Other administrative expenses	4	(267)	–	(267)	(259)	–	(259)
Net return before finance costs and taxation							
Finance costs of borrowings	5	838	16,391	17,229	896	139,949	140,845
		(501)	–	(501)	(591)	–	(591)
Return on ordinary activities before taxation							
Tax on ordinary activities	6	337	16,391	16,728	305	139,949	140,254
		(36)	–	(36)	(29)	–	(29)
Return on ordinary activities after taxation							
Ordinary dividend payable	7	301	16,391	16,692	276	139,949	140,225
		(263)	–	(263)	(263)	–	(263)
Transfer to reserves							
		38	16,391	16,429	13	139,949	139,962
Return per Ordinary share							
	8	0.34p	18.68p	19.02p	0.32p	161.39p	161.71p
Dividend per Ordinary share	7	0.30p			0.30p		

The revenue column of this statement is the revenue account of the Company.

All revenue and capital items in the above statement derive from continuing operations.

The accompanying notes on pages 33 to 41 are an integral part of this statement.

BALANCE SHEET

AT 31 DECEMBER 2004

	Notes	2004		2003	
		£'000	£'000	£'000	£'000
Fixed assets					
Investments	9		325,168		331,497
Current assets					
Debtors	11	1,880		898	
Cash at bank and in hand	10	34,907		18,639	
		36,787		19,537	
Creditors:					
Amounts falling due within one year	12	(25,385)		(30,150)	
Net current assets/(liabilities)			11,402		(10,613)
TOTAL NET ASSETS			336,570		320,884
Capital and reserves					
Called-up share capital	14		21,889		21,952
Share premium	15		73,738		73,738
Capital redemption reserve	15		63		–
Capital reserve – realised	15		202,442		182,463
Capital reserve – unrealised	15		36,339		40,670
Revenue reserve	15		2,099		2,061
EQUITY SHAREHOLDERS' FUNDS	16		336,570		320,884
NET ASSET VALUE PER ORDINARY SHARE	17		384.41p		365.44p

The accounts were approved by the Board of Directors and signed on their behalf on 17 February 2005.

Clay Brendish
Director

The accompanying notes on pages 33 to 41 are an integral part of this statement.

CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2004

	Notes	2004		2003	
		£'000	£'000	£'000	£'000
Net cash inflow from operating activities	18		762		927
Servicing of Finance					
Loan interest		(495)		(580)	
Net cash outflow from servicing of finance			(495)		(580)
Financial investment					
Purchase of investments		(65,423)		(77,543)	
Sale of investments		85,279		74,274	
Net cash inflow/(outflow) from financial investment			19,856		(3,269)
Equity dividend paid			(263)		(718)
Net cash inflow/(outflow) before financing			19,860		(3,640)
Financing					
Issue of Ordinary shares		–		3,332	
Loans drawn down		25,769		37,902	
Loans repaid		(28,618)		(27,718)	
Shares repurchased		(743)		–	
Net cash (outflow)/inflow from financing			(3,592)		13,516
INCREASE IN CASH	19		16,268		9,876
RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET (DEBT)/FUNDS	19				
Increase in cash in period			16,268		9,876
Decrease/(increase) in bank loans			2,849		(10,184)
Exchange movement on loans			1,813		3,169
MOVEMENT IN NET FUNDS/(DEBT) IN PERIOD			20,930		2,861
NET DEBT AT 1 JANUARY			(10,686)		(13,547)
NET FUNDS/(DEBT) AT 31 DECEMBER			10,244		(10,686)

The accompanying notes on pages 33 to 41 are an integral part of this statement.

NOTES TO THE ACCOUNTS

1. Accounting policies

The financial statements have been prepared in accordance with applicable accounting standards. The particular accounting policies adopted, which are unchanged from last year and have been applied consistently, are set out below.

(a) **Accounting convention**

The accounts are prepared under the historical cost convention, as modified by the revaluation of investments. The accounts have been prepared in accordance with the Statement of Recommended Practice “Financial Statements of Investment Trust Companies” issued in January 2003.

(b) **Investments**

Listed investments are valued at closing mid-market prices. Investments on the Alternative Investment Market are included at their quoted mid-market prices. Where material unlisted investments are valued by Directors on the basis of latest information in line with the relevant principles of the British Venture Capital Association Guidelines.

(c) **Income**

Dividend income is accounted for when the entitlement to the income is established (normally on the ex-dividend date). Interest receivable is accounted for on an accruals basis.

(d) **Capital reserves**

The Company is precluded by its Articles from making any distribution of capital profits by way of dividend. Realised profits and losses on disposals of investments are dealt with in the realised capital reserve. Unrealised revaluation movements are dealt with through the unrealised capital reserve. Special dividends representing repayments of capital are dealt with through the unrealised capital reserve. Purchases of the Company’s own shares for cancellation are also funded from this reserve.

(e) **Investment management fees**

Investment management fees are charged wholly to revenue.

(f) **Finance costs**

Finance costs are accounted for on an accruals basis and are charged through the revenue account.

(g) **Deferred taxation**

Deferred taxation is provided on all timing differences which have originated but not reversed at the balance sheet date, calculated on an undiscounted basis, and based on enacted tax rates relevant to the benefit or liability. Deferred tax assets are recognised only to the extent that it is more likely than not that there will be taxable profits from which underlying timing differences can be deducted.

(h) **Foreign currency**

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and loans denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date. Exchange differences of a revenue nature are taken to the revenue account. Those of a capital nature are taken to capital reserve.

NOTES TO THE ACCOUNTS *continued*

2. Income	2004	2003
	£'000	£'000
Income from investments		
Franked dividends from listed investments	2,559	2,423
Franked dividends from unlisted investments (inc AIM)	14	118
Unfranked income from unlisted (inc AIM) UK convertible bonds	123	86
Overseas dividend income	753	820
	<u>3,449</u>	<u>3,447</u>
Other income		
Deposit interest	1,310	428
Underwriting commission	17	7
	<u>1,327</u>	<u>435</u>
Total income	<u>4,776</u>	<u>3,882</u>
Total income comprises:		
Dividends	3,326	3,361
Interest from investments	123	86
Other	1,327	435
	<u>4,776</u>	<u>3,882</u>
Income from investments		
Listed UK	2,559	2,423
Listed overseas	753	820
Unlisted	137	204
	<u>3,449</u>	<u>3,447</u>

3. Investment management fee – <i>all charged to revenue</i>	2004	2003
	£'000	£'000
Investment management fee	3,314	2,455
Irrecoverable VAT thereon	357	272
	<u>3,671</u>	<u>2,727</u>

Herald Investment Management Limited are appointed investment managers under a management agreement which is terminable on twelve months notice. Their fee is calculated on a monthly rate of 0.08333% of the Company's net asset value and is subject to VAT at the appropriate rate.

4. Other administrative expenses – <i>all charged to revenue</i>	2004	2003
	£'000	£'000
Custodian's fees	39	37
Registrars' fees	23	25
Directors' fees	67	70
Auditors' fees – audit work	11	10
Miscellaneous expenses	127	117
	<u>267</u>	<u>259</u>

5. Finance costs of borrowings – <i>all charged to revenue</i>	2004	2003
	£'000	£'000
Bank loans repayable within one year	501	591
	<u>501</u>	<u>591</u>

NOTES TO THE ACCOUNTS *continued*

6. Taxation

	2004	2003
	£'000	£'000
Overseas taxation	36	29
The tax charge for the year is lower than the standard rate of corporation tax in the UK (30%). The differences are explained below.		
Revenue return on ordinary activities before taxation	337	305
Revenue return on ordinary activities multiplied by the standard rate of corporation tax in the UK of 30% (2003 – 30%)	101	92
Income not taxable	(772)	(762)
Overseas withholding tax claimed as a deduction	(11)	(9)
Overseas withholding tax written off	36	29
Excess expenses in period not provided for as an asset	682	679
Current tax charge for the year	36	29

Capital returns are not included in the above analysis; as an Investment Trust, the Company's capital gains are not taxable.

There is no corporation tax charge at 31 December 2004 or 31 December 2003 as the Company has unrelieved management expenses which are available to be carried forward. The tax charge for 31 December 2004 and 2003 comprises overseas withholding taxes written off.

At 31 December 2004 the Company had surplus management expenses of £10m (2003 – £7m) which have not been recognised as a deferred tax asset. This is because the Company is not expected to generate taxable income in a future period in excess of the deductible expenses of that future period and, accordingly, it is unlikely that the Company will be able to reduce future tax liabilities through the use of existing surplus expenses.

7. Ordinary dividend

	2004	2003	2004	2003
			£'000	£'000
Proposed dividend per ordinary share	0.30p	0.30p	263	263

The proposed dividend will be paid on 19 April 2005 to all shareholders on the register as at the close of business on 29 March 2005.

8. Return per Ordinary share

	2004			2003		
	Revenue	Capital	Total	Revenue	Capital	Total
	0.34p	18.68p	19.02p	0.32p	161.39p	161.71p

Revenue return per Ordinary share is based on the net revenue on ordinary activities after taxation of £301,000 (2003 – £276,000) and on 87,745,357 Ordinary shares (2003 – 86,711,829) being the weighted average number of Ordinary shares in issue during the year.

Capital return per Ordinary share is based on the net capital gain for the financial year of £16,391,000 (2003 – £139,949,000) and on 87,745,357 Ordinary shares (2003 – 86,711,829) being the weighted average number of Ordinary shares in issue during the year.

NOTES TO THE ACCOUNTS *continued*

9. Fixed assets – investments

	2004	2003
	£'000	£'000
Listed at market valuation on the London Stock Exchange	167,600	184,699
Listed at market valuation on other recognised Stock Exchanges	105,785	109,510
AIM	49,452	35,222
Unquoted*	2,331	2,066
	325,168	331,497
Total fixed asset investments	325,168	331,497

	Listed in UK £'000	Listed overseas £'000	AIM £'000	Unquoted £'000	Total £'000
Cost of investments at 1 January 2004	119,818	114,839	51,465	6,282	292,404
Unrealised appreciation/(depreciation) at 1 January 2004	64,881	(5,329)	(16,243)	(4,216)	39,093
	184,699	109,510	35,222	2,066	331,497
Value of investments at 1 January 2004					
Movements in the year:					
Purchases at cost	11,615	35,949	16,930	800	65,294
Sales – proceeds	(42,188)	(37,320)	(5,747)	(975)	(86,230)
– realised profit/(loss)	17,962	3,550	(3,251)	205	18,466
Increase in unrealised appreciation/(depreciation)	(5,463)	(5,904)	7,273	235	(3,859)
Change in listing	975	–	(975)	–	–
	167,600	105,785	49,452	2,331	325,168
Value of investments held at 31 December 2004					
Cost of investments at 31 December 2004	108,182	117,018	58,422	6,312	289,934
Unrealised appreciation/(depreciation) at 31 December 2004	59,418	(11,233)	(8,970)	(3,981)	35,234
	167,600	105,785	49,452	2,331	325,168
Value of investments at 31 December 2004	167,600	105,785	49,452	2,331	325,168

	2004	2003
	£'000	£'000
Gains/(losses) on investments		
Realised gains/(losses) on sales	18,466	(6,300)
(Decrease)/increase in unrealised appreciation/(depreciation)	(3,859)	142,980
	14,607	136,680
	14,607	136,680

Of the realised gains on sales of £18,466,000 (2003 – loss of £6,300,000) during the year, a net gain of £9,293,000 (2003 – loss of £24,852,000) was included in unrealised appreciation/(depreciation) at the previous year end.

* The unquoted balance comprises Herald Investment Management Limited, Herald Venture 2 and HIML Jersey Ltd included at their cost of £506,640, ID Data 7% Convertible Secured Loan Notes 2008 at £1,000,000, UbiNetics at £788,089, Culver Holdings at £36,000 and Atex Media Solutions (grey market value at 31 December 2004 of £4,400) at zero.

At 31 December 2004 the Company was the beneficial owner of 12.89% (2003 – 13.83%) of the Ordinary share capital of both HIML and HIML Jersey Ltd. HIML is incorporated in the United Kingdom whereas HIML Jersey Ltd is incorporated in Jersey.

NOTES TO THE ACCOUNTS *continued*

10. Financial assets

A full list of the Company's investments is given on pages 13 to 17. In addition, a geographical analysis of the portfolio, an analysis of the investment portfolio by broad industrial or commercial sector and a review of the 20 largest equity investments by their aggregate market value, are contained in the investment review section on pages 9 to 12. All financial assets are included in the accounts at market value (see note 1).

Exposure to currency risk through asset allocation is indicated below:

	2004	2003
Portfolio (currency of listing):	£'000	£'000
Sterling	219,383	222,497
US dollars	57,548	64,987
Euros	10,905	11,806
Other European currencies	9,364	6,128
Yen	2,643	2,139
Australian dollars	1,576	5,820
Hong Kong dollars	5,038	1,262
Malaysian ringitt	3,252	4,242
Singapore dollars	8,533	8,280
Other Asia Pacific currencies	6,926	4,336
	325,168	331,497
Cash:		
UK deposits	34,776	18,286
Foreign deposits – Taiwan dollars	48	228
– Singapore dollars	–	38
– Israel shekels	83	87
	34,907	18,639

The cash deposits generally comprise call or overnight deposit accounts which are payable on demand. The benchmark rate which determines the interest payments received on cash balances is the bank base rate.

The interest rate risk profile of the Company's financial assets at 31 December was:

	2004			2003		
	Market value	Weighted average interest rate	Weighted average maturity/period until maturity date	Market value	Weighted average interest rate	Weighted average maturity/period until maturity date
	£'000	rate	date	£'000	rate	date
Fixed rate:						
UK convertible bonds	1,664	7%	3 years	1,668	7%	4 years
US convertible bond	60	7%	4 years	50	–	01/08/04
Floating rate:						
UK convertible bond (interest rate linked to sterling LIBOR)	–	–	–	400	6%	02/01/04
	–	–	–	400	6%	02/01/04

NOTES TO THE ACCOUNTS *continued*

10. Financial assets (continued)

Short term debtors and creditors have been excluded from the disclosure of financial instruments as allowed by FRS13 other than for currency disclosures. The following currency amounts are included in net current assets:

	2004	2003
	£'000	£'000
Income accrued:		
Sterling	500	475
US dollar	3	1
Hong Kong dollar	26	–
Korean won	22	–
Malaysian dollar	–	19
	551	495
	551	495
Sales for subsequent settlement:		
Sterling	409	249
US dollar	791	–
	1,200	249
	1,200	249

Included within the analysis provided above and on pages 13 to 17 is the Company's holding in warrants which confer the right to convert into equity shares. An analysis of the currency exposure and maturity profile of these warrants at 31 December is provided below.

	2004		2003	
	Market value	Maturity date	Market value	Maturity date
	£'000		£'000	
Warrants:				
Hong Kong dollar	28	31/12/06	–	–
Hong Kong dollar	16	03/11/06	–	–
Singapore dollar	32	13/08/09	–	–

11. Debtors

	2004	2003
	£'000	£'000
Due within one year:		
Income accrued	551	495
Sales for subsequent settlement	1,200	249
Taxation recoverable	38	34
Other debtors and prepayments	91	120
	1,880	898
	1,880	898

12. Creditors

	2004	2003
	£'000	£'000
Amounts falling due within one year:		
Purchases for subsequent settlement	–	129
Proposed final dividend	263	263
Bank loans (see note 13)	24,663	29,325
Other creditors and accruals	459	433
	25,385	30,150
	25,385	30,150

Included in other creditors and accruals is £278,000 (2003 – £267,000) in respect of the investment management fee.

NOTES TO THE ACCOUNTS *continued*

13. Financial liabilities

The Company currently has a 364 day US\$47.35 million multi-currency loan facility with ING Bank N.V. which expires on 25 October 2005. At 31 December 2003 it also had a five year £3 million facility with the Royal Bank of Scotland plc which expired on 7 January 2004.

The interest rate risk profile of the Company's financial liabilities at 31 December was:

	2004			2003		
	£'000	Interest rate	Period until maturity	£'000	Interest rate	Period until maturity
<i>Bank loans:</i>						
US\$ 47,350,000 – fixed rate	24,663	2.62%	4 months	26,450	1.7%	10 months
Yen 551,550,000 – fixed rate	–	–	–	2,875	2.5%	1 week
	<u>24,663</u>			<u>29,325</u>		
				2004 £'000		2003 £'000

The maturity profile of the Company's financial liabilities at 31 December was:

In one year or less, or on demand	<u>24,663</u>	<u>29,325</u>
-----------------------------------	---------------	---------------

Interest on the multi-currency loan is payable in half yearly instalments in April and October. The loan is due for repayment in April 2005 and is with ING Bank N.V. The estimated repayment value of the loan was £24,989,000 (2003 – £25,769,000) as at 31 December 2004. The indicative costs of repaying the loan as at 31 December are not material in the context of the above figures.

The following covenants relate to the loan with ING Bank N.V.:

- (i) Total borrowings shall not exceed 30% of the Company's net asset value.
- (ii) The Company's minimum net asset value shall be £100,000,000.
- (iii) No one listed investment owned by the Company should represent more than 7.5% of the Company's total assets.

The fair value of the loans are not materially different from the carrying value.

Short term debtors and creditors have been excluded from the disclosure of financial instruments as allowed by FRS 13 other than for currency disclosures which include £nil (2003 – £129,000 of Singapore dollars) in respect of purchases for subsequent settlement and £117,000 of US\$ (2003 – £76,000 of US\$ and £35,000 of Japanese yen) in respect of loan interest.

Gains and losses on hedges

At 31 December 2004 there were no unrecognised gains/losses on hedges. Realised currency gains/losses are taken to the capital reserve and are not reflected in the profit and loss account unless they are of a revenue nature.

14. Called-up share capital

		2004	2003
Authorised:			
Ordinary shares of 25p:	Number	109,000,000	109,000,000
	£'000	<u>27,250</u>	<u>27,250</u>
Allotted, issued and fully paid:			
Ordinary shares of 25p:	Number	87,556,010	87,807,348
	£'000	<u>21,889</u>	<u>21,952</u>

At the Annual General Meeting in April 2004 Shareholders granted the Company authority to purchase shares in the market up to 13,162,321 Ordinary shares (equivalent to 14.99% of its issued share capital at that date). In the year to 31 December 2004, a total of 251,338 (2003 – nil) Ordinary shares with a nominal value of £62,835 were bought back at a total cost of £742,567 (2003 – £nil). At 31 December 2004 the Company had authority to buy back a further 12,910,983 Ordinary shares. Under the provisions of the Company's Articles share buy-backs are funded from the realised capital reserve. The nominal value of the share capital is maintained by the provision of a capital redemption reserve.

NOTES TO THE ACCOUNTS *continued*

15. Reserves

	Share premium £'000	Capital redemption reserve £'000	Capital reserve – realised £'000	Capital reserve – unrealised £'000	Revenue reserve £'000
Balance at 1 January 2004	73,738	–	182,463	40,670	2,061
Shares purchased for cancellation	–	63	(743)	–	–
Net gain on realisation of investments	–	–	18,466	–	–
Decrease in unrealised appreciation	–	–	–	(3,859)	–
Exchange difference on currency loans	–	–	2,285	(472)	–
Other exchange differences	–	–	(29)	–	–
Net revenue for the year	–	–	–	–	38
Balance at 31 December 2004	<u>73,738</u>	<u>63</u>	<u>202,442</u>	<u>36,339</u>	<u>2,099</u>

16. Reconciliation of movements in shareholders' funds

	2004 £'000	2003 £'000
Shareholders' funds at 1 January 2004	320,884	177,590
Total recognised gains and losses for the year (after dividend payments)	16,429	139,962
Shares purchased for cancellation	(743)	–
Proceeds from exercise of warrants	–	3,332
Shareholders' funds at 31 December 2004	<u>336,570</u>	<u>320,884</u>

17. Net asset value per Ordinary share

The net asset value per Ordinary share and the net assets attributable to the Ordinary shareholders at the year end calculated in accordance with the Articles of Association were as follows:

	2004	2003	2004 £'000	2003 £'000
Ordinary shares	384.41p	365.44p	336,570	320,884

Net asset value per Ordinary share is based on net assets as shown above and 87,556,010 (2003 – 87,807,348) Ordinary shares, being the number of Ordinary shares in issue at each date.

18. Reconciliation of net revenue before finance costs and taxation to net cash inflow from operating activities

	2004 £'000	2003 £'000
Net revenue on ordinary activities before finance costs and taxation	838	896
(Increase) in accrued income	(49)	(46)
Decrease/(increase) in debtors	29	(70)
Increase in creditors	20	87
Income tax suffered	(11)	(11)
Overseas tax suffered	(36)	(29)
Realised currency (loss)/profit	(29)	100
Net cash inflow from operating activities	<u>762</u>	<u>927</u>

NOTES TO THE ACCOUNTS *continued*

19. Analysis of changes in net (debt)/funds

	At 1 January 2004	Cash flows	Exchange movement	At 31 December 2004
	£'000	£'000	£'000	£'000
Cash at bank and in hand	18,639	16,268	–	34,907
Loans due within one year	(29,325)	2,849	1,813	(24,663)
	<u>(10,686)</u>	<u>19,117</u>	<u>1,813</u>	<u>10,244</u>

20. Contingent Liabilities, Guarantees and Financial Commitments

At 31 December 2004 the Company had a commitment to participate in Herald Ventures II Limited Partnership. The Company's commitment is limited to £3 million, drawn down in tranches, over a 5 year period. The first tranche of £300,000 was drawn down on 27 October 2004.

21. Derivatives and Other Financial Instruments

In accordance with the corporate objective of maximising total returns the Company invests in securities on a worldwide basis. The Company makes use of gearing to achieve improved performance in rising markets. Other financial instruments consist of cash, short term debtors and creditors.

The main risks arising from the Company's financial instruments are market price, foreign currency, liquidity and interest rate risks. The Manager's policies for managing these risks, which have been applied throughout the year, are summarised below.

Market Price Risk

The Company's investment portfolio is exposed to market price fluctuations which are monitored by the Manager in pursuance of the corporate objective. Securities held by the Company are valued at mid-market prices, where material unlisted investments are valued by the Directors on the basis of latest information in line with the relevant principles of the British Venture Capital Association Guidelines (Accounting Policy (b)). These valuations also represent the fair value of the investments.

The Company has authority to write options against individual shares held within the portfolio. No such transactions were undertaken in the year under review.

Foreign Currency Risk

Herald invests on a worldwide basis and the balance sheet can be affected by movements in foreign currency exchange rates. The list of equity investments on pages 13 to 17 shows the countries in which the Company is invested. The securities in the portfolio are priced in local currency.

The Company does not hedge the sterling value of investments that are priced in other currencies. Overseas income is subject to currency fluctuations. The Company does not hedge this currency risk.

The main foreign currency exposure at 31 December 2004 is detailed in note 10 Financial assets and note 13 Financial liabilities.

Liquidity Risk

The Company's assets mainly comprise readily realisable securities. Cash balances are held with The Bank of New York, The Bank of Scotland, Lloyds TSB and Rabobank. Short term flexibility is achieved by an overdraft facility of £2 million with The Bank of New York.

Interest Rate Risk

The majority of the Company's assets are equity shares and other investments which neither pay interest nor have a maturity date. However, the Company does hold Convertible Bonds and has held Treasury Stocks, the interest rate and maturity dates of which are detailed in note 10 Financial assets. Interest is accrued on sterling cash balances at a rate linked to the UK base rate.

At the year end the Company had borrowings totalling £24,663,000 (US\$47,350,000) (2003 – £29,325,000 (Yen 551,550,000 and US\$47,350,000)) which becomes due for repayment in April 2005 (see note 13).

NOTICE OF ANNUAL GENERAL MEETING

Notice is hereby given that the Annual General Meeting of Herald Investment Trust plc will be held at 12 Charterhouse Square, London EC1M 6AX on 13 April 2005 at 11.30 am for the following purposes:

Ordinary Business

1. To receive and adopt the Directors' report, the annual accounts and the Auditors' report in respect of the year ended 31 December 2004.
2. To approve the Directors' Remuneration Report.
3. To declare a dividend of 0.30p per share in respect of the year ended 31 December 2004.

To consider resolution No. 4, special notice having been received of the intention to propose the resolution as an ordinary resolution (see note 4).

4. To re-elect Mr M Boase, who is aged 72, as a Director of the Company.
5. To re-elect Mr D C P McDougall as a Director of the Company.
6. To elect Mr T M Curtis as a Director of the Company.
7. To reappoint Ernst & Young LLP as Auditors to the Company.
8. To authorise the Directors to determine the remuneration of the Auditors.

To consider and, if thought fit, pass the following resolution as a Special Resolution:

9. THAT, the Company be generally and subject as hereinafter appears 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 its issued shares of 25p each in the capital of the Company in substitution for any existing authority under section 166 of the Act but without prejudice to any exercise of any such authority prior to the date hereof.

PROVIDED ALWAYS THAT

- (i) the maximum number of shares hereby authorised to be purchased shall be 14.99% of the issued share capital on the date on which this resolution is passed;
- (ii) the minimum price which may be paid for a share shall be 25p;
- (iii) the maximum price which may be paid for a share shall be an amount equal to 105% of the average of the middle market quotations for a share taken from and calculated by reference to the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the share is purchased;
- (iv) any purchase of shares will be made in the market for cash at prices below the prevailing net asset value per share (as determined by the Directors);
- (v) unless previously varied, revoked or renewed, the authority hereby conferred shall expire at the conclusion of the Annual General Meeting of the Company to be held in 2006; and
- (vi) the Company may make a contract to purchase shares under the authority hereby conferred prior to the expiry of such authority and may make a purchase of shares pursuant to any such contract notwithstanding such expiry.

By order of the Board

Baillie Gifford & Co.
Secretaries

Registered Office:
12 Charterhouse Square
London EC1M 6AX
2 March 2005

NOTES

1. A shareholder entitled to attend and vote at the meeting is entitled to appoint one or more proxies to attend and, on a poll, to vote in his stead. Such proxy need not be a member of the Company.
2. A form of proxy is enclosed and to be valid must be lodged with the Registrars of the Company not less than forty-eight hours before the time fixed for the meeting.
3. Pursuant to Regulation 41 of the Uncertificated Securities Regulations 2001, the Company specifies that only those shareholders entered on the Register of Members of the Company as at 11.30 am on 11 April 2005 or, in the event that the meeting is adjourned, on the Register of Members 48 hours before the time of any adjourned meeting, shall be entitled to attend or vote at the meeting in respect of the number of ordinary shares registered in their name at that time. Changes to the entries on the Register of Members after 11.30 am on 11 April 2005 or, in the event that the meeting is adjourned, in the Register of Members 48 hours before the time of any adjourned meeting, shall be disregarded in determining the rights of any person to attend or vote at this meeting, notwithstanding any provisions in any enactment, the Articles of Association of the Company or other instrument to the contrary.
4. In accordance with section 293 of the Companies Act 1985 special notice has been given to the Company of the resolution to reappoint a Director who is over the age of 70.
5. No Director has a contract of service with the Company.

FURTHER SHAREHOLDER INFORMATION

- **How to Invest** The Company's shares are traded on the London Stock Exchange. They can be bought by placing an order with a stockbroker or by asking a professional adviser to do so.
- **Sources of Further Information on the Trust** The price of shares is quoted daily in the *Financial Times*, *The Daily Telegraph* and *The Times*. The NAV per share is calculated and released daily to the London Stock Exchange and monthly to the Association of Investment Trust Companies.
- **Key Dates** Ordinary shareholders normally receive a dividend in respect of each financial year which is normally paid in April. The AGM is normally held in April.
- **Taxation** The price of the Ordinary shares (adjusted for the price of attributable warrants) on 21 February 1994, which was the first day of trading, was 90.9p. The amount attributable to the warrants for the purpose of capital gains tax is 9.1p per share issued (1994 Annual Report). Up to 5 April 1998 the basis for calculating non-trading gains or losses was the difference between that price, or any subsequent purchase price, and the sale price, using the indexation allowance for inflation. However, this indexation allowance was frozen at 5 April 1998, and replaced by a taper relief. Taper relief, however, cannot create or increase a loss. Any shareholder uncertain of his or her position is recommended to seek expert advice.
- **ISAs/PEPs** The Ordinary shares of the Company are qualifying investments for individual saving accounts and personal equity plans. PEPs ceased to be available for further investment from 5 April 1999. Any individual contemplating investment should consult his or her own adviser.

Herald is an investment trust. Investment trusts offer investors the following:

- Participation in a diversified portfolio of shares.
- Constant supervision by experienced professional managers.
- The Company is free from capital gains tax on capital profits realised within the portfolio.
- The opportunity to achieve improved performance for shareholders' funds in rising markets by the borrowing of additional money.

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