SC 7058

Scottish Mortgage Investment Trust PLC

Annual Report and Accounts 2004

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The World and the Scottish Thistle
(Cirsium Vulgare)
These emblems represent both our global reach and our Scottish origins. From an Edinburgh base, we have invested throughout the world since 1909.

Company data at 31 March 2004

Total assets	Shareholders' funds	Market capitalisation
£1,355m†	**£1,128m**	**£907m**

†before deduction of debentures and short term borrowings.

Company Summary

Scottish Mortgage is one of the largest investment trust companies in the UK. Its objective is to maximise total return whilst also generating real dividend growth.

Policy and Objective
Scottish Mortgage's objective is to maximise total return whilst also generating real dividend growth.
We invest internationally but with a core of exposure to the UK market. Our equity portfolio is relatively concentrated. We look to buy and hold strong businesses with good prospects for growth. We do not replicate regional indices but instead manage the portfolio and gearing levels actively; our focus is on identifying outstanding global investments.

Benchmark
The portfolio benchmark against which performance is measured is 50% FTSE All-Share Index and 50% FTSE World Ex UK Index (in sterling terms).

Management Details
Baillie Gifford & Co is appointed as investment managers and secretaries to the Company. The management contract can be terminated at 12 months' notice.

Capital Structure
At the year end the Company's share capital consisted of 297,305,115 ordinary shares of 25p each which were issued and fully paid. During the year the Company bought back 700,000 shares for cancellation. Long term gearing has been secured by the issue of £146 million (nominal value) of debenture stocks.

Management Fee
Baillie Gifford & Co's annual remuneration is 0.32% of total assets less current liabilities (excluding short term borrowings for investment purposes), calculated and payable on a quarterly basis.

ISA/PEP
ISA and PEP transfer facilities are available (see inside back cover).

AITC
The Company is a member of the Association of Investment Trust Companies, of which it was one of the founder members in 1932.

Notes
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 as such are not authorised or regulated by the Financial Services Authority.

Year's Summary

The following information illustrates how an investment in Scottish Mortgage has performed relative to its benchmark over the year to 31 March 2004.

	31 March 2004	31 March 2003	% change
Total assets (before deduction of debentures, long and short term borrowings)	£1,355.3m	£1,051.5m	
Loans and Debentures	£227.5m	£207.2m	
Equity shareholders' funds	£1,128.8m	£844.3m	
Net asset value per ordinary share (after deducting debentures at par)	381.5p	285.5p	33.6
Net asset value per ordinary share (after deducting debentures at market value)	362.8p	268.0p	35.4
Share price	305.0p	234.5p	30.1
FTSE All-Share Index	2,197.0	1,735.7	26.6
FTSE World Ex UK Index (in sterling terms)	235.4	191.8	22.7
FTSE World Index (in sterling terms)	238.1	194.0	22.7
Benchmark composite index			24.7
Dividend per ordinary share	7.00p	6.60p	6.1
Earnings per ordinary share	8.05p	7.43p	8.3
Expense ratio	0.60%	0.49%	
Discount (after deducting prior charges at par)	20.1%	17.9%	
Discount (after deducting prior charges at market value)	15.9%	12.5%	

	Year to 31 March 2004		Year to 31 March 2003	
Year's high and low	High	Low	High	Low
Share price	318.5p	234.5p	369.0p	212.3p
Net asset value	392.0p	285.5p	423.6p	263.8p
Discount	15.8%	20.6%	11.7%	21.4%

	31 March 2004	31 March 2003
Total return per ordinary share		
Revenue	8.05p	7.43p
Capital	94.86p	(141.69p)
Total	**102.91p**	**(134.26p)**

Past performance is no guarantee of future performance.

One Year Performance

(figures rebased to 100 at 31 March 2003)

Five Year Summary

The following charts indicate how an investment in Scottish Mortgage has performed relative to its benchmark (applied retrospectively), its underlying net asset value and the retail price index over the five year period to 31 March 2004.

5 Year Total Return Performance

(figures rebased to 100 at 31 March 1999)

Dividend and RPI Growth

(figures rebased to 100 at 31 March 1999)

Annual Net Asset Value and Share Price Total Returns (relative to the *benchmark total return)*

Discount to Net Asset Value

(plotted on a monthly basis)

Past performance is no guarantee of future performance.

highlights

- During the year, equity markets generally recovered strongly. *The benchmark rose by 24.7%.*
- Net asset value per share rose by 33.6%, 9 percentage points ahead of the benchmark.
- Exposure to Asian and Emerging Markets increased considerably during the year.

Chairman's Statement

In a year when equity markets made a strong recovery, our Company significantly outperformed its benchmark index. Net asset value per share rose by 33.6% compared to a 24.7% increase in the benchmark (50% FTSE All-Share and 50% FTSE World Ex UK (in sterling terms)). Our share price rose by 30.1%.

Having paid a regular interim dividend of 2.2p and a second interim dividend of 4.4p, the Board is recommending a final dividend of 0.4p making a proposed total for the year of 7.0p; a 6.1% increase compared to a 2.6% rise in inflation (RPI).

The total return (revenue and capital combined) per ordinary share this year was 102.9p (2003 – (134.3p)). In percentage terms, the total return was 36.8% while the benchmark index total return was 28.1%.

These results reflect two enduring strengths of Scottish Mortgage:

- its truly global perspective
- the active approach taken by the Managers.

Market Background

Global equity markets recovered considerably during the first three quarters of our financial year with the pace slackening somewhat in the final quarter. The recovery was reflected in generally better corporate earnings, especially in the United States, an improvement in the outlook for many economies helped by low interest rates and the boost given to the global economy by continued rapid Chinese growth. Two striking features of the period were the weakness of the US dollar and the strength of metal and commodity prices.

Investment Performance and Activity

The good performance of our Company relative to its benchmark can be accounted for by a combination of:

- the benefits from the investment of borrowings
- the decisions taken on where to allocate assets throughout the world (most notably through greater exposure to Emerging Markets and Asia)
- the generally good choice of shares by the Managers.

Performance attribution details can be found with the Managers' Overview on pages 10 and 11. Past performance is no guarantee of future performance.

Being able to borrow funds to invest in equities, or other assets, has been a distinct advantage for the trust this year. Carrying gearing into rising equity markets made a good contribution to the overall performance. As gearing can adversely affect performance in falling markets, it is important that it is actively managed and adjusted to suit circumstances, and this we have done. During the year we borrowed an additional £25m (denominated first in Swiss francs and subsequently in US dollars) to take advantage of the prospects for equity market recovery. Net investment of £20m was made into equities funded largely through sales of fixed interest holdings. As a percentage of total assets, exposure to fixed interest and cash fell from 9.1% to 7.3% over the course of the year.

In geographic terms, we continued to increase the Asian (excluding Japan) and Emerging Markets content which rose sharply from 8.8% of total assets to 14.4%. We continue to see the opportunities in many of these rapidly expanding economies as more attractive over the longer term than those available in the majority of developed countries.

The Company was underweight in the United States, relative to its benchmark, throughout the period. While there was a strong rebound in corporate profitability in the US, the weakness of the dollar diminished market gains in sterling terms. Exposure to the UK market was reduced as more attractive investment opportunities were found overseas. However, we note that the UK equity market does offer an above average yield and reasonable prospects for renewed dividend growth.

Balance Sheet

While more short term debt was taken out, no changes were made to the long term debt which, when priced at market value, now accounts for a reduced 14.9% (18.8%) of total assets following the rise in markets over the period. If our debentures are valued at current market prices rather than at par the net asset value would fall to 362.8p compared to an unadjusted 381.5p. We will continue to manage the Balance Sheet by offsetting the debt against appropriate classes of assets and adjusting this balance in the light of prevailing conditions.

Repurchase of Shares

A total of 700,000 shares were bought back at a cost of £1.8m. While we are not convinced that there is a direct correlation between the level of discount and buyback activity, we will be asking shareholders to renew the mandate to repurchase up to 15% of the then outstanding shares at the AGM. Buybacks can benefit shareholders by enhancing NAV per share for continuing shareholders.

Marketing

Large global investment trusts can be excellent vehicles for long term investment and savings. Scottish Mortgage gives investors exposure to a diversified global portfolio under very experienced management at a reasonable cost. It has a good track record in comparison with its large peers in the global growth sector, especially so over the past year.

Significant resources were devoted to marketing to attract new investors and levels of activity have been high. The Managers are looking at ways to accelerate progress in this area and further initiatives can be expected in the current year.

Board and AGM

I am pleased to welcome Michael Gray and Lord Strathclyde to the Board. Both are extremely experienced in their respective fields of business and politics and I am sure that they will make a valuable contribution to the Company in the years ahead. I would also like to express the Board's gratitude to Lord Portarlington who is retiring at the AGM having served on the Board for 7 years. During his term, I know that his balanced viewpoint and carefully considered opinions have been of considerable benefit to both myself and my predecessor.

I have pleasure in inviting shareholders to the AGM which will be held on 1 July in Edinburgh. Details are given on page 50 of this document.

Outlook

The global economy is currently buoyant. This has allowed stockmarkets to recover from the prolonged bear market. Further progress will depend on the continuance of healthy and non-inflationary growth in America and China. At present growth in both economies is sufficiently strong to reassure those looking for corporate earnings growth but also to alert markets to the probability of tightening in monetary policy. Scottish Mortgage will manage your investments actively in the hope that we can again report good results in 12 months' time.

Sir Donald MacKay

Sir Donald MacKay
10 May 2004

Directors and Management

Members of the Board come from a broad variety of backgrounds. The Board can draw on a very extensive pool of knowledge and experience. Baillie Gifford & Co, a leading UK investment management firm, who act as Managers and Secretaries to the Company have done so since its formation in 1909.

Directors

1 Sir Donald MacKay

Donald MacKay is 67 and was appointed a Director of Scottish Mortgage Investment Trust PLC in 1999, became Chairman in 2003 and is Chairman of the Nomination Committee. He is an economist who was Professor of Political Economy at Aberdeen University and Professor of Economics at Heriot-Watt University. He is a former chairman of The Malcolm Group PLC and Scottish Enterprise and is currently a director of Edinburgh Income and Value Trust plc.

2 GA Ball

Geoffrey Ball is 60 and was appointed a Director of Scottish Mortgage Investment Trust PLC in 1983 and is the senior independent director. He is executive chairman of CALA Group Ltd, having led the Management Buy Out in 1999. He was president of the House Builders Federation of England and Wales from 2001 to 2003. He was a director of The Standard Life Assurance Company for 13 years until 2001.

3 MM Gray

Michael Gray is 56 and was appointed a Director of Scottish Mortgage Investment Trust PLC on 26 February 2004. As Chairman and Chief Executive he led the growth of McQueen International over a 17 year period as it evolved from being a printing company into a global enterprise providing a range of support services to technology companies. On McQueen's acquisition, he became Senior Vice-President of Sykes Enterprises Inc., a global NASDAQ quoted outsourcing services company. He retired from Sykes in 1999 and currently has many business, community, charity and sporting interests and responsibilities. He is a director of the Scottish Community Foundation and a former director of Scottish Enterprise.

4 WG McQueen

Gordon McQueen is 57 and was appointed a Director of Scottish Mortgage Investment Trust PLC in 2001 and is Chairman of the Audit Committee. He was an executive director of HBOS plc, Bank of Scotland and Halifax plc, where his chief role was Chief Executive, Treasury.

5 The Earl of Portarlington

George Portarlington is 65 and was appointed a Director of Scottish Mortgage Investment Trust PLC in 1997. He is a former director of Queensland Trading and Holding Company Limited of Brisbane and of Cold Storage Holdings Limited of Singapore.

6 JPHS Scott

John Scott is 51 and was appointed a Director of Scottish Mortgage Investment Trust PLC in 2001. He is a former executive director of Lazard Brothers & Co. Limited. During his twenty years with Lazard, he was deeply involved with the merchant bank's Asian activities. He is currently a director of various companies, including Dunedin Income Growth Investment Trust PLC, Martin Currie Pacific Trust plc, Xaar plc, Miller Insurance, Albany Venture Managers and Schroder Japan Growth Fund plc.

7 Lord Strathclyde

Thomas Strathclyde is 44 and was appointed a Director of Scottish Mortgage Investment Trust PLC on 26 February 2004. He is currently the Leader of the Opposition in the House of Lords. His parliamentary career to date includes extensive ministerial experience at the Departments of Employment, the Environment, Trade and Industry and the Scottish Office. Prior to entering politics in 1988 as a Government Whip, Lord Strathclyde worked in the City for the insurance brokers, Bain Dawes. Lord Strathclyde is also Chairman of London based hedge fund manager Trafalgar Capital Management Limited and a Director of Trafigura Asset Management Limited.

All Directors are members of the Nomination and Audit Committees.

Managers and Secretaries

Scottish Mortgage is managed by Baillie Gifford & Co, an investment management firm formed in 1927 out of the legal firm Baillie & Gifford, WS, which had been Managers and Secretaries to the Company since its formation in 1909.

Baillie Gifford is one of the largest investment trust managers in the UK and currently manages eight investment trusts. Baillie Gifford also manages unit trusts and open ended investment companies, together with investment portfolios on behalf of pension funds, charities and other institutional clients, both in the UK and overseas. Funds under the management or advice of Baillie Gifford total around £28 billion. Based in Edinburgh, it is one of the leading privately owned investment management firms in the UK, with 27 partners and a staff of over 400. It won both the Investment Week 'Investment Trust Group of the Year' award (for the second year running) and also the Investment Trusts Magazine 'Group of the Year' award. There is no guarantee that Baillie Gifford's past performance will be repeated in the future.

The manager of Scottish Mortgage's portfolio is James Anderson, a partner of Baillie Gifford. Stock selection is primarily the responsibility of specialist teams covering all the regions of the world.

The firm of Baillie Gifford & Co is authorised and regulated by the Financial Services Authority.

Returns From Markets
for the year ended 31 March 2004
Geographical performance against*
benchmark in local currency

Managers' Overview

It is pleasant to be able to report on a much improved year. This comes as a relief after the prolonged bear market but we are particularly pleased that we have been able to exceed the benchmark returns by a considerable margin.

Part of our success stemmed from maintaining our gearing. It need scarcely be said that the experience of recent years has made us very conscious of both the dangers and opportunities inherent in long term borrowings. We have made significant improvements in our bond capabilities in recent years and this should allow us to handle our borrowing levels more effectively and consistently in the years ahead with the guidance of the Board.

At a geographical asset allocation level we have continued to benefit from our rising exposure towards Asia and Emerging Markets. We think that this reflects an historic shift in the global economy that will dominate the investment scene of the next 20 years. There will, of course, be interruptions to this process as politics, valuations and – above all – economic cycles play out and we will try to take account of these whilst keeping the strategic picture firmly in mind.

For the third year in a row overall stock selection has been positive. UK performance continued its consistent record whilst the contributions from Asia and Emerging Markets selection were noteworthy and that from Europe a relief after a period of poor performance. There were no major areas of concern with both America and Japan performing in line with their regional indices. We regard all these figures with a degree of interest but it is far more important to consider the overall stock selection picture as we view the Trust's portfolio on an integrated global basis. We have, for example, added significantly to our returns by moving our oil exposure away from the UK towards Emerging Markets.

Our current view is that world economic growth will be strong in the year ahead and that corporate earnings are likely to continue to rise. We see some signs of renewed dividend growth which is refreshing. Whilst the global political scene remains of serious concern we think that the decisive issues in the year ahead will prove to be the sustainability of strong growth with low inflation. Britain is no exception to this issue but developments in America and China will be critical. We are cautiously optimistic.

Performance Attribution for the year to 31 March 2004

Computed relative to the benchmark (50% FTSE All-Share Index and 50% FTSE World Ex UK Index (in sterling terms)) with net income reinvested.

Performance Attribution (in sterling terms)

	Benchmark		Scottish Mortgage		Performance*		Contribution to relative	Contribution attributable to: Stock	Asset†
	01.04.03	31.03.04	01.04.03	31.03.04	SM	Benchmark	return	selection	allocation
Portfolio breakdown	%	%	%	%	%	%	%	%	%
UK	50.0	50.0	54.9	50.5	32.4	31.0	0.7	0.6	0.1
Europe ex. UK	9.5	9.8	10.8	10.7	42.3	36.9	0.5	0.4	0.1
North America	32.5	30.5	29.4	26.1	17.3	16.8	0.4	0.1	0.4
Japan	4.3	5.4	5.5	6.8	46.3	46.5	0.2	–	0.2
Asia Pacific ex. Japan	3.0	3.4	6.2	11.0	45.4	40.6	0.6	0.2	0.4
Other Emerging Markets	*0.7*	*0.9*	*4.7*	*6.3*	*75.9*	*54.0*	*1.7*	*1.0*	*0.7*
Bonds	–	–	11.0	7.2	12.5	–	(1.3)	–	(1.3)
Cash	–	–	0.9	1.0	12.1	–	(0.4)	–	(0.4)
Debentures and Loans	–	–	(23.4)	(19.6)	4.1	–	4.4	–	4.4
Total	**100.0**	**100.0**	**100.0**	**100.0**	**36.8**	**28.1**	**7.0**	**2.2**	**4.7**

Past performance is no guarantee of future performance.

Source: HSBC/Baillie Gifford & Co

* The above returns are calculated on a total return basis with net income reinvested. Scottish Mortgage's figures represent the returns on the Company's portfolio and the benchmark figures for each geographical area represent the return on the appropriate FTSE index.

Contributions cannot be added together as they are geometric; for example to calculate how a return of 36.8%, against a benchmark return of 28.1% translates into a relative return of 7.0%, divide the portfolio return of 136.8 by the benchmark return of 128.1 and subtract one.

† Asset allocation includes the contribution attributable to currency movements.

Investment Changes (£'000)

	Valuation at 31 March 2003	Net acquisitions (disposals)	Appreciation (depreciation)	Valuation at 31 March 2004
Equities*:				
UK	470,559	(32,127)	131,145	569,577
Continental Europe	92,750	(8,643)	36,370	120,477
North America	252,417	2,114	40,070	294,601
Japan	47,508	7,072	22,696	77,276
Asia Pacific	52,992	48,877	22,420	124,289
Other Emerging Markets	40,124	2,958	27,900	70,982
	956,350	20,251	280,601	1,257,202
Sterling bonds	65,797	(12,009)	4,271	58,059
Euro bonds	25,248	(6,229)	1,032	20,051
US dollar bonds	3,353	48	(217)	3,184
Total investments	1,050,748	2,061	285,687	1,338,496
Net liquid assets	797	16,159	(111)	16,845
Total assets	**1,051,545**	**18,220**	**285,576**	**1,355,341**

The figures above for total assets are made up of total net assets before deduction of debentures, long and short term borrowings.

* Equities include convertibles, warrants, limited partnerships and OEICs.

Distribution of Portfolio

Geographical 2004 (2003)

Other Emerging Markets 5.2% (4.0%)

Asia Pacific 9.2% (5.0%)

Japan 5.7% (4.5%)

UK 47.5% (50.4%)

North America 21.9% (24.3%)

Continental Europe 10.5% (11.8%)

Sectoral 2004 (2003)

Net Liquid Assets 1.3% (0.1%)

Overseas Bonds 1.7% (2.7%)

Sterling Bonds 4.3% (6.3%)

Resources 9.1% (9.1%)

Industrials 9.1% (6.3%)

Information Technology 6.1% (7.2%)

Financials 28.0% (26.7%)

Consumer Goods 22.1% (22.5%)

Services and Utilities 18.3% (19.1%)

Thirty Largest Equity Holdings

Name	Region	Business	Market value £'000	% of total assets
†Vodafone	United Kingdom	Mobile telecommunication services	61,058	4.5
Royal Bank of Scotland	United Kingdom	Banking	41,898	3.1
GlaxoSmithKline	United Kingdom	Pharmaceuticals	38,250	2.8
Barclays	United Kingdom	Banking	32,544	2.4
HSBC	United Kingdom	Banking	31,292	2.3
British American Tobacco	United Kingdom	Tobacco	25,987	1.9
Golden West Financial	North America	Savings and loans	24,365	1.8
Wellpoint	North America	Managed care	23,203	1.7
Man Group	United Kingdom	Hedge fund manager and asset gatherer	21,303	1.6
Aviva	United Kingdom	Life assurance	20,191	1.5
Diageo	United Kingdom	Branded spirits	19,285	1.4
Omnicom	North America	Advertising agency	19,038	1.4
Samsung Electronics	Asia Pacific	Electronics manufacturer	19,003	1.4
Moody's	North America	Bond rating agency	18,760	1.4
Prudential	United Kingdom	Life assurance	17,947	1.3
Altria	North America	Tobacco and food	17,568	1.3
Imperial Tobacco	United Kingdom	Tobacco	16,865	1.2
Nokia	Continental Europe	Mobile telecommunications equipment	16,160	1.2
Wolseley	United Kingdom	Builders' merchant	15,792	1.2
Pfizer	North America	Pharmaceuticals	15,676	1.2
BHP Billiton	Asia Pacific	Diversified resources	15,278	1.1
Suncor Energy	North America	Oil company	15,264	1.1
Allied Domecq	United Kingdom	Branded spirits	14,650	1.1
Atlas Copco	Continental Europe	Engineering	14,541	1.1
HBOS	United Kingdom	Banking	14,509	1.1
SAP	Continental Europe	Business software	14,255	1.0
Norilsk Nickel	Other Emerging Markets	Mining company	13,790	1.0
Carnival	United Kingdom	Cruise ship operator	13,283	1.0
BMW	Continental Europe	Automobiles	12,954	1.0
BG Group	United Kingdom	Oil and gas exploration and production	12,932	1.0
			637,641	**47.1**

† Includes holding partly in convertible loan stock.

Classification of Investments

Classification	UK %	Continental Europe %	North America %	Japan %	Asia Pacific %	Other Emerging Markets %	2004 Total %	2003 Total %
Equities*:								
Mining	–	–	–	–	1.1	1.4	2.5	1.8
Oil and gas	1.0	0.6	1.1	–	1.1	2.8	6.6	7.3
Resources	1.0	0.6	1.1	–	2.2	4.2	9.1	9.1
Chemicals	0.6	–	–	0.3	–	–	0.9	0.5
Construction and building materials	2.1	–	–	0.4	–	–	2.5	3.2
Diversified industrials	–	–	–	–	0.4	–	0.4	0.6
Electronic and electrical equipment	–	0.4	–	1.2	1.8	–	3.4	1.3
Engineering and machinery	0.4	1.5	–	–	–	–	1.9	0.7
Industrials	3.1	1.9	–	1.9	2.2	–	9.1	6.3
Automobiles	–	1.6	–	0.4	0.7	–	2.7	1.2
Household goods and textiles	–	–	0.9	–	–	–	0.9	–
Beverages	2.5	–	–	–	–	–	2.5	3.1
Food producers and processors	–	–	1.4	–	–	–	1.4	1.2
Healthcare and pharmaceuticals	3.9	–	3.8	0.2	0.2	0.6	8.7	12.0
Personal care and household products	–	0.5	–	–	–	–	0.5	0.4
Tobacco	4.1	–	1.3	–	–	–	5.4	4.6
Consumer Goods	10.5	2.1	7.4	0.6	0.9	0.6	22.1	22.5
Retailers	–	0.4	1.9	0.4	–	–	2.7	3.7
Leisure and hotels	1.5	–	0.4	–	–	–	1.9	1.1
Media and entertainment	1.4	–	1.4	–	0.2	–	3.0	4.4
Support services	2.1	–	0.6	–	–	–	2.7	2.3
Transport	–	–	–	0.5	1.3	–	1.8	0.4
Telecommunication services	4.5	–	–	0.5	–	0.4	5.4	6.5
Electricity	0.8	–	–	–	–	–	0.8	0.7
Services and Utilities	10.3	0.4	4.3	1.4	1.5	0.4	18.3	19.1
Banks	9.4	–	0.8	0.7	1.0	–	11.9	11.7
Insurance	0.2	–	0.9	–	–	–	1.1	1.8
Life assurance	2.8	–	–	–	–	–	2.8	1.9
Investment companies	0.7	0.9	–	–	–	–	1.6	2.5
Real estate	0.9	–	–	–	0.7	–	1.6	0.5
Other financial	2.1	–	5.6	0.9	0.4	–	9.0	8.3
Financials	16.1	0.9	7.3	1.6	2.1	–	28.0	26.7
Information technology hardware	0.5	1.9	0.7	0.2	0.3	–	3.6	3.0
Software and computer services	0.5	1.1	0.9	–	–	–	2.5	4.2
Information Technology	1.0	3.0	1.6	0.2	0.3	–	6.1	7.2
Total Equities*	**42.0**	**8.9**	**21.7**	**5.7**	**9.2**	**5.2**	**92.7**	
Total Equities* – 2003	44.8	8.8	24.0	4.5	5.0	3.8		90.9
Bonds	4.3	1.5	0.2	–	–	–	6.0	9.0
Net Liquid Assets	1.2	0.1	–	–	–	–	1.3	0.1
Total Assets (before deduction of debentures and short term borrowings)	**47.5**	**10.5**	**21.9**	**5.7**	**9.2**	**5.2**	**100.0**	
Total Assets – 2003	50.4	11.8	24.3	4.5	5.0	4.0		100.0
Debentures, Long and Short Term Borrowings	(11.2)	–	(3.3)	–	(2.3)	–	(16.8)	(19.7)
Equity Shareholders' Funds	**36.3**	**10.5**	**18.6**	**5.7**	**6.9**	**5.2**	**83.2**	
Equity Shareholders' Funds – 2003	35.9	11.8	24.3	(0.7)	5.0	4.0		80.3
Number of equity investments*	**42**	**12**	**24**	**16**	**18**	**8**	**120**	129

* Including convertibles, warrants, limited partnerships and OEICs.

1 Vodafone

The huge popularity of picture *messaging is helping grow* revenues and profits at Vodafone. Picture courtesy of Vodafone.

2 Wolseley

Wolseley has seen strong demand *in the US for its timber products* which are widely used in residential construction. Picture courtesy of Wolseley.

United Kingdom

In common with other stockmarkets around the world, UK share prices staged a very welcome recovery in the year to 31 March. We believe this rise in share prices is well-founded. Though an important element of the recovery is the increased willingness of *investors to own sometimes volatile assets*, there has also been an improvement in profitability at many companies. We are also encouraged by the fact that, after a long period of rather paltry distributions, the average rate of dividend increase from UK companies has begun to accelerate.

The performance of the Company's UK investments was strong in absolute terms and tolerably good when compared to the wider UK market – the Company's UK investments returned 32.4% which compares to the total return on the FTSE All-Share of 31.0%. Many holdings saw exceptional gains in their share prices, most notably the hedge fund manager Man Group, the building materials distributor Wolseley and the cruise-line operator Carnival. It is particularly encouraging that these share price gains have been accompanied by operational performance that either met or exceeded our initial expectations. The Company also profited from additions to more cyclical stocks such *as the electronics group Spirent and the* publishing company United Business Media.

Inevitably there were parts of the portfolio that shone less brightly. Where this was felt to reflect a fundamental disappointment in the business, the holding has been sold. However, we have been reluctant to dispose of long-standing investments which *have performed well operationally simply* because their share price has lagged the market during the last 12 months. Vodafone, for example, delivered a total return half that of the market but we believe the likely progress in its earnings will reward handsomely the patient investor and we have therefore increased the holding. Similarly, the number of shares held in Royal Bank of Scotland is higher now than a year ago. The investments in tobacco companies which, in aggregate, lagged the market return have also been increased.

The net effect of transactions though has been to reduce the Company's exposure to the UK market. Primarily, this has been a function of views on individual stocks and the fact that, whenever our enthusiasm for a particular UK-domiciled company waned, we did not automatically seek to reinvest the proceeds of any sale into other UK companies but instead looked to where that money can *be most profitably invested regardless of* geographic domicile.

The clearest example of this effort is the transactions in the UK oil majors, BP and Shell. Having begun the period under review with some £34m invested in these stocks, Scottish Mortgage no longer has any money invested in either of the *two companies. We are not persuaded* that either company can provide the investor with a total return in excess of that offered by the wider UK market. Instead, any enthusiasm for oil exposure has been channelled into other companies, often domiciled in developing countries, whose production prospects appear stronger and whose valuations are usually lower.

The other aspect to the reduction in UK exposure, though less important an influence than stock specific views, is that the duration and extent of the earnings recovery in the UK may prove less than that in other markets. The British economy has been relatively robust in recent years and this means there is less scope for a cyclical rebound in earnings. The economy has also been supported by enthusiastic borrowing on the part of consumers. The gradual tightening of monetary policy that the Bank of England appears to have *embarked on is likely to restrain this hitherto* important contributor to growth.

1 MAN

This MAN B&W Diesel two-stroke engine with a piston diameter of 98 cm ranks among the largest diesel engines in the world, being constructed mainly by Asian licensees. Picture courtesy of MAN.

2 ABB

The revolutionary AZIPOD drive system is fitted to the outside of the hull of a ship, and can be rotated through 360 degrees. It allows large ships to manoeuvre in small spaces, making tugs unnecessary. Picture courtesy of ABB.

Continental Europe

European stocks rose sharply in the year under review. The European economy deserves very little credit for this as the global recovery was barely perceptible in continental data. Some of the responsibility for this depressing state of affairs lies with the appreciation of the Euro but it has been disappointing that previously relatively buoyant economies such as France have succumbed to the widespread stagnation and that even Ireland has shown only moderate growth. The strength of European markets was instead a reflection of the intense sensitivity of many continental companies to the progress of the global rather than regional economy. For many of the more successful companies this has allowed sales and profitability to benefit from the boom in Asia whilst for others falling global interest rates and risk premiums have allowed balance sheet restructuring and an end to threatened insolvency. We have concentrated on the higher quality set of these companies but we have also profited from the marked recovery in troubled shares such as Ericsson. In combination this has enabled us to outperform the regional benchmark and to contribute to the overall performance of the Trust.

Looking forward to the year ahead we see little evidence that European growth is likely to accelerate. We therefore intend to retain our focus on companies that have the geographical range and competitive strengths to enable them to flourish globally. Long-standing examples of this approach include the French hair care giant L'Oreal and the luxury goods company Hermes. Perhaps less predictably we would make similar claims for several European industrials. For instance, BMW and Porsche both seem to us to exemplify brand strengths that comfortably transcend the limitations of the German domestic market. Equally the manufacturing skills and broad international operations of Atlas Copco, MAN and a revived ABB appear to us to offer good earnings growth rates and low valuations. SAP has thus far demonstrated the market leadership and growth potential to show that there are some areas of technology where Europe can compete but the faltering efforts of Nokia have disappointed us.

Given the unpromising economic and political prospects we see little reason to expand our European holdings. We much prefer to focus on the small selection of companies that appear to us to be both globally competitive and attractively rated than to build an entire portfolio of stocks that gives broad exposure to continental equities and economies. We hope that this approach will again be successful in the year ahead.

1 Wendy's

The Tim Hortons Coffee Shop chain is owned by Wendy's International. Picture courtesy of Wendy's.

2 Iron Mountain

An Iron Mountain driver on his rounds. Picture courtesy of Iron Mountain.

North America

The US economy grew rather faster than expected last year as tax cuts and mortgage refinancing boosted consumer spending. The scope for further such stimulus appears limited – the budget deficit is approaching 5% of GDP and interest rates are expected to rise this year – and so we would expect to see some slowing in personal consumption growth in the medium term.

It is therefore encouraging that the corporate sector is showing signs of life. Profits have now been rebounding for two and a half years and while executives' language remains cautious, their actions have become a little bolder – there has been a pick-up in mergers and acquisitions activity and advertising and capital spending are rising gently.

There were a number of new purchases during the year. Iron Mountain is the dominant record management company in the US and UK. After a decade of heavy investment the business's strong and growing cashflows should increasingly be returned to shareholders. T Rowe Price is a conservatively-run investment manager which is unusual among its listed peers in having grown largely without making acquisitions and which is currently taking share in the mutual fund market. Mohawk is the leading US producer and distributor of floor coverings. In recent years it and a subsidiary of Berkshire Hathaway have consolidated the industry and now control 70% of the carpet market between them. Loblaw is a well-run Canadian supermarket chain with attractive growth prospects.

The most notable sale was of the semiconductor company, Analog Devices. Despite additions to the Company's remaining American tech stock, Microchip, this sale resulted in a further reduction in the Company's already limited exposure to the US technology sector. While technology demand continues to recover, we remain concerned about valuations: the technology sector is trading on a large premium to the rest of the market, particularly when options are expensed.

The US market rallied strongly during the year as optimism over the economic and profit cycles grew. Despite having very little exposure to the most cyclical parts of the economy, the Company's North American portfolio marginally outperformed the market, thanks largely to very solid profit growth from large holdings like Golden West Financial, Wellpoint and Moody's. In aggregate the Company's North American investments remain both considerably more profitable and no more expensive than the market as a whole and we expect them to continue to grow profits faster than the market over extended periods. Whilst there will be further individual stock changes in the portfolio these characteristics should remain intact.

1 Canon

At Canon, demand for colour *photocopiers is rising.* Picture courtesy of Canon.

2 Asahi Glass

Asahi Glass manufactures *glass for TV displays.* Picture courtesy of Asahi Glass.

Japan

1

2

Japanese equities finally returned to form in the year under review with Tokyo offering the best return amongst developed market indices with a gain of 50% in local currency terms. This followed a fall that had taken the main equity indices to their lowest levels in nearly 20 years by March 2003.

The relatively modest economic expansion that began in 2002 continued last year. Industrial production rose further, helped by export demand and rising private capital spending. Unemployment fell, although private consumption has been steady rather than buoyant over the last year. In addition, nominal GDP growth is not yet clearly positive, as price levels have continued to fall in certain areas. The outlook for prices is one of the more interesting issues for Japan at the moment. Over the past decade, and particularly in recent years, falling prices have depressed profitability and exacerbated the banking sector's troubles. Recent trends in some property prices and consumer prices suggest that downward pricing pressure has eased, although it is too early to confidently project a sustained period of rising prices.

The situation in the banking sector remains pivotal. The sector's health is improving and perceptions have changed dramatically over the course of the year to the considerable benefit of our holding in UFJ. The effective bailout of Resona by the government in the spring of 2003 was critical, and the larger banks have also made some progress in increasing their profitability. A reduction in debt levels at the most highly geared companies have also contributed to an improvement in the quality of the banking sector's loan portfolios.

The remainder of the Trust's investments are mainly concentrated in Japanese companies that boast a record of successful expansion. These include holdings in companies with globally competitive businesses, such as Canon and Toyota Motor, or in those with very strong domestic positions, such as consumer products manufacturer Kao. However, changes in management style are widespread, and provide opportunities to invest in businesses with latent strengths but erratic track records. For example, we purchased a holding for the Trust in Tokyu Corporation, a collection of operating businesses with a private railway company its core. The value of these assets is being enhanced by various management improvements, although the better environment is acting as a tailwind. We will continue to look for similar situations, whatever path the economy takes next.

1 BHP Billiton

BHP Billiton is one of three dominant global players in iron ore. Picture courtesy of BHP Billiton.

2 CNOOC

CNOOC has a unique position in the Chinese offshore oil industry. Picture courtesy of CNOOC.

1

2

Asia Pacific and Other Emerging Markets

It has been a remarkable period in the Asia Pacific region and the other emerging markets. For the first time markets have begun to recognise the full impact of Chinese growth. 2004 may also turn out to be the year in which the crippling deflation in some Asian economies, most notably Hong Kong, finally comes to an end. Elsewhere declining risk premiums and improved economic management have allowed India, Russia and Brazil to prosper.

The most notable feature of markets globally has been the accrual of pricing power to producers of raw materials and energy, as Chinese demand has surged. Our portfolio has benefited from this powerful trend through holdings such as Petrobras, Lukoil, Norilsk Nickel and BHP Billiton. A note of caution may be due now, as the current high returns in these industries are bound to attract substantial new supply. Nevertheless, we think that a substantial position in certain energy and commodity stocks may be warranted for some considerable time.

We have made some increases to our direct Chinese investments, for instance with new purchases of Zhejiang Expressway and Sinotrans, the freight forwarder. Although there is some risk of slowing activity over the next year, we believe that some of the most exciting individual long term growth stocks are becoming apparent as Chinese companies develop the management capabilities to exploit the inherent growth of their markets. We have continued to be encouraged by the growth that India is now producing. We have replaced our successful holding in the State Bank with Oil and Natural Gas Corporation on price grounds.

Comfortably our largest individual holding in the region is in Samsung Electronics. Once again this company has exceeded forecasts and has prospered in each of its major business segments. We continue to add to our position as despite its excellent stock price performance the rating still seems abnormally cheap in a global context.

We will be surprised if the year ahead offers such smooth progress as we have recently enjoyed. A period of nerves over Chinese economic overheating or Russian politics is probably overdue, whilst rising global interest rates are seldom helpful to volatile assets in Asia and Emerging Markets. We intend to use any such periods of nervousness to add to our exposure to these regions as we strongly believe that the economic and corporate opportunities available are still highly attractive in the years ahead.

1 Avio

Avio is part of the Arianespace consortium, the world's largest satellite launcher. Picture courtesy of Avio.

2 Messer Griesheim

Messer Griesheim, the German industrial gases company, was acquired by its larger, better rated competitor Air Liquide. Picture courtesy of Air Liquide.

Fixed Interest

1

2

The general economic and financial climate was beneficial for Scottish Mortgage's bond portfolio in the year to 31 March and we are pleased to report a 12.5% return on the Trust's portfolio. Growth was stronger than anticipated almost everywhere but the slack in the economy and the impact of Asian production kept a lid on inflation. This mix of improved growth and low inflation is perfect for corporate bonds. It allows companies to enhance their credit ratings without inflationary fears hurting bond markets.

Our preference through the year has been to buy bonds with a positive exposure to economic recovery. For example we have invested in insurance companies' bonds which have benefited both from the recovery in equity markets and an increased focus on risk management after recent painful episodes. We have also invested in a selection of high yield bonds which have performed very well due to institutional investors' shift into higher yielding assets and the sharp decline in the default rate. Our focus on companies which are expected to reduce indebtedness has also led to several success stories. For example BSkyB, Stagecoach, Castle Transmission and Messer Griesheim have all either been upgraded to investment grade or redeemed their bonds early at a premium.

Our expectation is that interest rates will continue to rise in the next 12 months in the UK and US but that this is largely reflected in bond prices. European bonds look less susceptible and we continue to favour this market. However the risk is that inflation rises more than anticipated and we will guard against this. Higher company profitability will likely be sustained and there should be ample opportunity to find companies which are reducing indebtedness in both investment grade and high yield markets. While we would be surprised to see the returns of the past two years matched, Scottish Mortgage's bond portfolio should continue to meet its objective of generating income to help offset borrowing costs while also proving an attractive investment in its own right.

Classification	Name	Business	Market value £'000	%
United Kingdom				
Oil and gas	BG Group	Exploration and production	**12,932**	1.0
Chemicals	BOC	Industrial gases supplier	**8,645**	0.6
Construction and building materials	Bellway	House builder	3,184	
	Bovis Homes	House builder	3,312	
	Redrow	House builder	3,120	
	Travis Perkins	Builders' merchant	3,183	
	Wolseley	Builders' merchant	15,792	
			28,591	2.1
Engineering and machinery	FKI	Diversified engineer	**5,889**	0.4
Beverages	Allied Domecq	Branded spirits	14,650	
	Diageo	Branded spirits	19,285	
			33,935	2.5
Healthcare and pharmaceuticals	Alliance UniChem	Pharmaceutical wholesale distributor	11,343	
	GlaxoSmithKline	Pharmaceuticals	38,250	
	Shire Pharmaceuticals	Pharmaceuticals	3,239	
			52,832	3.9
Tobacco	British American Tobacco	Tobacco	25,987	
	Gallaher	Tobacco	12,021	
	Imperial Tobacco	Tobacco	16,865	
			54,873	4.1
Leisure and hotels	Carnival	Cruise ship operator	13,283	
	William Hill	Licensed betting operator	6,761	
			20,044	1.5
Media and entertainment	Aegis	Media services	5,093	
	Trinity Mirror	Newspaper publisher	9,112	
	United Business Media	Diversified media company	4,950	
			19,155	1.4
Support services	Bunzl	Supermarket support services	8,565	
	Capita	Support services	5,928	
	Compass	Contract catering	11,623	
	Premier Farnell	Distributor of electronic components	2,303	
			28,419	2.1
Telecommunication services	†Vodafone	Mobile telecommunication services	**61,058**	4.5
Electricity	Scottish & Southern Energy	Electricity utility	**10,897**	0.8
Banks	Barclays	Banking	32,544	
	HBOS	Banking	14,509	
	HSBC	Banking	31,292	
	Royal Bank of Scotland	Banking	41,898	
	Standard Chartered	Banking	7,115	
			127,358	9.4
Insurance	Jardine Lloyd Thompson	Insurance broker	**2,105**	0.2
Life assurance	Aviva	Life assurance	20,191	
	Prudential	Life assurance	17,947	
			38,138	2.8
Investment companies	UK Balanced Property Trust	Property investment trust	**9,584**	0.7

†denotes holding partly in convertible loan stock.

Classification	*Name*	*Business*	Market value *£'000*	%
United Kingdom (continued)				
Real estate	Hammerson	Property	9,129	
	Shaftesbury	Property	3,622	
			12,751	0.9
Other financial	Intermediate Capital Group	Mezzanine finance provider	7,730	
	Man Group	Hedge fund manager and asset gatherer	21,303	
			29,033	2.1
Information technology hardware	Spirent	Telecom equipment	6,795	0.5
Software and computer services	Sage	Small business software	6,543	0.5
Total United Kingdom Equities			**569,577**	**42.0**
Continental Europe				
Oil and gas	ENI	Oil and gas – Italy	8,368	0.6
Electronic and electrical equipment	ABB	Electrical equipment – Switzerland	4,813	0.4
Engineering and machinery	Atlas Copco	Engineering – Sweden	14,541	
	MAN	Engineering – Germany	5,235	
			19,776	1.5
Automobiles	BMW	Automobiles – Germany	12,954	
	Porsche	Automobiles – Germany	9,399	
			22,353	1.6
Personal care and household products	L'Oreal	Personal care – France	6,956	0.5
Retailers	Hermes	Luxury goods – France	5,994	0.4
Investment companies	Baillie Gifford European Smaller Companies Fund	Small company fund	11,574	0.9
Information technology hardware	Ericsson	Telecommunications equipment – Sweden	10,228	
	Nokia	Mobile telecommunications equipment – Finland	16,160	
			26,388	1.9
Software and computer services	SAP	Business software – Germany	14,255	1.1
Total Continental European Equities			**120,477**	**8.9**
North America				
Oil and gas	Suncor Energy	Oil company – Canada	15,264	1.1
Household goods and textiles	*Mohawk Industries*	*Carpets*	11,717	0.9
Food producers and processors	William Wrigley	Chewing gum	7,238	
	Loblaw	Supermarkets – Canada	11,144	
			18,382	1.4
Healthcare and pharmaceuticals	Eli Lilly	Pharmaceuticals	7,644	
	Pfizer	Pharmaceuticals	15,676	
	Wellpoint	Managed care	23,203	
	Wyeth	Pharmaceuticals	5,312	
			51,835	3.8
Tobacco	Altria	Tobacco and food	17,568	1.3

Classification	Name	Business	Market value £'000	%
North America (continued)				
Retailers	Tiffany	Jeweller	11,013	
	TJX	Off-price clothing	5,613	
	Walgreen	Pharmacy chain	9,789	
			26,415	1.9
Leisure and hotels	Wendy's	Restaurants	6,088	0.4
Media and entertainment	Omnicom	Advertising agency	19,038	1.4
Support services	Iron Mountain	Document management	7,987	0.6
Banks	M & T Bank	Banking	11,440	0.8
Insurance	Marsh & McLennan	Insurance and fund management	11,840	0.9
Other financial	Freddie Mac	Mortgages	11,546	
	Golden West Financial	Savings and loans	24,365	
	Moody's	*Bond rating agency*	18,760	
	State Street	Custodian bank	11,147	
	T Rowe Price	Fund management	9,753	
			75,571	5.6
Information technology hardware	Microchip Technology	Semiconductors	9,459	0.7
Software and computer services	Automatic Data Processing	Payroll processing	11,997	0.9
Total North American Equities			**294,601**	**21.7**
Japan				
Chemicals	Konica	Office equipment and imaging	3,860	0.3
Construction and building materials	Asahi Glass	Glass	5,855	0.4
Electronic and electrical equipment	Alps Electric	Electronic components	2,545	
	Brother	Office equipment	3,016	
	Canon	Copiers and cameras	7,781	
	Keyence	Sensors	3,316	
			16,658	1.2
Automobiles	Toyota Motor	Car manufacturer	5,323	0.4
Healthcare and pharmaceuticals	Kao	Household goods	3,211	0.2
Retailers	*Yamada Denki*	*Consumer electronics retailer*	4,789	0.4
Transport	Tokyu	Rail and property	6,585	0.5
Telecommunication services	NTT	Telecommunications	2,518	
	NTT DoCoMo	Mobile telecommunications	3,771	
			6,289	0.5
Banks	UFJ	Bank	10,030	0.7
Other financial	*MAC Japan Active Shareholder Fund Limited Partnership	Shareholder activist fund	6,866	
	Promise	Consumer finance	5,048	
			11,914	0.9
Information technology hardware	Rohm	Specialist semiconductors	2,762	0.2
Total Japanese Equities			**77,276**	**5.7**

*denotes unlisted security.

Classification	Name	Business	Market value £'000	%
Asia Pacific				
Mining	BHP Billiton	Diversified resources – Australia	15,278	1.1
Oil and gas	CNOOC	Oil and gas exploration – China	12,772	
	Oil & Natural Gas Corp.	*Oil and gas exploration and production – India*	1,638	
			14,410	1.1
Diversified industrials	Li & Fung	Supply chain management – Hong Kong	5,817	0.4
Electronic and electrical equipment	Hon Hai Precision	Electronics manufacturer – Taiwan	5,332	
	Samsung Electronics	Electronics manufacturer – Korea	19,003	
			24,335	1.8
Automobiles	Hero Honda Motors	Motorcycle and scooter manufacturer – India	9,219	0.7
Healthcare and pharmaceuticals	CK Life Sciences	Biotechnology company – Hong Kong	3,266	0.2
Media and entertainment	Tom.Com	Media company – Hong Kong	2,584	0.2
Transport	Shanghai Forte Land	Residential property – China	3,237	
	Sinotrans	Logistics services provider – China	6,600	
	Zhejiang Expressway	Transport – China	7,228	
			17,065	1.3
Banks	Australia and New Zealand Banking	Banking – Australia	6,283	
	BOC Hong Kong	Financial services – Hong Kong	7,260	
			13,543	1.0
Real estate	Cheung Kong	Property developer – Hong Kong	5,260	
	Sun Hung Kai Property	*Property developer – Hong Kong*	3,981	
			9,241	0.7
Other financial	Singapore Exchange	Securities exchange owner/operator – Singapore	5,388	0.4
Information technology hardware	Legend	PC manufacturer – Hong Kong	4,143	0.3
Total Asia Pacific Equities			**124,289**	**9.2**
Other Emerging Markets				
Mining	Anglo American Platinum	Platinum mining – South Africa	5,880	
	Norilsk Nickel	Mining company – Russia	13,790	
			19,670	1.4
Oil and gas	Gazprom	Gas producer – Russia	8,638	
	Lukoil	Oil company – Russia	10,799	
	Petrobras	*Oil company – Brazil*	9,161	
	Yukos	Oil company – Russia	9,292	
			37,890	2.8
Healthcare and pharmaceuticals	Teva Pharmaceuticals	Generic drugs manufacturer – Israel	8,620	0.6
Telecommunication services	Tele Norte Leste	Telephone service operator – Brazil	4,802	0.4
Total Other Emerging Markets Equities			**70,982**	**5.2**
Value of equity stocks and OEICs			1,251,667	
Convertible loan stock having an element of equity			5,535	
Total Equity Investments			**1,257,202**	**92.7**

Classification	Name	Market value £'000	%
Fixed Interest			
Sterling denominated	AMP Group Finance 6.875% 2022	1,990	
	AMP Group Finance G/R 2019	1,964	
	Bank of Scotland FR (SAMS) 2072	23,952	
	Baxi Heating Finance 7.875% 2014	1,598	
	Bayerische Hypo-und Vereinsbank 8.675% 2005	228	
	British Gas 8.875% 2008	3,971	
	British Telecom 5.75% 2028	926	
	Cairngorm FRN 2016	2,978	
	Dignity Finance 8.151% 2030	2,725	
	EGG Banking 6.875% 2021	722	
	France Telecom 8% 2017	3,602	
	Gallaher 6.625% 2009	3,387	
	Hilton 7.25% 2008	1,105	
	Household Finance 6.125% 2010	1,081	
	Next 5.25% 2013	181	
	Pemex Project 7.5% 2013	2,098	
	Scottish Mutual Assurance 7.25% Perpetual	2,126	
	Standard Life Finance Plc 6.75% Perpetual	939	
	Unique Pub Finance 6.464% 2032	926	
	Westcoast Trains 6% 2015	1,560	
		58,059	4.3
Euro denominated	Avio 9.625% 2013	2,578	
	Duchess II E2 FRN 2015	1,337	
	Eco-Bat Finance 10.125% 2013	1,493	
	Eircom 8.25% 2013	2,256	
	Europa Two 14% 2027	1,672	
	Kronos 8.875% 2009	1,452	
	Messer Griesheim 10.375% 2011	3,195	
	MTU Aero Engines 8.25% 2014	1,233	
	North Westerly 10.993% 2016	2,674	
	Nymphenburg FRN 2025	988	
	Teksid Aluminium 11.375% 2011	1,173	
		20,051	1.5
US$ denominated	Smurfit Capital 6.75% 2005	2,309	
	Stagecoach 8.625% 2009	875	
		3,184	0.2
Total Fixed Interest		**81,294**	**6.0**
Total Investments		**1,338,496**	**98.7**
Net Liquid Assets		**16,845**	**1.3**
Total Assets at Market Value		**1,355,341**	**100.0**
(before deduction of debentures and short term borrowings)			

Capital

At 31 March	Total assets £'000	Debenture stocks, long and short term borrowings £'000	Equity shareholders' funds £'000	Equity shareholders' funds per share p	Net asset value per share* p	Share price p	Discount† %
1994	1,047,750	123,542	924,208	256.2	257.4	219.0	14.9
1995	1,072,822	195,505	877,317	243.2	244.4	217.0	11.2
1996	1,323,010	209,871	1,113,139	308.6	309.8	268.7	13.3
1997	1,472,300	256,229	1,216,071	337.1	338.4	290.5	14.2
1998	1,877,159	303,063	1,574,096	436.4	437.4	384.0	12.2
1999	1,868,328	222,427	1,645,901	456.3	457.3	375.5	17.9
2000	2,206,594	279,010	1,927,584	569.1	570.2	493.5	13.5
2001	1,660,182	195,893	1,464,289	445.4	447.5	377.0	15.8
2002	1,509,887	206,899	1,302,988	421.4	423.6	369.0	12.9
2003	1,051,545	207,225	844,320	283.3	285.5	234.5	17.9
2004	**1,355,341**	**227,560**	**1,128,781**	**379.3**	**381.5**	**305.0**	**20.1**

* Net asset value per ordinary share has been calculated after deducting prior charges at par value (see note 18, page 48).

† Discount is the difference between Scottish Mortgage's quoted share price and its underlying net asset value.

Revenue

Year to 31 March	Gross revenue £'000	Available for ordinary shareholders £'000	Earnings per ordinary share‡ p	Dividend per ordinary share net p	Expense ratio§ %
1994	35,751	14,847	4.12	4.10	0.34
1995	42,504	19,390	5.37	4.40	0.24
1996	48,114	21,394	5.93	4.65	0.29
1997	50,571	24,604	6.82	5.15	0.27
1998	52,184	21,685	6.01	5.35	0.37
1999	44,894	20,263	5.62	5.50	0.38
2000	44,100	27,807**	7.82**	5.65	0.50
2001	44,075	25,212	7.57	6.00	0.51
2002	36,377	24,213	7.56	6.25	0.47
2003	33,909	22,597	7.43	6.60	0.49
2004	**35,829**	**23,931**	**8.05**	**7.00**	**0.60**

Gearing Ratios

Year to 31 March	Actual gearing¶	Potential gearingll
1994	106	113
1995	105	122
1996	101	119
1997	104	121
1998	107	119
1999	107	114
2000	105	114
2001	104	113
2002	109	116
2003	113	125
2004	**111**	**120**

‡ *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 43).*

§ Ratio of total operating costs to average shareholders' funds.

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

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

** Restated for change in accounting policy to charge expenses 50:50 between revenue and capital.

Cumulative Performance (taking 1994 as 100)

At 31 March	*Net* asset value per share	*Net asset value* total return††	Benchmark	*Bechmark* total return‡‡	Share price	*Share price* total return††	*Earnings per* ordinary share	Dividend per *ordinary* share net	*Retail* price index
1994	100	100	100	100	100	100	100	100	100
1995	95	97	98	101	99	101	130	107	104
1996	120	125	120	128	123	128	144	113	106
1997	131	139	126	139	133	141	166	126	109
1998	170	182	164	185	175	189	146	130	113
1999	178	193	178	205	171	188	136	134	115
2000	222	243	207	241	225	250	190	138	118
2001	174	192	177	211	172	193	184	146	121
2002	165	184	168	204	168	192	183	152	122
2003	111	126	113	141	107	125	180	161	126
2004	**148**	**174**	**141**	**181**	**139**	**169**	**195**	**171**	**130**
Compound annual returns									
5 year	(3.6%)	(2.0%)	(4.6%)	(2.4%)	(4.1%)	(2.1%)	7.5%	5.0%	2.5%
10 year	4.0%	5.7%	3.5%	6.1%	3.4%	5.4%	6.9%	5.5%	2.7%

†† Source: AITC.

‡‡ Source: Thomson Financial Datastream.

Past performance is no guarantee of future performance.

Directors' Report

The Directors have pleasure in submitting their Annual Report together with the results of the Company for the year to 31 March 2004.

Status

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

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 March 2003, subject to any matters that may arise from any subsequent enquiry by the Inland Revenue into the Company's tax return. In the opinion of the Directors the Company has subsequently 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.

Review of Activities

During the year under review the Company has followed the normal activities of an investment trust company. A review of the main features of the year is contained in the Chairman's Statement and in the Managers' Portfolio Review on the preceding pages.

Dividends

The Board recommends a final dividend of 0.40p per ordinary share which, together with the interim of 2.20p and the second interim of 4.40p already paid, makes a total of 7.00p for the year compared with 6.60p for the previous year.

If approved, the recommended final dividend on the ordinary shares will be paid on 7 July 2004 to shareholders on the register at the close of business on 11 June 2004.

After payment of the dividend the accumulated revenue balance is increased by £3,152,000 to £54,041,000.

Corporate Governance

In July 2003 the Financial Reporting Council issued a revised Combined Code on Corporate Governance (the "revised Code") which is mandatory for accounting periods beginning on or after 1 November 2003, effective for the Company's year end 31 March 2005. In addition, the AITC issued a Code of Corporate Governance (the "AITC Code") in August 2003.

Following the publication of the revised Code and the AITC Code, the Board held a special meeting to review fully its corporate governance procedures. Procedures have been amended, where appropriate, to ensure that the Company should be compliant with the revised Code for its accounting period to 31 March 2005.

Compliance

The Board has considered the principles set out in the 1998 Combined Code (the "Code") and 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 with the provisions set out in Section 1 of the Code which are relevant to it.

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, treasury matters and dividend policy. The Board also reviews the financial statements, investment transactions, revenue budgets and performance.

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

	Board	Audit Committee
Number of meetings	**8**	**2**
Lord Sanderson of Bowden	3	1
Sir Donald MacKay	8	2
GA Ball	6	2
MM Gray	2	–
WG McQueen	7	2
The Earl of Portarlington	6	2
JPHS Scott	7	2
Lord Strathclyde	2	–

Lord Sanderson of Bowden attended all the meetings held up to the date of his retiral and Mr Gray and Lord Strathclyde attended all the meetings held since their appointment.

The Board currently comprises 7 Directors, all of whom are non-executive and are considered to be independent. Mr GA Ball offers himself for re-election this year, having served on the Board for more than 9 years. The Board takes the view that Mr Ball's independence has not been compromised by his length of service and that he is independent in character and judgement and there are no relationships or circumstances that are likely to affect his judgement. Mr GA Ball is the senior independent director.

During the course of the year the Board reviewed its composition having regard to the present and future needs of the Company and the need for a balanced Board. Sir Donald MacKay was appointed Chairman on 3 July 2003 following the retiral of Lord Sanderson of Bowden. Lord Strathclyde and Mr MM Gray, who are very experienced in the worlds of politics and industry respectively, were appointed to the Board on 26 February 2004. Lord Portarlington will retire from the Board at the conclusion of the Annual General Meeting on 1 July 2004.

The Directors all have appropriate business and financial experience to enable the Board to provide effective strategic leadership and proper governance of the Company. Information about the Directors can be found on pages 8 and 9.

The executive responsibilities for investment management have been delegated to the Company's Managers and Secretaries, Baillie Gifford & Co, and in the context of a Board comprised entirely of non-executive Directors, there is no chief executive officer.

A Nomination Committee was established in March 2004 consisting of the whole Board. The Chairman of the Committee is the Chairman of the Board. The terms of reference include reviewing the Board, identifying and nominating candidates for appointment to the Board, appraising the Chairman and the Board, succession planning and training. The Committee will consider the use of an external search consultant depending on circumstances at the appropriate time.

Under the provisions of the Company's Articles, a Director appointed during the year is required 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 and submit themselves for re-election. The Board has resolved further that no Director shall serve for a period of greater than 3 consecutive years without submitting himself for re-election and that any Director who has served on the Board for more than 9 years will submit himself for re-election annually.

New Directors appointed to the Board have a formal induction meeting with the Managers. Directors will receive other relevant training as necessary.

There is an agreed procedure for Directors to seek independent professional advice if necessary at the Company's expense.

Remuneration

Since all the Directors are non-executive, a remuneration committee is considered unnecessary. The Company's policy on remuneration is set out in the Directors' Remuneration Report on pages 31 and 32.

Internal Controls and Risk Management

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 the Managers and Secretaries, Baillie Gifford & Co, under the terms of the Management Agreement. The Board acknowledges its responsibilities to supervise and control the discharge by the Managers and Secretaries of their obligations.

Baillie Gifford & Co is 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 those of Baillie Gifford & Co and its other clients through the appointment of independent custodian banks.

Baillie Gifford & Co has an established compliance function in accordance with the Financial Services Authority regulations. The compliance function provides the Board with a report on monitoring procedures at least annually. 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 internal audit and compliance provide the Board with regular reports on their monitoring programmes.

The Directors acknowledge their overall 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 has undertaken a full review of all aspects of the published guidance "Internal Control: Guidance for Directors on the Combined Code" (the Turnbull guidance) and has established an ongoing process for identifying, evaluating and managing the significant risks faced by the Company, in accordance with the Turnbull recommendations. To ensure that risk management and internal controls are considered on a regular basis and that a full risk and control assessment is undertaken on an annual basis, the following processes have been established in compliance with the guidance:

- internal controls strategy has been formalised following the production of a detailed risk map whereby significant risks are identified and the key controls to manage these risks are confirmed as in place and operating effectively;

- reporting procedures for the internal audit department, in respect of its risk framework monitoring and audit programme, and the compliance department, in respect of its regulatory monitoring programme, are defined and formalised within a service level agreement; and

- regular reports on internal controls are prepared by the Managers and submitted for Board review.

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.

Accountability and Audit

The respective responsibilities of the Directors and the auditors in connection with the Financial Statements are set out on pages 33 to 35.

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

An audit committee has been established in compliance with the Combined Code consisting of the whole Board. Its authority and duties are clearly defined within its written terms of reference. Mr WG McQueen replaced the Chairman of the Board as Chairman of the Audit Committee on 18 March 2004.

The Committee meets at least twice a year to review the Company's interim and annual financial statements. The Committee keeps under review the scope and effectiveness of the external audit and considers on a regular basis the independence and objectivity of the external auditors. It meets at least annually with the external auditors and recommends to the Board the level of fees for audit and non-audit services. It also reviews regularly

Directors' interests

Name	Nature of interest	Ordinary 25p shares held at 31 March 2004	31 March 2003 or date of appointment
Sir Donald MacKay	Beneficial	2,469	2,469
GA Ball	Beneficial	10,000	10,000
MM Gray	Beneficial	272,900	271,900
	Non-beneficial	12,500	12,500
WG McQueen	Beneficial	1,500	1,500
	Non-beneficial	3,000	3,000
The Earl of Portarlington	Beneficial	936,000	936,000
JPHS Scott	Beneficial	15,464	2,129
Lord Strathclyde	Beneficial	3,142	-

The Directors at the year end, and their interests in the Company, were as shown above.

the terms of the Investment Management Agreement.

Investment Manager

An Investment Management Agreement between the Company and Baillie Gifford & Co sets out the matters over which the Managers have authority in accordance with the policies and directions of, and subject to restrictions imposed by, the Board. The Management Agreement is terminable on not less than 12 months' notice. Details of the fee arrangements with Baillie Gifford & Co are shown on page 41. It is the opinion of the Directors that the continuing appointment of Baillie Gifford & Co on the terms agreed is in the interest of shareholders as a whole as the Managers' experienced and well resourced investment team has managed the Company's assets in accordance with its stated policy and objective. Additionally, the secretarial and administrative functions have been well conducted.

Relations with Shareholders

The Company's Managers meet regularly with shareholders and their representatives and report to the Board. The Chairman is available to meet shareholders as appropriate. Shareholders wishing to communicate with the Chairman, the senior independent director or any other member of the Board may do so by writing to the Company, for the attention of the secretaries at the address on the back cover. The Company's Annual General Meeting provides a forum for all communication with shareholders and the Board announces the level of proxies lodged. The notice period for the Annual General Meeting is at least 20 working days.

The Company has given discretionary voting powers to the investment managers, Baillie Gifford & Co. The Managers vote against resolutions they consider may damage shareholders' rights or economic interests. Baillie Gifford & Co give due weight to what they consider to be socially responsible investment when making investment decisions, but their overriding objective is to produce good investment returns for shareholders.

Directors

Mr MM Gray and Lord Strathclyde were appointed to the Board on 26 February 2004. Their appointments fall to be confirmed at the Annual General Meeting.

Mr WG McQueen retires by rotation and, being eligible, is recommended by the Board for re-election.

Mr GA Ball, having served for more than 9 years, offers himself and is recommended by the Board for re-election.

The Earl of Portarlington will retire from the Board at the conclusion of the Annual General Meeting.

Lord Sanderson of Bowden retired from the Board on 3 July 2003.

There have been no changes intimated in the Directors' interests up to 7 May 2004.

Directors' and officers' liability insurance cover is held by the Company in respect of the Directors.

Repurchase of Shares

At the Annual General Meeting held on 3 July 2003 the Company renewed its authority to purchase shares in the market, in respect of up to 44,566,036 ordinary shares (equivalent to 14.99% of its then issued share capital), such authority to expire at the conclusion of the Annual General Meeting of the Company to be held in respect of the year ending 2004 or 2 January 2005, whichever is earlier, unless previously varied, revoked or renewed.

During the year to 31 March 2004 the Company bought back 700,000 ordinary shares (nominal value £175,000), on the London Stock Exchange for cancellation. The total consideration for these shares was £1,779,000. Between 1 April 2004 and the date of this report no further shares have been bought back.

The principal reasons for such share buy-backs are:

(i) to enhance net asset value for continuing shareholders by purchasing shares at a discount to the prevailing net asset value;

(ii) to address any imbalance between the supply of and the demand for Scottish Mortgage's shares that results in a discount of the quoted market price to the published net asset value per share.

The shares in question were purchased at a price (after allowing for costs) below the net asset value and subsequently cancelled, thereby reducing the issued share capital (see note 15 on page 47). As a result of such purchases the net asset value of the Company has increased by approximately 0.05%.

The Directors are seeking shareholders' approval at the Annual General Meeting to renew the authority to purchase up to 14.99% of the Company's ordinary shares in

Substantial Holdings

Name	No. of ordinary 25p shares held	% of issue
DC Thomson & Co Ltd	15,000,000	5.0
Prudential plc	10,938,100	3.7
Legal & General Investment Management	9,092,501	3.1

The above information has been intimated to the Company as at 7 May 2004 in compliance with section 198 of the Companies Act 1985.

issue at the date of the passing of the resolution, such authority to expire at the Annual General Meeting of the Company to be held in respect of the year ending 2005 or 31 December 2005, whichever is earlier. Under the Listing Rules of the UK Listing Authority of the Financial Services Authority, the maximum price that may be paid on the exercise of the authority must not exceed 105% of the average of the middle market quotations for the shares over the 5 business days immediately preceding the date of purchase. The minimum price that may be paid will be 25p per share. Purchases of shares will be made within guidelines established, from time to time, by the Board. Your attention is drawn to Special Resolution No. 10, in the Notice of Annual General Meeting.

Creditor Payment Policy

It is the Company's payment policy for the forthcoming financial year to obtain the best terms for all business. In general, the Company agrees with its suppliers the terms on which business will take place and it is its policy to abide by these terms.
The Company had no trade creditors at 31 March 2004.

Auditors

The auditors, KPMG Audit Plc, are willing to continue in office and in accordance with section 385 and section 390A of the Companies Act 1985 resolutions concerning their reappointment and remuneration will be submitted to the Annual General Meeting.

By order of the Board

BAILLIE GIFFORD & Co
Managers and Secretaries
10 May 2004

Baillie Gifford & Co.

Directors' emoluments for the year (audited)

	2004 £	2003 £
Directors who served during the year:		
Lord Sanderson of Bowden (Chairman) (retired 3 July 2003)	6,181	22,000
Sir Donald MacKay (assumed the Chair 3 July 2003)	21,973	16,000
GA Ball	16,000	16,000
MM Gray (appointed 26 February 2004)	1,534	–
WG McQueen	16,000	16,000
The Earl of Portarlington	16,000	16,000
JPHS Scott	16,000	16,000
Lord Strathclyde (appointed 26 February 2004)	1,534	–
	95,222	102,000
Past Directors:		
FPM Johnston (retired 4 July 2002)	–	4,164
	95,222	**106,164**

The Directors who served in the year received the above emoluments in the form of fees.

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 34 and 35.

Remuneration Committee

The Company has 7 Directors, all of whom are non-executive. There is no separate remuneration committee and the Board as a whole considers changes to Directors' fees from time to time. Baillie Gifford & Co, who have been appointed by the Board as Managers and Secretaries, provide advice and comparative information 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 should take account of the level of fees paid by comparable investment trusts. This policy will continue for the year ended 31 March 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. These state that the fees paid to the Chairman shall not exceed £30,000 per annum and those paid to a Director shall not exceed £20,000 per annum. Non-executive Directors are not eligible for any other remuneration apart from the reimbursement of allowable expenses.

The Board carried out a review of the level of Directors' fees during the year, and concluded that the fees should be increased from £22,000 to £24,000 for the Chairman but there should be no change to the Directors fee, currently £16,000 per annum. The increase was effective from 1 April 2003.

Sums paid to third parties (audited)

The Directors' fees payable to Lord Sanderson of Bowden were paid to Russell Consultants. The payment was for making his services available as a Director of the Company.

Directors' service details

	Date of appointment	Due date for election/re-election
Sir Donald MacKay	1 July 1999	AGM 2005
GA Ball	17 February 1983	AGM July 2004
MM Gray	26 February 2004	AGM July 2004
WG McQueen	15 February 2001	AGM July 2004
The Earl of Portarlington	23 April 1997	retires AGM July 2004
JPHS Scott	31 October 2001	AGM 2005
Lord Strathclyde	26 February 2004	AGM July 2004

Directors' service contracts

It is the Board's policy that none of the Directors has a service contract. 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. Thereafter they are obliged to retire by rotation, and, if they wish, to offer themselves for re-election, no longer than every 3 years after that. Any Director who has served on the Board for more than 9 years will submit himself for re-election annually. There is no notice period and no provision for compensation upon early termination of appointment.

Company performance

The graph opposite compares 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 a widely used measure of performance for UK listed companies. (Benchmark provided for information purposes only.)

Performance Graph

Scottish Mortgage's Share Price, FTSE All-Share Index and Benchmark*
(figures have been rebased to 100 at 31 March 1999)

Past performance is no guarantee of future *performance.*

Approval

The Directors' Remuneration Report on pages 31 and 32 was approved by the Board of Directors and signed on its behalf on 10 May 2004.

SIR DONALD MACKAY
Chairman

Statement of Directors' Responsibilities in Respect of 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 and of the profit or loss for that period. In preparing those financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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

Independent Auditors' Report

to the members of Scottish Mortgage Investment Trust PLC ('the Company')

We have audited the financial statements on pages 36 to 49. 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 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 and the Directors' Remuneration Report. As described on page 33, this includes responsibility for preparing the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, the Listing Rules of the Financial Services Authority, and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and 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 regarding Directors' remuneration and transactions with the Company is not disclosed.

We review whether the statement on pages 26 to 29 reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the Board's statements on internal 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 the other information contained in the Annual Report, including the corporate governance statement and the unaudited part of the Directors' Remuneration Report, and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements 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.

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 March 2004 and of its total return 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.

KPMG Audit Plc
Chartered Accountants
Registered Auditor
Edinburgh
10 May 2004

KPMG Audit Plc

		for the year ended 31 March 2004			for the year ended 31 March 2003		
	Notes	Revenue £'000	Capital £'000	**Total £'000**	Revenue £'000	Capital £'000	**Total £'000**
Gains/(losses) on investments	9	–	285,687	**285,687**	–	(421,063)	**(421,063)**
Currency gains/(losses)	16	–	5,980	**5,980**	–	(701)	**(701)**
Income	2	35,829	–	**35,829**	33,909	–	**33,909**
Investment management fee	3	(2,276)	(2,276)	**(4,552)**	(2,053)	(2,053)	**(4,106)**
Other administrative expenses	4	(1,404)	–	**(1,404)**	(1,185)	–	**(1,185)**
Net return before finance costs and taxation		32,149	289,391	**321,540**	30,671	(423,817)	**(393,146)**
Finance costs of borrowings	5	(7,290)	(7,303)	**(14,593)**	(7,119)	(7,119)	**(14,238)**
Return on ordinary activities before taxation		24,859	282,088	**306,947**	23,552	(430,936)	**(407,384)**
Tax on ordinary activities	6	(928)	–	**(928)**	(955)	–	**(955)**
Return on ordinary activities after taxation for the financial year attributable to equity shareholders		23,931	282,088	**306,019**	22,597	(430,936)	**(408,339)**
Dividends in respect of equity shares	7	(20,779)	–	**(20,779)**	(19,730)	–	**(19,730)**
Transfer to/(from) reserves		**3,152**	**282,088**	**285,240**	**2,867**	**(430,936)**	**(428,069)**
Return per ordinary share	8	**8.05p**	**94.86p**	**102.91p**	**7.43p**	**(141.69p)**	**(134.26p)**

* The revenue column of this statement is the profit and loss account of the Company.

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

The accompanying notes on pages 39 to 49 are an integral part of this statement.

	Notes	at 31 March 2004 £'000	at 31 March 2004 £'000	at 31 March 2003 £'000	at 31 March 2003 £'000
Fixed assets					
Investments	9		1,338,496		1,050,748
Current assets					
Debtors	11	16,404		22,360	
Cash at bank and in hand	10	20,394		3,915	
		36,798		26,275	
Creditors					
Amounts falling due within one year	12	(95,302)		(48,953)	
Net current liabilities			(58,504)		(22,678)
Total assets less current liabilities			1,279,992		1,028,070
Creditors					
Amounts falling due after more than one year	13		(152,211)		(183,750)
			1,127,781		**844,320**
Capital and reserves					
Called-up share capital	15		74,326		74,501
Capital redemption reserve	16		15,854		15,679
Capital reserve – realised	16		777,982		798,814
Capital reserve – unrealised	16		205,578		(95,563)
Revenue reserve	16		54,041		50,889
Equity shareholders' funds	17		**1,127,781**		**844,320**
Net asset value per ordinary share	18		**381.5p**		**285.5p**

The Accounts were approved by the Board and signed on their behalf on 10 May 2004.

SIR DONALD MACKAY
Chairman

The accompanying notes on pages 39 to 49 are an integral part of this statement.

Sir Donald Mackay

	Notes	for the year ended 31 March 2004 £'000	£'000	for the year ended 31 March 2003 £'000	£'000
Net cash inflow from operating activities	20		31,040		27,837
Servicing of finance					
Interest paid		(14,431)		(14,287)	
Net cash outflow from servicing of finance			(14,431)		(14,287)
Taxation					
Income tax refunded/(paid)		52		(48)	
Overseas tax suffered		(947)		(961)	
Total tax paid			(895)		(1,009)
Financial investment					
Acquisitions of investments		(378,635)		(347,442)	
Disposals of investments		376,127		371,734	
Realised currency loss		(111)		(323)	
Net cash (outflow)/inflow from financial investment			(2,619)		23,969
Equity dividends paid			(19,919)		(19,460)
Net cash (outflow)/inflow before financing			(6,824)		17,050
Financing					
Shares purchased for cancellation		(3,184)		(31,414)	
Loans repaid		(46,844)		–	
Loans drawn down		73,331		–	
Net cash inflow/(outflow) from financing			23,303		(31,414)
Increase/(decrease) in cash	21		**16,479**		**(14,364)**
Reconciliation of net cash flow to movement in net debt	21				
Increase/(decrease) in cash in the period			16,479		(14,364)
Increase in bank loans			(26,487)		-
Exchange movement			6,091		(378)
Other non-cash changes			61		52
Movement in net debt in the year			(3,856)		(14,690)
Net debt at 1 April			(203,310)		(188,620)
Net debt at 31 March			**(207,166)**		**(203,310)**

The accompanying notes on pages 39 to 49 are an integral part of this statement.

Notes to Accounts

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1 Principal Accounting Policies

A summary of the principal accounting policies is set out in paragraphs (a) to (h) below. All have been applied consistently throughout the current and preceding year.

(a) Basis of Accounting

The accounts are prepared under the historical cost convention, modified to include the revaluation of fixed asset investments, and on the assumption that approval as an investment trust will continue to be granted.

The accounts have been prepared in accordance with applicable UK accounting standards and with the revised Statement of Recommended Practice 'Financial Statements of Investment Trust Companies' issued in January 2003.

(b) Investments

Listed investments are shown at middle market value, or in the case of FTSE 100 constituents, at last traded prices issued by the London Stock Exchange.

Listed investments include Open Ended Investment Companies ('OEICs') authorised in the UK; these are valued at mid price and are classified for valuation purposes according to the principal geographical area of the underlying holdings.

Unlisted investments are shown at a valuation determined by the Directors based upon latest dealing prices, stockbroker valuations, net asset values and other information, as appropriate.

(c) Income

(i) Income from equity investments is brought into account on the date on which the investments are quoted ex-dividend or, where no ex-dividend date is quoted, when the Company's right to receive payment is established.

(ii) Interest from fixed interest securities is recognised on an accruals basis. Fixed interest securities issued at a significant discount or premium are accounted for on an effective yield basis.

(iii) Franked income is stated net of tax credits.

(iv) Unfranked investment income includes the taxes deducted at source.

(v) Interest receivable on deposits is recognised on an accruals basis.

(vi) If scrip is taken in lieu of dividends in cash, the net amount of the cash dividend declared is credited to the revenue account.

(d) Expenses

All expenses are accounted for on an accruals basis. Expenses are charged through the revenue account except as follows: where they relate directly to the acquisition or disposal of an investment, in which case they are added to the cost of the investment or deducted from the sale proceeds and where they are connected with the maintenance or enhancement of the value of investments, in which case they are charged 50:50 to the revenue account and realised capital reserve.

(e) Long Term Borrowings and Finance Costs

Long term borrowings are carried in the balance sheet at the cumulative amount of net proceeds after issue, plus accrued finance costs. The finance costs of such borrowings are allocated 50:50 to the revenue account and realised capital reserve at a constant rate on the carrying amount. Issue costs are written off at a constant rate over the life of the borrowings. Gains and losses on the repurchase or early settlement of debt is wholly charged to capital.

(f) Taxation

Deferred taxation is provided on all timing differences, calculated at the current tax rate relevant to the benefit or liability. Deferred tax assets are recognised only to the extent that it will be more likely than not that there will be taxable profits from which underlying timing differences can be deducted.

(g) Foreign Currencies

Transactions involving foreign currencies are converted at the rate ruling at the time of the transaction. Assets and liabilities in foreign currencies are translated at the closing rates of exchange at the balance sheet date. Any gain or loss arising from a change in exchange rate subsequent to the date of the transaction is included as an exchange gain or loss in capital reserve or revenue reserve as appropriate.

(h) Capital Reserves

(i) Capital Reserves Realised:
Gains and losses on realisation of investments and realised exchange differences of a capital nature are dealt with in this reserve. Purchases of the Company's own shares for cancellation are also funded from this reserve. 50% of management fees, including related VAT, and finance costs are allocated to the realised capital reserve in accordance with the Company's objective of combining capital and income growth.

(ii) Capital Reserves Unrealised:
Unrealised appreciation represents the amount by which assets and liabilities valued at market value differs from their book value and is dealt with in this reserve.

2 Income

	2004 £'000	2003 £'000
Income from investments		
Franked investment income	17,766	19,072
UK unfranked investment income†	4,921	3,411
Overseas dividends	10,635	7,825
Overseas interest	1,929	2,341
	35,251	**32,649**
Other income		
Deposit interest	448	1,078
Underwriting commission	130	182
	578	**1,260**
Total income	**35,829**	**33,909**
Total income comprises		
Dividends	29,493	27,778
Interest from investments	5,758	4,871
Other	578	1,260
	35,829	**33,909**
Income from investments		
Listed UK	21,496	23,136
Listed overseas	13,755	9,513
	35,251	**32,649**

† Includes income from OEICs.

3 Investment Management Fee

	Revenue £'000	2004 Capital £'000	**Total £'000**	Revenue £'000	2003 Capital £'000	**Total £'000**
Investment management fee	2,042	2,042	**4,084**	1,834	1,834	**3,668**
Irrecoverable VAT thereon	234	234	**468**	219	219	**438**
	2,276	**2,276**	**4,552**	**2,053**	**2,053**	**4,106**

Baillie Gifford & Co is employed by the Company as Managers and Secretaries under a management agreement which is terminable on not less than 12 months' notice, or on shorter notice in certain circumstances. The fee in respect of each quarter is 0.08% of total assets less current liabilities (excluding short term borrowings for investment purposes) and is subject to VAT at the appropriate rate. The *management fee is levied on all assets, including holdings in collective investment schemes (OEICs) managed by Baillie Gifford & Co;* however the OEICs' share class held by the Company does not attract a management fee.

4 Other Administrative Expenses – all charged to revenue

	2004 £'000	2003 £'000
General administrative expenses	1,294	1,065
Directors' fees (see Directors' Remuneration Report page 31)	95	106
Auditors' remuneration for audit services	15	14
	1,404	**1,185**

5 Finance Costs of Borrowings

	2004 Revenue £'000	2004 Capital £'000	2004 Total £'000	2003 Revenue £'000	2003 Capital £'000	2003 Total £'000
Bank loans and overdrafts repayable within five years	327	340	**667**	151	151	**302**
Debentures repayable wholly or partly in more than five years	6,963	6,963	**13,926**	6,968	6,968	**13,936**
	7,290	**7,303**	**14,593**	**7,119**	**7,119**	**14,238**

6 Tax on Ordinary Activities

	2004 Revenue £'000	2004 Capital £'000	2004 Total £'000	2003 Revenue £'000	2003 Capital £'000	2003 Total £'000
Overseas taxation	928	–	**928**	955	–	**955**

	2004 £'000	2003 £'000
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	24,859	23,552
Revenue return on ordinary activities multiplied by the standard rate of corporation tax in the UK of 30% (2003 – 30%)	7,458	7,066
Income not taxable (franked investment income)	(5,330)	(5,722)
Overseas withholding tax claimed as a deduction	(278)	(287)
Overseas withholding tax written off	928	955
Capitalised expenses	(2,874)	(2,752)
Excess expenses in period not provided for as an asset	1,024	1,695
Current tax charge for the year	**928**	**955**

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 March 2004 or 31 March 2003 as the Company has unrelieved management expenses which are available to be carried forward. The tax charge for 31 March 2004 and 2003 comprises overseas withholding taxes written off.

At 31 March 2004 the Company had surplus management expenses of £38 million (2003 – £33 million of which £7 million was of a revenue nature) 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 Dividends

	2004	2003	2004 £'000	2003 £'000
Interim dividend per ordinary share (paid 28 November 2003)	2.20p	2.10p	6,540	6,369
Second interim dividend per ordinary share (paid 1 April 2004)	4.40p	–	13,081	–
Proposed final dividend per ordinary share (payable 7 July 2004)	0.40p	4.50p	1,189	13,410
Adjustment to provision for 2003/2002 final dividend	–	–	(31)	(49)
	7.00p	**6.60p**	**20,779**	**19,730**

8 Return per Ordinary Share

	2004 Revenue	2004 Capital	2004 Total	2003 Revenue	2003 Capital	2003 Total
	8.05p	**94.86p**	**102.91p**	**7.43p**	**(141.69p)**	**(134.26p)**

Revenue return per ordinary share is based on the net revenue on ordinary activities after taxation of £23,931,000 (2003 – £22,597,000), and on 297,361,946 (2003 – 304,134,148) ordinary shares, 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 £282,088,000 (2003 – net capital loss of £430,936,000), and on 297,361,946 (2003 – 304,134,148) ordinary shares, being the weighted average number of ordinary shares in issue during the year.

9 Fixed Assets – Investments

	2004 £'000	2003 £'000
Listed at market value – UK	610,211	532,041
– overseas	721,419	513,790
Unlisted	6,866	4,917
	1,338,496	**1,050,748**

	Listed in UK £'000	Listed overseas £'000	Unlisted £'000	**Total £'000**
Cost of investments held at 1 April 2003	*548,243*	*596,638*	*5,967*	***1,150,848***
Unrealised depreciation at 1 April 2003	(16,202)	(82,848)	(1,050)	**(100,100)**
Value of investments held at 1 April 2003	532,041	513,790	4,917	**1,050,748**
Movements in year:				
Purchases at cost	108,761	264,428	–	**373,189**
Sales – proceeds	(164,335)	(206,793)	–	**(371,128)**
– realised profits/(losses) on sales	3,778	(15,177)	–	**(11,399)**
Increase in unrealised appreciation	129,966	165,171	1,949	**297,086**
Value of investments held at 31 March 2004	**610,211**	**721,419**	**6,866**	**1,338,496**
Cost of investments held at 31 March 2004	496,447	639,096	5,967	**1,141,510**
Unrealised appreciation at 31 March 2004	113,764	82,323	899	**196,986**
Value of investments held at 31 March 2004	**610,211**	**721,419**	**6,866**	**1,338,496**

	2004 £'000	2003 £'000
Gains/(losses) on investments		
Realised losses on sales	(11,399)	(89,334)
Book cost of investments written off	–	(11,368)
Increase/(decrease) in unrealised appreciation	297,086	(320,361)
	285,687	**(421,063)**

9 Fixed Assets – Investments (continued)

During the year the Company had holdings in Open Ended Investment Companies ('OEICs') managed by Baillie Gifford & Co, the Company's investment manager. The share class held in these OEICs does not attract a management fee. At 31 March the Company held:

	2004		2003	
	C income shares held	% of share class held	C income shares held	% of share class held
Baillie Gifford European Smaller Companies Fund	7,910,800	95.9	7,910,800	94.9
Baillie Gifford Latin American Fund	–	–	15,000,000	80.0

10 Financial Assets

A full list of the Company's investments is given on pages 20 to 24. In addition a geographical analysis of the portfolio, an analysis of the investment portfolio by broad industrial or commercial sector, and a list of the 30 largest equity investments by their aggregate market value are contained in the Managers' Review Section.

Exposure to currency risk through asset allocation is indicated below.

	2004 £'000	2003 £'000
Portfolio (currency of listing):		
Sterling	639,210	556,951
US dollar	368,219	288,945
Euro	99,372	87,212
Swedish kroner	24,769	9,241
Swiss franc	4,813	11,322
Japanese yen	77,276	47,508
Hong Kong dollar	62,148	14,131
Korean won	19,003	10,788
Australian dollar	21,561	12,271
Singapore dollar	5,388	3,135
Indian rupee	10,857	9,244
South African rand	5,880	–
	1,338,496	**1,050,748**
Cash:		
UK deposits	16,609	3,907
Foreign deposits – Euro	2,801	–
– US dollar	984	–
– Japanese yen	–	8
	20,394	**3,915**

The cash deposits generally comprise call or short term money market deposits of less than one month.

Short term debtors and creditors have been excluded from the disclosure of financial instruments.

Included within the analysis provided on pages 20 to 24 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 March is provided below.

	2004		2003	
	Market value £'000	Weighted average period until maturity	Market value £'000	Weighted average period until maturity
Warrants:				
Euro	–	–	*1,151*	*12 months*

10 Financial Assets (continued)

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

	2004			2003		
	Market value £'000	Weighted average interest rate	Weighted average period until maturity	Market value £'000	Weighted average interest rate	Weighted average period until maturity
Fixed rate:						
UK bonds	28,064	7.4%	12 years	38,009	7.6%	12 years
UK bonds (perpetual)	3,065	7.1%	N/A	1,615	7.3%	N/A
UK convertible loan stock	*5,535*	*7.3%*	*6 months*	*4,726*	*7.3%*	*2 years*
European bonds	17,726	10.2%	10 years	19,714	8.3%	7 years
US bonds	3,184	7.2%	3 years	3,353	7.3%	4 years
Floating rate:						
UK bonds (interest rate linked to sterling LIBOR)	26,930	2.7%	61 years	26,173	3.0%	62 years
European bonds (interest rate linked to euro LIBOR)	2,325	7.6%	15 years	2,734	8.3%	22 years

11 Debtors

	2004 £'000	2003 £'000
Due within one year:		
Income accrued	9,101	9,911
Sales for subsequent settlement	6,044	11,043
Taxation recoverable	77	130
Other debtors and prepayments	1,182	1,276
	16,404	**22,360**

12 Creditors – Amounts falling due within one year

	2004 £'000	2003 £'000
ING Bank N.V. US$ loan	*21,764*	–
ING Bank N.V. yen loan	–	23,475
National Australia Bank Limited multi-currency loan	30,858	–
The Royal Bank of Scotland Plc multi-currency loan	22,727	–
Purchases for subsequent settlement	2,158	7,604
Second interim dividend	13,081	–
Proposed final dividend	1,189	13,410
Other creditors and accruals	3,525	4,464
	95,302	**48,953**

Included in other creditors is £335,000 (2003 – £91,000) in respect of the investment management fee.

Borrowing facilities

A US$40 million loan facility has been arranged with ING Bank N.V.
A £35 million multi-currency loan facility has been arranged with National Australia Bank Limited.
A £100 million short term multi-currency loan facility has been arranged with The Royal Bank of Scotland Plc, expiring within 12 months.

At 31 March 2004 drawings were as follows:

ING Bank N.V.	US$40 million at an interest rate of 1.78% per annum.
National Australia Bank Limited	¥5,900 million at an interest rate of 0.65% per annum.
The Royal Bank of Scotland Plc	*US$41.8 million at an interest rate of 1.64% per annum.*

13 Creditors – Amounts falling due after more than one year

	Nominal rate	Effective rate	2004 £'000	2003 £'000
Debenture stocks:				
£20 million 8–14% stepped interest debenture stock 2020	14.0%	12.3%	22,374	22,419
£75 million 6.875% debenture stock 2023	6.875%	6.9%	74,303	74,265
£50 million 6–12% stepped interest debenture stock 2026	12.0%	10.8%	54,859	54,913
4½% irredeemable debenture stock			675	675
National Australia Bank Limited multi-currency loan (see note 12)			–	31,478
			152,211	**183,750**

Debenture stocks

The debenture stocks are stated in accordance with the requirements of Financial Reporting Standard 4 'Capital Investments' ('FRS4'); the cumulative effect is to increase the carrying amount of borrowings by £6.5 million (2003 – £6.6 million).

The debenture stocks are secured by a floating charge over the assets of the Company.

14 Financial Liabilities

	2004 £'000	2003 £'000
The interest rate risk profile of the Company's financial liabilities at 31 March was:		
Floating rate – yen denominated	30,858	54,953
Floating rate – US$ denominated	44,491	–
Fixed rate – sterling denominated	152,211	152,272
	227,560	**207,225**
The maturity profile of the Company's financial liabilities at 31 March was:		
In one year or less, or on demand	75,349	23,475
In more than one year, but less than five years	–	31,478
In more than five years (weighted average period fixed 20 years)	151,536	151,597
No fixed date for repayment	675	675
	227,560	**207,225**

Fair value of financial liabilities

The debenture stock issues are included in the accounts in accordance with FRS4. A comparison with the closing mid market value is as follows:

	2004 Nominal £'000	2004 Book £'000	2004 Market £'000	2003 Nominal £'000	2003 Book £'000	2003 Market £'000
8–14% stepped interest debenture stock 2020	20,000	22,374	35,568	20,000	22,419	35,576
6.875% debenture stock 2023	75,000	74,303	81,053	75,000	74,265	79,485
6–12% stepped interest debenture stock 2026	50,000	54,859	84,085	50,000	54,913	82,300
4½% irredeemable debenture stock	675	675	564	675	675	575
	145,675	**152,211**	**201,270**	**145,675**	**152,272**	**197,936**

All short term borrowings are stated at market value.

Deducting prior charges at market value would have the effect of reducing net asset value per share from 381.5p to 362.8p. Taking the market price of the ordinary shares at 31 March 2004 of 305.0p, this would have given a discount to net asset value of 15.9% as against 20.1% on a traditional basis. At 31 March 2003 the effect would have been to reduce net asset value from 285.5p to 268.0p. Taking the market price of the ordinary shares at 31 March 2003 of 234.5p, this would have given a discount to net asset value of 12.5% as against 17.9% on a traditional basis.

Short term debtors and creditors other than short term loans have been excluded from the disclosure of financial instruments.

Gains and losses on hedges

At 31 March 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 revenue account unless they are of a revenue nature.

15 Called-up Share Capital

	2004 Number	2004 £'000	2003 Number	2003 £'000
Authorised ordinary shares of 25p each	**360,720,000**	**90,180**	**360,720,000**	**90,180**
Allotted, called-up and fully paid ordinary shares of 25p each	**297,305,115**	**74,326**	**298,005,115**	**74,501**

At the Annual General Meeting on 3 July 2003 the Company renewed its authority to purchase shares in the market, in respect of 44,566,036 ordinary shares (equivalent to 14.99% of its issued share capital at that date). In the year to 31 March 2004 a total of 700,000 (2003 – 11,179,573) ordinary shares with a nominal value of £175,000 were bought back at a total cost of £1,779,000 (2003 – £30,599,000). At 31 March 2004 the Company had authority to buy back a further 44,566,036 ordinary shares.

Under the provisions of the Company's Articles the share buy-backs were funded from the realised capital reserve.

16 Reserves

	Capital redemption reserve £'000	Capital reserve – realised £'000	Capital reserve – unrealised £'000	Revenue reserve £'000
At 1 April 2003	15,679	798,814	(95,563)	50,889
Net loss on realisation of investments	–	(11,399)	–	–
Increase in unrealised appreciation	–	–	297,086	–
Exchange differences	–	(111)	–	–
Exchange differences on multi-currency loans	–	2,036	4,055	–
Shares purchased for cancellation	175	(1,779)	–	–
Investment management fee	–	(2,276)	–	–
Finance costs of borrowings	–	(7,303)	–	–
Retained net revenue for the year	–	–	–	3,152
At 31 March 2004	**15,854**	**777,982**	**205,578**	**54,041**

17 Total Shareholders' Funds

	2004 £'000	2003 £'000
Total shareholders' funds are attributable as follows:		
Equity shares	**1,127,781**	**844,320**

Total shareholders' funds have been calculated in accordance with the provisions of FRS4. However, the net asset value per share figures in note 18 have been calculated on the basis of shareholders' rights to reserves as specified in the Articles of Association of the Company. A reconciliation of the two figures is as follows:

Shareholders' funds attributable to ordinary shares (as above)	£1,127,781,000
Number of ordinary shares in issue at the year end	297,305,115
Shareholders' funds per ordinary share	379.3p
Additions/(deductions)	
– expenses of debenture issue	(0.8p)
– allocation of interest on borrowings	3.0p
Net asset value per ordinary share	**381.5p**

18 Net Asset Value per Ordinary Share

The net asset value per ordinary share and the net asset value 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	**381.5p**	**285.5p**	**1,134,321**	**850,921**

	2004 £'000	2003 £'000
The movements during the year of the assets attributable to the ordinary shares were as follows:		
Total net assets at 1 April	850,921	1,309,641
Total recognised gains and (losses) for the year	306,019	(408,339)
Dividends appropriated in the year	(20,779)	(19,730)
Adjustment to debentures	(61)	(52)
Shares purchased for cancellation	(1,779)	(30,599)
Total net assets at 31 March	**1,134,321**	**850,921**

Net asset value per ordinary share is based on net assets (adjusted to reflect the deduction of the debentures at par) and on 297,305,115 (2003 – 298,005,115) ordinary shares, being the number of ordinary shares in issue at the year end. Shareholders' funds as reported on the face of the balance sheet has been computed in accordance with the provisions of FRS4. A reconciliation of the two sets of figures under these two conventions is given in note 17.

19 Reconciliation of Movements in Shareholders' Funds

	2004 £'000	2003 £'000
Shareholders' funds at 1 April	844,320	1,302,988
Total recognised gains and (losses) for the year (after dividend payments)	285,240	(428,069)
Shares purchased for cancellation	(1,779)	(30,599)
Shareholders' funds at 31 March	**1,127,781**	**844,320**

20 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	32,149	30,671
Investment management fees charged to capital	(2,276)	(2,053)
Decrease/(increase) in accrued income	830	(868)
Decrease/(increase) in debtors	96	(24)
Increase in creditors	241	111
	31,040	**27,837**

21 Analysis of Change in Net Debt

	At 1 April 2003 £'000	*Cash* flows £'000	*Other non-cash* changes £'000	*Exchange* movement £'000	*At 31 March* 2004 £'000
Cash at bank and in hand	3,915	16,479	–	–	**20,394**
Loans due within one year	(23,475)	(26,487)	(31,478)	6,091	**(75,349)**
Loans due in more than one year	(31,478)	–	31,478	–	**–**
Debenture stocks	*(152,272)*	–	*61*	–	**(152,211)**
	(203,310)	**(10,008)**	**61**	**6,091**	**(207,166)**

22 Directors' Interest in Contracts

No Director has a contract of service with the Company.

During the year no Director was interested in any contract or other matter requiring disclosure under section 232 of the Companies Act 1985.

23 Contingencies, Guarantees and Financial Commitments

At the year end the Company had a contingent liability amounting to £14 million (2003 – £14 million) under a subscription agreement relating to participating loan notes. The obligation will expire on 31 December 2005.

24 Summary of Main Investment Restrictions

(as incorporated within the investment management agreement between the Company and Baillie Gifford & Co)

Holding size

At the time of investment, a maximum of 8% of total assets may be invested in any one holding. This restriction does not apply to investment in collective investment schemes, issues by way of rights or certain government bonds.

A maximum of 40% of total assets may be invested in holdings exceeding 3% of the value of the Company's total assets. Again, this restriction does not apply to collective investment schemes, issues by way of rights or certain government bonds.

Categories of investment

No investment shall be made on which there is unlimited liability.

The Managers must seek permission of the Board to invest in collective investment schemes managed by Baillie Gifford & Co.

Transactions in futures and options must be consistent with Inland Revenue guidelines so as to ensure maintenance of the Company's Investment Trust status.

25 Derivatives and Other Financial Instruments

The Company operates as an investment trust company in accordance with S842 of the Income and Corporation Taxes Act 1988. The international nature of the Company's investment activities provides opportunities for both market appreciation and currency gains, but leaves it exposed to the risk of market volatility and currency fluctuations.

In the case of an investment trust, capital profits from investing activities and currency gains are not recognised in the revenue account, but are credited directly to a separate capital reserve which the Company is prohibited from distributing in the form of dividends.

Gearing

The Company has long term and short term borrowings. The aim of the use of gearing is to enhance long term returns to shareholders by investing borrowed funds in equities and other assets. Gearing is actively managed. How and where borrowings are invested is reviewed by the Board in consultation with the Managers at every Board meeting. In light of the decisions made, appropriate adjustments to the gearing position are then made by the Managers. Details of borrowings and where they are invested is given in monthly Factsheets published on the Managers' website, **www.bailliegifford.com**

The Company's revenue account may be affected by fluctuations in short term interest rates; income from overseas investment can be affected by currency fluctuations.

The Company's financial instruments, which provide finance for investment activities, comprise its debenture stocks, its long and short term borrowings, and its cash and liquid resources. In addition to the equity portfolio, the Company maintains investments in UK and overseas corporate bonds as part of its investment strategy.

The Company may, from time to time, enter into derivative transactions to hedge specific currency or interest rate risk. No such transactions were undertaken in the period under review.

The Company has precisely defined guidelines to govern the purchase or writing of options on individual shares. No options were purchased or written in the year under review.

Trading in financial instruments is not within the normal activities of an investment trust, nor is it the Company's policy to trade in such instruments. Transactions in financial instruments generally arise as a result of strategic investment decisions.

The Company's Managers may not enter into derivative transactions without the prior approval of the Board, and all borrowing facilities require Board authorisation. The Board agrees policies for managing risk with the Company's Managers. The main risks arising from the Company's financial instruments are market risk (as noted above), interest rate risk, credit risk, liquidity risk and foreign currency risk.

Interest Rate Risk

The Company finances its operations by means of realised capital profits, retained revenue reserves, bank borrowings and the issue of debenture stocks. The value of the Company's bond portfolio is subject to interest rate risk. It is not the Company's policy to hedge this risk.

The Company has negotiated short term multi-currency borrowing facilities at interest rates linked to LIBOR and may draw down funds for a period of up to 12 months.

The Company has issued a mix of stepped and fixed interest debenture stocks. The stepped interest debenture stocks have reached their final step and are deemed to be fixed.

Credit Risk

In addition to interest rate risk, the Company's investments in bonds are also subject to credit risk. Credit risk reflects the possibility that a borrower will not be able to meet its obligation to make payments of interest or principal when they fall due. The Managers analyse the credit risk of the Company's bond investments prior to purchase and continue to monitor developments in credit quality subsequently.

Liquidity Risk

The Company's policy with regard to liquidity is to ensure continuity of funding. Short term flexibility is achieved by overdraft facilities.

Foreign Currency Risk

The international nature of the Company's investment activities gives rise to a currency risk which is inherent in the performance of its overseas investments. It is not the Company's policy to hedge this risk on a continuing basis, but the Company may from time to time match specific overseas investment with foreign currency borrowings.

The revenue account is subject to currency fluctuation arising on overseas income. The Company does not hedge this currency risk.

The Annual General Meeting of the Company will be held at the new offices of Baillie Gifford & Co, Calton Square, 1 Greenside Row, Edinburgh EH1 3AN, on Thursday, 1 July 2004 at 4.00 pm.

If you have any queries as to how to vote or how to attend the meeting, please call us on 0800 027 0133.

Notice of Annual General Meeting

Notice is hereby given that the ninety-fifth Annual General Meeting of Scottish Mortgage Investment Trust PLC will be held within the Registered Office of the Company, Calton Square, 1 Greenside Row, Edinburgh EH1 3AN, *on Thursday, 1 July 2004, at* 4.00 pm for the following purposes:

Ordinary Business

1. To approve the Accounts of the Company for the year to 31 March 2004 with the Reports of the Directors and of the Auditors thereon.
2. To approve the Directors' Remuneration Report.
3. To declare a dividend.
4. To elect Mr MM Gray as a Director.
5. To elect Lord Strathclyde as a Director.
6. To re-elect Mr WG McQueen as a Director.
7. To re-elect Mr GA Ball as a Director.
8. To reappoint KPMG Audit Plc as Auditors.
9. To authorise the Directors to determine the remuneration of the Auditors.

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

10. That, in substitution for any existing authority under section 166 of the Companies Act 1985 (the 'Act'), but without prejudice to the exercise of any such authority prior to the date hereof, the Company be authorised, in accordance with section 166 of the Companies Act 1985 (the 'Act'), to make market purchases (within the meaning of section 163(3) of the Act) of ordinary shares of 25p each in the capital of the Company ('Shares'), provided that:

(a) the maximum aggregate number of Shares hereby authorised to be purchased shall be 14.99% of the issued ordinary share capital on the date on which this resolution is passed;

(b) the minimum price which may be paid for a Share shall be 25p;

(c) the maximum price (exclusive of expenses) which may be paid for a Share shall be an amount equal to 105% of the average of the middle market quotations (as derived from the Daily Official List of the London Stock Exchange) for the Shares for the 5 business days immediately preceding the date of purchase; and

(d) unless previously varied, revoked or renewed by the Company in general meeting, the authority hereby conferred shall expire at the conclusion of the Annual General Meeting of the Company to be held in 2005 or 31 December 2005, whichever is the earlier, save that the Company may, prior to such expiry, enter into a contract to purchase Shares under such authority which will or might be completed or executed wholly or partly after the expiration of such authority and may make a purchase of Shares pursuant to any such contract.

By order of the Board

Baillie Gifford & Co Baillie Gifford & Co
Managers and Secretaries
28 May 2004

Notes

1 A member entitled to attend and vote at the meeting is entitled to appoint one or more proxies to attend and, on a poll, vote on his/her behalf. A proxy need not be a member of the Company. A Form of Proxy for the use of members is enclosed.

2 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 6.00 pm on 29 June 2004 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 6.00 pm on 29 June 2004 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 the meeting, notwithstanding any provisions in any enactment, the articles of association of the Company or other instrument to the contrary.

3 Shareholders participating in the Baillie Gifford Investment Trust Share Plan, Children's Savings Plan or the Baillie Gifford Investment Trust ISA/PEP who wish to vote and/or attend the meeting must complete and return the enclosed reply-paid Form of Direction.

4 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, by asking a professional adviser to do so, or through the Baillie Gifford savings vehicles (see inside back cover for details).

Sources of Further Information on the Company

The price of shares is quoted daily in the Financial Times and can also be found on the Baillie Gifford website at **www.bailliegifford.com**, Trustnet at **www.trustnet.co.uk** and on other financial websites. Company factsheets are also available on the Baillie Gifford website and are updated monthly. These are available from Baillie Gifford on request.

Key Dates

Ordinary shareholders normally receive two dividends in respect of each financial year. An interim dividend is paid at the end of November and a final dividend is paid in early July. The AGM is normally held in early July.

Capital Gains Tax

For Capital Gains Tax indexation purposes, the market value (adjusted for the bonus issue of 4 for 1) of an ordinary share in the Company as at 31 March 1982 was 30.6p.

Share Register Enquiries

Computershare Investor Services PLC maintains the share register on behalf of the Company. In the event of queries regarding shares registered in your own name, please contact the Registrars on 0870 702 0010. By quoting the reference number on your share certificate you can check your holding on the Registrars' web site: **www-uk.computershare.com/investor.**

Telephone Share Dealing Service

A telephone share dealing service has been established with our Registrar, Computershare Investor Services PLC, which provides shareholders with a way of buying or selling Scottish Mortgage Investment Trust PLC ordinary shares on the London Stock Exchange. There are no forms to complete and the share price at which you deal will generally be confirmed to you whilst you are still on the telephone. Please ensure you have your Shareholder Reference Number (SRN) ready when making the call. The SRN appears on your share certificate. For further information about this service please phone 0870 702 0000.

Please note that this share dealing service is not available to shareholders participating in the Baillie Gifford Investment Trust Share Plan, Children's Savings Plan, ISA and PEP.

This is not a recommendation to buy, sell or hold shares in Scottish Mortgage. If you are unsure of what action to take contact a financial adviser authorised under the Financial Services and Markets Act 2000. Please note that share values may go down as well as up, which may result in you receiving less than what you originally invested.

Computershare Investor Services PLC is authorised and regulated by the Financial Services Authority.

Electronic Communications and Proxy Voting

If you hold stock in your own name you can choose to receive communications from the Company, and vote, in electronic format. This method reduces costs, is environmentally friendly and, for many, is convenient too. The paragraphs below explain how you can use these services.

- **Electronic Communications** If you would like to take advantage of this service, please visit our Registrar's website at **www-uk.computershare.com/investor** and register. You will need your shareholder reference number (which is on your share certificate and tax voucher)

Analysis of Shareholders

	At 31 March 2004 Number	%	At 31 March 2003 Number	%
Institutions	119,787,855	40.3	119,212,623	40.0
Intermediaries	87,828,979	29.5	85,011,649	28.5
Individuals	66,966,028	22.5	70,707,032	23.7
Baillie Gifford Share Plan/PEP/ISA	19,859,703	6.7	19,553,382	6.6
Marketmakers	2,862,550	1.0	3,520,429	1.2
	297,305,115	**100.0**	298,005,115	100.0

to hand. If you then agree to the terms and conditions, in future, on the day that documents are sent to shareholders by post, you will receive an e-mail providing *the website address link to the* documents. After you register, paper documents will be available on request.

- **Electronic Proxy Voting** You can also return proxies electronically at **www-uk.computershare.com/proxy**. If you have registered for electronic communications you will be issued a PIN number to use when returning proxies to the secure Registrar website. You do not need to register for electronic communications to use electronic proxy voting, paper proxy forms will contain a PIN number to allow you to return proxies electronically.

If you have any questions about these services please contact Computershare on 0870 702 0000.

CREST Proxy Voting

If you are a user of the CREST system (including a CREST Personal Member), you may appoint one or more proxies or give an instruction to a proxy by having an appropriate CREST message transmitted. To appoint a proxy or to give an instruction to a proxy (whether previously appointed or otherwise) via the CREST system, the CREST message must be received by the issuer's agent (ID number 3RA50) not later than 48 hours before the time appointed for holding the meeting. For this purpose, the time of receipt will be *taken to be the time (as determined by the* timestamp generated by the CREST system) from which the issuer's agent is able to retrieve the message. CREST Personal Members or other CREST sponsored members should contact their CREST sponsors for assistance with appointing proxies via CREST. For further information *on CREST procedures, limitations and* systems timings, please refer to the CREST Manual. The Company may treat as invalid a proxy appointment sent by CREST in the circumstances set out in Regulation 35(5)(a) of the Uncertificated Securities Regulations 2001. Computershare Investor Services PLC is authorised and regulated by *the Financial Services Authority*.

Where this has been received in a country where the provision of such a service would be contrary to local laws or regulations, this should be treated as information only.

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

- Participation in a diversified portfolio of shares.
- Constant supervision by experienced professional managers.
- The Trust is free from capital gains tax on capital profits realised within its portfolio.

These accounts have been approved by the Directors of Scottish Mortgage Investment Trust PLC. Baillie Gifford Savings Management Limited is the ISA Manager of the Baillie Gifford Investment Trust ISA, the PEP Manager of the Baillie Gifford Investment Trust PEP and the Manager of the Baillie Gifford Investment Trust Share Plan and Children's Savings Plan. Baillie Gifford Savings Management Limited is wholly owned by Baillie Gifford & Co. Both are authorised and regulated by the Financial Services Authority. Baillie Gifford only provides information about its products and does not provide investment advice. The staff of Baillie Gifford may have positions in Scottish Mortgage and may buy, sell or offer to make a purchase or sale of such securities from time to time. The value of ISA and PEP tax advantages will depend on personal circumstances. Past performance is no guarantee of future performance. The capital value of and income distributed by an investment trust can go down as well as up and an investor may not get back the amount originally invested. The price of an investment trust share will fluctuate in accordance with supply and demand and may not reflect the underlying net asset value.

Scottish Mortgage's shares are traded on the London Stock Exchange. They can be bought through a stockbroker, by asking a professional adviser to do so, or through the Baillie Gifford savings vehicles – see below.

Baillie Gifford's Investment Trust Share Plan

You can invest from £250 or from £30 per month. The plan is designed to be a cost-effective way of saving on a regular or lump sum basis.

Baillie Gifford's Investment Trust ISA

You can invest in a tax efficient way by investing a minimum of £2,000 or from £250 per month or by transferring an ISA with a value of at least £2,000 from your existing manager.

Baillie Gifford's Children's Savings Plan

A cost-effective plan tailored especially to meet the requirements to save for children. You can invest a minimum of £250 or from £30 per month.

Baillie Gifford's Investment Trust PEP Transfer

You can transfer an existing PEP to access a different market or to change your investment manager (minimum value of £2,000).

Further Information

Retail Investments Department
Baillie Gifford Savings Management Limited
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1 Greenside Row
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Tel: 0800 027 0133
We may record your call

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Directors

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Sir Donald MacKay

GA Ball
MM Gray
WG McQueen
The Earl of Portarlington
JPHS Scott
Lord Strathclyde

Registrar

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Company Broker

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Auditor

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Saltire Court
20 Castle Terrace
Edinburgh EH1 2EG

Company Registration No. 7058

Managers, Secretaries and Registered Office

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