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# The Baillie Gifford Japan Trust PLC

Annual Report & Accounts  
31 August 2000

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# Company Summary

## COMPANY DATA AT 31 AUGUST 2000

Total assets†	Shareholders' funds	Market capitalisation
£192m	£165m	£160m

† total assets less current liabilities before deduction of bank loans.

<b>Policy and Objective</b>	<i>Baillie Gifford Japan's objective is to pursue long-term capital growth principally through investment in medium to smaller sized Japanese companies which are believed to have above average prospects for growth. The portfolio usually consists of around 50 holdings at any one time.</i>
<b>Benchmark</b>	The portfolio benchmark against which performance is measured is 75% TOPIX and 25% Tokyo Stock Exchange Second Section Index in sterling terms.
<b>Management Details</b>	Baillie Gifford & Co are appointed as investment managers and secretaries to the Company. The management contract can be terminated at twelve months notice.
<b>Capital Structure</b>	The Company's share capital consists of 12,750,000 ordinary shares of 25p each which are issued and fully paid. The Company has been granted authority to buy back a limited number of its own ordinary shares for cancellation. The Directors are seeking to renew this authority at the forthcoming Annual General Meeting.
<b>Management Fee</b>	Baillie Gifford & Co's annual remuneration is 1.0% of the net assets of the Company attributable to its shareholders, calculated on a quarterly basis.
<b>ISA/PEP</b>	An ISA and a PEP transfer facility are available (see inside back cover). Up to £7,000 per annum can be invested in a Maxi ISA currently.
<b>AITC</b>	The Company is a member of the Association of Investment Trust Companies.
<b>Continuance Vote</b>	The Company's Articles of Association give shareholders the right to vote annually at the AGM on whether the Company should continue in business.

# Year's Summary

	31 August 2000	31 August 1999	% change	
Total assets (total assets less current liabilities before deduction of bank loans)	£191.7m	£153.8m	24.6	
Bank loans	£26.4m	£23.3m	13.3	
Equity shareholders' funds	£165.3m	£130.5m	26.7	
Net asset value per ordinary share	1,296.5p	1,023.6p	26.7	
Share price	1,255.0p	880.0p	42.6	
Benchmark composite index			17.7	
TOPIX (in sterling terms)			17.9	
Tokyo Stock Exchange Second Section Index (in sterling terms)			17.2	
Earnings per ordinary share	(12.53p)	(2.47p)		
Expense ratio	1.34%	1.21%		
Premium/(discount)	(3.2%)	(14.0%)		
	Year to 31 August 2000		Year to 31 August 1999	
Year's high and low	High	Low	High	Low
Share price	1,362.5p	880.0p	884.5p	340.0p
Net asset value	1,476.0p	1,013.0p	1,028.0p	419.3p
Premium/(discount)	1.5%	(15.8%)	(6.7%)	(19.7%)
	31 August 2000		31 August 1999	
Total return per ordinary share				
Revenue	(12.53p)		(2.47p)	
Capital	285.50p		571.16p	
Total	272.97p		568.69p	

# Five Year Summary

The following charts indicate how an investment in Baillie Gifford Japan has performed relative to its benchmark and its underlying net asset value over a five year period to 31 August 2000:

## TEN YEAR RECORD

### CAPITAL

At 31 August	Total assets† £'000	Bank loans £'000	Equity shareholders' funds £'000	Net asset value per share p	Diluted net asset value per share* p	Share price p	Premium/ (discount) # %
1990	62,926	-	62,926	572.1	-	496.0	(13.3)
1991	65,586	-	65,586	596.2	-	565.0	(5.2)
1992	48,055	-	48,055	436.9	436.9	372.0	(14.9)
1993	87,214	-	87,214	792.8	773.4	749.0	(5.5)
1994	84,416	-	84,416	767.4	756.0	708.0	(7.7)
1995	81,221	6,590	74,631	678.4	673.2	681.0	0.4
1996	101,293	12,961	88,332	669.2	-	630.0	(5.9)
1997	87,356	11,277	76,079	576.4	-	535.0	(7.2)
1998	68,581	9,305	59,276	449.1	-	362.5	(19.3)
1999	153,759	23,255	130,504	1,023.6	-	880.0	(14.0)
<b>2000</b>	<b>191,733</b>	<b>26,425</b>	<b>165,308</b>	<b>1,296.5</b>	<b>-</b>	<b>1,255.0</b>	<b>(3.2)</b>

† Total assets comprise total assets less current liabilities before deduction of bank loans.

\* The diluted net asset value per ordinary share figures have been calculated in accordance with FRS 14 'Earnings per share'.

# Premium/(discount) is the difference between Baillie Gifford Japan's quoted share price and its underlying net asset value.

### REVENUE

### GEARING RATIOS

Period to 31 August	Gross revenue £'000	Available for ordinary shareholders £'000	Earnings per ordinary share p	Expense ratio¶ %	Actual gearing‡	Potential gearing§
1990	848	(30)	(0.28)	1.19	84	100
1991	897	54	0.49	1.24	94	100
1992	428	(342)	(3.11)	1.26	96	100
1993	719	(169)	(1.54)	1.21	96	100
1994	608	(389)	(3.54)	1.08	95	100
1995	522	(375)	(3.41)	1.03	105	109
1996	671	(666)	(5.27)	1.25	107	115
1997	545	(661)	(5.01)	1.13	110	115
1998	834	(205)	(1.55)	1.15	92	116
1999	1,149	(325)	(2.47)	1.21	117	118
<b>2000</b>	<b>866</b>	<b>(1,597)</b>	<b>(12.53)</b>	<b>1.34</b>	<b>109</b>	<b>116</b>

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

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

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

### CUMULATIVE PERFORMANCE

At 31 August	Net asset value per share	Share price	Benchmark ††	TOPIX ††	Tokyo Stock Exchange Second Section Index ††
1990	100	100	100	100	100
1991	104	114	99	104	86
1992	76	75	72	78	52
1993	139	151	138	150	103
1994	134	143	138	147	112
1995	119	137	119	130	85
1996	117	127	116	125	89
1997	101	108	90	101	58
1998	79	73	58	65	36
1999	179	177	110	114	98
<b>2000</b>	<b>227</b>	<b>253</b>	<b>130</b>	<b>134</b>	<b>115</b>

#### Compound Annual Returns

5 year	13.8%	13.0%	1.8%	0.7%	6.2%
10 year	8.5%	9.7%	2.7%	3.0%	1.4%

†† Source: Primark Datastream.

The original warrants issued on 15 December 1981 were exercised by 30 November 1989. The warrants issued on 20 November 1991 were exercised by 5 December 1995.

# Directors and Management

## Directors

**Malcolm Murray CBE**, the Chairman, is 62 years old and is a former director and chief general manager of The Scottish Life Assurance Company. He was previously investment manager of that company and had been involved in investment management for over thirty years. He is chairman of the Trustees of University of Edinburgh Trust Funds, a director of Scottish and Newcastle Pensions Investments (1998) Ltd and investment adviser to the Smith & Nephew UK Pension Fund. He was appointed the Chairman of The Baillie Gifford Japan Trust PLC on the Company's inception in 1981.

**Richard Barfield**, who is 53, was appointed a Director in 1997. He serves on the Executive Committee of the Association of Investment Trust Companies and was formerly chief investment manager of The Standard Life Assurance Company. He is a director of Equitas Limited, The Merchants Trust plc and other companies.

**Graham McCallum CBE**, who is 74, was appointed a Director in 1981. He was formerly an executive director of John Swire & Sons Ltd in London, and is a director of Pacific Horizon Investment Trust PLC.

**George Veitch**, who is 57, was appointed a Director in 1989. He is a partner of Baillie Gifford & Co, which he joined in 1969. He has had overall responsibility for managing Baillie Gifford's Japanese investments since 1981.

## Managers and Secretaries

Baillie Gifford Japan is managed by Baillie Gifford & Co, an investment management business formed in 1927 out of the legal firm Baillie & Gifford, WS, which had been involved in investment management since 1908.

Baillie Gifford is one of the five largest investment trust groups in the UK and currently manages six 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 £22 billion. Based in Edinburgh, it is one of the leading privately owned investment management firms in the UK, with 20 partners and a staff of over 300.

The manager of Baillie Gifford Japan is Sarah Whitley, a partner of the firm. She is supported by a team of ten people covering the Japanese market and has been involved with Baillie Gifford Japan since 1985.

The firm of Baillie Gifford & Co is regulated by IMRO.

Malcolm Murray  
Chairman

# Chairman's Statement

The Association of Investment Trust Companies (AITC) has recently issued its Guide to Good Practice for the Report & Accounts of Investment Trust Companies. The purpose of this Guide, which is non-prescriptive, is to encourage the provision of information that shareholders say is most valuable to them and to recommend how that information might be presented in order to maximise clarity, consistency and comparability. Your Board welcomes the Guide and has incorporated the vast majority of its recommendations, including the disclosure of fund performance against a formal performance benchmark. The Company has a specialist mandate to invest in medium and smaller sized Japanese companies. There is no single index that recognises this specialist universe at the present time. Accordingly, the Company has adopted a composite benchmark comprising a 75% weighting in TOPIX and a 25% weighting in the Tokyo Stock Exchange Second Section Index, both indices converted to a sterling basis. We believe this to be the most appropriate benchmark at the moment. However, the area of indices is rapidly developing in Japan and if a more suitable index emerges we would be prepared to adopt it as our benchmark and shareholders would be informed of the proposed change.

## Performance

The year to 31 August 2000 has been another successful one for the Company with the net asset value rising by 26.7% to 1,296.5p per share. This increase was comfortably ahead of the 17.7% rise in the Company's benchmark index. The share price over the same period increased by 42.6%. This outcome means that the Company produced the highest share price return and the second highest net asset value return within the Japanese investment trust sector (source: AITC) over the year to 31 August 2000. It was, however, very much a year of two contrasting halves with an exceptionally strong first half being followed by a disappointing second half. Over the first six months of the Company's year the market continued the strong upward trend which began in the earlier part of 1999 when evidence that the economy was beginning to recover provided support. The rise was driven by an exceptionally strong performance by stocks in industries such as electronics and communications, which have excellent growth prospects. Heavy buying both by domestic and especially by foreign investors pushed share prices of such issues sharply higher. However, market conditions changed and investors then sold the highly rated technology issues, especially foreign investors alarmed by a sharp fall in such stocks in the US. Over the past few months the market has been particularly volatile and declining despite a background of rising economic activity and a robust recovery in corporate profits. Nevertheless, the overall outcome can be considered encouraging following last year's exceptional performance. Since the

Japanese stockmarket began to recover in late 1998, the increase in net asset value per share over the last two years to 31 August has been 188.7%. As is customary, the Managers' Report on page 8 reviews the performance in greater detail.

## Revenue Account

Revenue for the year declined by 24.6% mainly because the Company did not hold any short term UK government bonds as it had on a temporary basis the previous year. These had the effect of substantially boosting the prior year's income. A rise in costs linked to the strong growth in the asset value and a full year's interest charge on the Company's borrowings produced an increased loss for the year. On a per share basis the loss was 12.53p compared with a loss of 2.47p the previous year. No dividend can be recommended.

## Continuance Vote

Shareholders have the right every year to vote on whether the Company should continue in business. At the Annual General Meeting to be held on 24 November 2000, as an item of special business, shareholders will have the opportunity to vote on the continuance of the Company. Last year the Company received support for continuance from 99.4% of those voting and your Directors believe that the improved economic conditions and rising profitability of Japanese companies combined with the Company's good performance are positive reasons for the Company's continuance in business. Accordingly, the Directors intend to vote their own shareholdings in favour of the resolution. I encourage shareholders to give due consideration to this important matter and express their wishes by casting their vote.

## Share Split


The Company's share price on 31 August 2000 was £12.55. In order to increase the liquidity and hence the marketability of the shares, the Board is proposing that the shares be split in the ratio of 5 new shares for each existing share thereby reducing the nominal value per ordinary share from 25p to 5p. A further advantage of this change will be that the lower share price will allow greater efficiency in the management of the Baillie Gifford Investment Trust Share Plan for investors who choose to invest regular payments with Baillie Gifford Japan. My fellow Directors and I recommend that shareholders vote in favour of the proposal.

## Share Buy Backs

Shareholders voted at the Annual General Meeting held in November 1999 to renew the Company's power to buy back up to 14.99% of its outstanding shares. The purpose of using such power is to enhance the net asset

value of the Company for remaining shareholders by buying back shares at a substantial discount to the net asset value. For most of the past year the discount to net asset value has been low both in absolute terms and relative to the Japanese investment trust sector and the opportunity to buy back shares on attractive terms limited. Therefore, no shares have been repurchased. However, your Board believes that it is essential that the Company retains the power to transact share buy backs and hence, at the Annual General Meeting to be held on 24 November 2000, it is seeking a renewal of the power to buy back up to 14.99% of the Company's shares. My fellow Directors and I intend to support the proposal and urge shareholders to do likewise.

#### AITC Publicity Campaign

Last year the Board agreed that the Company should support the Association of Investment Trust Companies campaign to promote and publicise the case for investing in investment trusts under the slogan . The marketing plan has featured extensive television and newspaper advertising and is designed to boost the awareness of the investment trust sector to private individuals. We have renewed our support of this campaign for a further year in the belief that any reduction in the discount to net asset value on which the shares trade as a result of such activity is to the benefit of shareholders.

#### Directors' Fees

Directors' fees were last increased in September 1997. Total Directors' fees for the year ending 31 August 2000 were £35,000 which are considerably lower than those of comparable Japanese investment trust companies. We, therefore, propose to increase total fees to £44,000 to reflect growth in the size of the Company and the increased responsibilities faced by Directors from legislative changes. In 1994 shareholders authorised the Directors to approve their remuneration within an overall limit of £50,000 on total fees. The proposed increase in fees leaves the Board with little flexibility and so shareholders approval is being sought to increase the total fee limit to £75,000.

#### Borrowing and Hedging

The Company had unchanged borrowings at 31 August 2000 of ¥4,100 million (£26.4 million), which represents 16.0% of net assets. From the August 1999 year end to the end of February 2000 most of these borrowings had been invested. We then adopted a more cautious approach to the market and sold or reduced a number of stocks which reduced our net gearing (borrowings less cash) to below 3% by the end of May 2000. In August we began to utilise the gearing again and at 31 August 2000 the net gearing had risen to 8.8% of net assets.

The Company has been unhedged over the past year, a period when the yen rose by 13.6% against sterling. Our policy remains to hedge only when we believe the yen to be significantly overvalued.

#### Outlook

Evidence continues to build that the Japanese economy is recovering. The most recent GDP figures to the end of June 2000 show that the economy expanded by 1% over the year and further improvement seems likely going forward. The decision by the Bank of Japan in August 2000, despite political opposition, to end its zero interest rate policy by raising the overnight call rate to 0.25% was based on its belief that economic growth was becoming stronger and that the deflationary pressure that Japan has suffered for many years is easing. Japan has a new Prime Minister, Mr Mori, who replaced Mr Obuchi who died. The election called by Mr Mori saw his Liberal Democratic Party lose seats but retain power with the support of coalition partners. No significant policy changes have resulted from the change of leadership and we believe that the government remains committed to building a sustainable recovery in the economy. It is especially encouraging that corporate profits are rising strongly. The benefits of lower costs from restructuring plans implemented by many companies have enabled profit margins to rise. We expect further progress in boosting corporate returns this year.

While there are fundamental reasons to be optimistic about Japan, the short-term technical position of the market is a concern. In particular, the unwinding of cross-held shares and the flow of new issues is increasing supply of stock at a time when investor demand is weak. This has proved a dampener on the stockmarket over the last few months, as has a resurgence of bad debt fears after the bankruptcy of Sogo, a leading Japanese department store group. In spite of such concerns, we believe that the healthier economy and the likely upward revisions in profit forecasts will reverse the recent bout of weakness in the market and that the changes underway are positioning Japan for a period of improved performance.



G Malcolm Murray  
5 October 2000

# Managers' Report

## INVESTMENT CHANGES (£'000)

	Valuation at 31 Aug 1999	Net acquisitions (disposals)	Appreciation (depreciation)	Valuation at 31 Aug 2000
Equities (including convertibles):				
Electricals	20,254	13,195	15,602	49,051
Manufacturing and machinery	15,248	7,650	2,382	25,280
Retail	13,369	3,516	1,542	18,427
Commerce and services	31,772	(6,775)	1,095	26,092
Pharmaceuticals and food	13,959	1,364	2,042	17,365
Real estate, construction and housing	4,253	2,300	(740)	5,813
Financials and utilities	24,422	1,991	(7,533)	18,880
Telecoms and Internet	23,107	(37,634)	22,784	8,257
Chemicals and other materials	8,232	1,004	1,751	10,987
<b>Total investments</b>	<b>154,616</b>	<b>(13,389)</b>	<b>38,925</b>	<b>180,152</b>
Net liquid assets/(liabilities)	(857)	11,804	634	11,581
<b>Total assets</b>	<b>153,759</b>	<b>(1,585)</b>	<b>39,559</b>	<b>191,733</b>
Bank loans	(23,255)	(12)	(3,158)	(26,425)
<b>Equity shareholders' funds</b>	<b>130,504</b>	<b>(1,597)</b>	<b>36,401</b>	<b>165,308</b>

### Performance and Portfolio Changes

Over the year, the net asset value per share has risen by 26.7% to 1,296.5p. The Japanese yen appreciated by 13.6% against sterling, significantly helping returns. We were fully invested in yen assets throughout the year, with no currency hedging. Japanese stockmarket indices were little changed over the year in yen terms, but this masked a big divergence between the two halves of the year. In the first half of the Company's year, Japanese markets soared and the Company made substantial amounts of money in the Telecoms and Internet sector. In the second half, the euphoria surrounding new economy stocks waned and, with the market becoming more value oriented, the Company underperformed its benchmark.

Over the year as a whole, the Company's NAV outperformed its new composite benchmark index and both the TOPIX and Tokyo Second Section indices.

The bar chart on the top half of page 9 shows the Company's returns in each of the key sectors against TOPIX. This chart is derived from the new performance attribution analysis table shown on the bottom half of page 9 which compares the performance of the Company relative to TOPIX (full sector performance of the new composite benchmark was not available). This performance attribution analysis is calculated on a monthly chain-linked basis and so the total return does not tally exactly with the NAV performance, although

the underlying trends are correct. The breakdown of our performance shows that stock selection was a larger contributor to outperformance than asset allocation, a reflection of our focus on selecting individual companies.

The table at the top of this page gives details of the investment changes which we have made in each of the industrial sectors over the past year. The sectors shown are slightly different from the TOPIX industry classifications used in the performance analysis on page 9. A footnote at the base of page 9 explains the differences. Details of the top ten holdings and some of the new purchases are on pages 14 to 17.

The most significant contributions to performance came from the Telecoms, Electricals, Commerce and services and Retail sectors. The biggest negative contribution came from the Financials area.

In Telecoms and Internet, we began the year with 14.9% of our investments in the sector. After exceptional performance, this had risen to 21.2% by the end of February and we then took significant profits. We sold Hikari Tsushin (retailer of mobile phone handsets), Softbank (Internet investment company), NTT DoCoMo (mobile telecoms operator) and Matsushita Communications (manufacturer of mobile phone handsets), many of which were large holdings. These sales proved well timed, as most of the stocks sold are now priced significantly lower. By the

The chart below compares Baillie Gifford Japan's performance with that of TOPIX, by industrial sector.

PORTFOLIO PERFORMANCE ATTRIBUTION FOR THE YEAR TO 31 AUGUST 2000

PERFORMANCE ATTRIBUTION RELATIVE TO TOPIX (in sterling terms)

	TOPIX	Baillie Gifford Japan		Performance*		Contribution to relative return %	Contribution attributable to:	
	allocation	asset allocation		BG Japan	TOPIX		Stock selection	Asset allocation
	01.09.99 %	01.09.99 %	31.08.00 %	%	%	%	%	%
Equity markets†								
Electricals	16.7	18.0	30.8	83.3	55.2	3.7	3.5	0.2
Manufacturing and machinery	15.8	12.7	14.1	2.6	13.6	(0.9)	(1.1)	0.2
Retail	5.2	10.2	11.1	8.4	(8.4)	1.3	2.5	(1.1)
Commerce and services	11.2	26.4	15.8	15.2	13.6	1.4	1.4	–
Pharmaceuticals and food	7.1	10.6	10.5	13.5	12.9	0.2	0.1	0.1
Real estate, construction and housing	3.0	3.2	3.5	(20.0)	(6.8)	(0.3)	(0.5)	0.2
Financials	19.4	17.5	11.4	(22.7)	(2.0)	(2.9)	(3.6)	0.8
Telecoms and utilities	11.3	12.7	5.0	31.8	33.6	4.6	3.0	1.5
Chemicals and other materials	10.3	6.3	6.6	18.1	15.4	0.5	0.1	0.5
Cash	–	0.1	7.2	–	–	–	–	–
Gearing	–	(17.7)	(16.0)	15.8	15.8	0.5	–	0.5
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>28.3</b>	<b>17.9</b>	<b>8.8</b>	<b>5.4</b>	<b>3.3</b>

Source: The WM Company

Contributions cannot be added together, they are geometric; for example, to calculate how a return of 28.3% (against a TOPIX return of 17.9%) translates into a relative return of 8.8%, divide the portfolio return of 128.3 by the TOPIX return of 117.9.

† The performance tables above use sectoral classifications as defined by TOPIX. However, for the purposes of investment changes and the breakdown of the Company's portfolio by sector, we have used slightly different, more common sense sectoral definitions to try to reflect more appropriately the businesses that the Company's holdings are involved in. For example, Softbank, which is Japan's leading Internet stock, is classified by TOPIX under Commerce and services; we believe it more sensible to place it in the Telecoms and Internet sector.

\* The above returns are capital returns, calculated on a monthly chain-linked method. The total return for Baillie Gifford Japan under this method is 28.3% as compared to the rise in the net asset value per share for the year of 26.7%.

year-end the Company was underweight in the Telecoms and Internet sector, with our only addition being DDI, the telecoms operator which should benefit from its merger with two other telecoms companies in October. For the year, this sector was the most positive contributor to the Company's relative return.

We were overweight in the Electricals sector, which was the best performing sector of TOPIX. We also benefited greatly in this area from individual stock selection. We believe that changes occurring in Japan, such as the increasing spread of Internet usage and rapidly expanding spending by businesses on technology, are best played through the hardware companies which benefit from this growth and are on reasonable valuations. We added to Electricals during the year by buying three electronic component makers, *Kyocera, Mitsumi Electric and Murata Manufacturing*. We sold the holding in *Hitachi Medical*, the manufacturer of medical equipment, because it did not meet profit expectations. The Electricals sector represents our largest overweight position against the benchmark (see bar chart on page 12).

The Retail sector of TOPIX declined during the year, but our stocks did well and the area provided a positive overall return. We continued to have a large overweight position throughout the year, concentrating our investments on speciality retailers which we believe will enjoy good results despite the weak consumption background in Japan. Our largest Retail holding is *Fast Retailing*, which we bought during the year. It has developed a highly competitive product line-up by offering high quality casual clothes at low prices and has built a widely recognised brand name. We also purchased shares in the leading toy retailer, *Toys R Us*, which listed during the year. In Commerce and services, our positive performance again came from stock selection. We made major changes in this area, selling five of the eleven companies held at the previous year-end, for valuation or operational reasons, and buying three new holdings.

In the Financial sector we were correctly underweight in one of the worst performing areas of the market. However, much of our investment in the sector was in non-bank financial companies, many of which did particularly poorly. We made a small reduction in the Company's weighting in the Financial sector over the year.

### Economy

The Japanese economy has continued to recover from recession over the past year, although the progress as measured by the quarterly GDP figures has been

erratic. Growth for the fiscal year to the end of March 2000 was 0.5%, whilst expectations for the current year are now above 2% having risen steadily over the past few months. Recent experience has highlighted the poor quality of economic data in Japan, a point now acknowledged by the government who are working to improve its reliability. Despite impressive monthly figures, such as industrial production, the GDP data theoretically showed that Japan returned to recession in the second half of 1999. Rapid growth was then shown in the first half of the current year. We believe that the underlying trend has been much steadier and look for continued expansion in the second half of the year.

Perception and reality have also diverged in the make-up of the recovery. Despite the large number of supplementary budgets over the past few years, the expansion has not been reliant on public spending with the private sector producing most of the growth. For example, corporate profits are now recovering rapidly in Japan, rising 40% year-on-year in the last quarter. In a significant change of behaviour from that of previous cycles, companies are increasing capital spending at a slower rate than profits are recovering. This bodes well both for long term profitability and improving returns. The make-up of such spending is also being transformed, as technology investment rises, mimicking trends in the US in the 1990s. This may well have positive implications for overall productivity, which lags Japan's competitors, longer term.

On the other hand the positive change in corporate behaviour, with labour costs being trimmed and spending restrained, is having a negative impact on consumers, who remain relatively cautious. Although unemployment has not risen as rapidly as some feared, incomes have only just started to grow as job offers in the new areas of the economy expand rapidly. The difficulties in accurately measuring consumption, as patterns of spending have changed dramatically over the last decade, have also meant that any recovery has been difficult to pick-up. However, there are tentative signs of improvement particularly in the larger metropolitan areas and we expect that consumption will show more robust signs of expansion next year.

### Corporate Change

We believe that the fundamental drivers of corporate behaviour in Japan have changed, and that the results of this will become increasingly apparent over the next few years. Although the government is reluctant to unleash the full effect of market forces on the sectors still damaged by the bubble economy, notably banking and construction, there are a number of areas where

developments are progressing rapidly. As mentioned above corporate profits are recovering rapidly, and this is generating strong cash flow of around 4% of GDP per annum. This is strengthening balance sheets significantly and allowing many companies to free themselves from their keiretsu group.

Pressures for change have continued to build and now include new accounting standards, taxation adjustment to allow easier mergers and acquisitions, legislative changes on the corporate code and ongoing globalisation trends which are bringing increased competition and foreign capital to Japan. These are resulting in more rapid selling of cross shareholdings and the unveiling of corporate assets and liabilities not previously shown in accounts. Those companies which are in the weakest positions are the worst affected with several quoted companies finally declaring bankruptcy over the summer. The better managed companies, however, are beneficiaries of the greater transparency. Against this background we continue to believe that company specific investment decisions will yield the best returns.

#### Financial Sector

Further consolidation and reform have taken place in the last year within Japan's financial system. The announced merger of three major banks to form Mizuho, the largest banking group in the world, was followed by three other significant merger plans. Sumitomo Bank is to combine with Sakura Bank, a move that crosses traditional keiretsu boundaries between the Sumitomo and Mitsui groups. Sanwa Bank, Tokai Bank and Toyo Trust are to merge, creating a banking operation with a powerful retail presence. Finally, Bank of Tokyo Mitsubishi is to amalgamate with Mitsubishi Trust. All four new groups have announced ambitious medium-term financial targets, aimed at cutting costs, moving into new business lines, and boosting returns on equity from their current low levels into double digits. However, recent operational performance by Japan's city banks has remained disappointing, hampered by the continuing burden of high credit costs and a legacy of imprudent lending during the bubble period. Banks have been compensating by realising substantial profits on their equity portfolios, but reciprocal selling of cross shareholdings by companies has put pressure

on banks' own share prices. It is still too early to be confident that these balance sheet bad debt problems are near resolution, given the recent spate of major company bankruptcies.

Outside the banking sector there have been the first signs of restructuring in the hitherto static insurance industry, spurred partly by government deregulation. In the non-life sector there have been mergers announced between Sumitomo and Mitsui, Nippon and Koa, and Chiyoda and Dai-Tokyo, helping to consolidate the industry around five major groups. These moves give the potential for significant cost cutting and balance sheet reform. Japan's ailing life insurers seem increasingly prepared to combine with non-life insurance companies or foreign operators. Meanwhile Japan's securities houses are emerging as significant beneficiaries of financial reform in general: demand for mutual funds and for investment banking expertise is growing as households diversify their assets from low-yielding bank deposits and corporate restructuring accelerates. Our holdings in the financial sector are positioned to take advantage of these developments.

#### Outlook

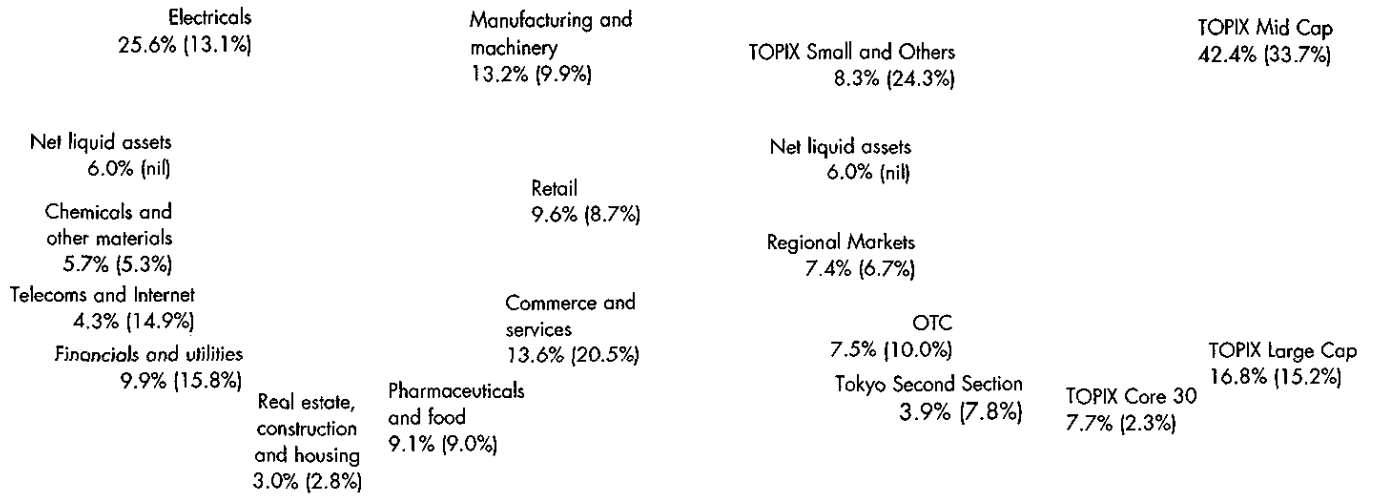
Although we remain optimistic about growth prospects in Japan, we acknowledge that there are risks such as policy errors by the government or adverse global trends. However many companies are pushing forward with change, even if not encouraged by government policy, in response to the changing background that they face. The stockmarket has been focusing in recent months on the negative implications of some of these changes, such as accelerating cross shareholding unwinding, and the impact of a rise in interest rates, which was well-flagged by the Bank of Japan. Whilst aware that these factors may well affect market sentiment for some time, we believe that the corporate profits background and the valuation level of the market justify a more positive outlook. We therefore invested some of the gearing into the market towards the company's year end and believe that the continuing economic recovery and the changes in corporate behaviour should benefit equity prices in due course.

Baillie Gifford & Co  
5 October 2000

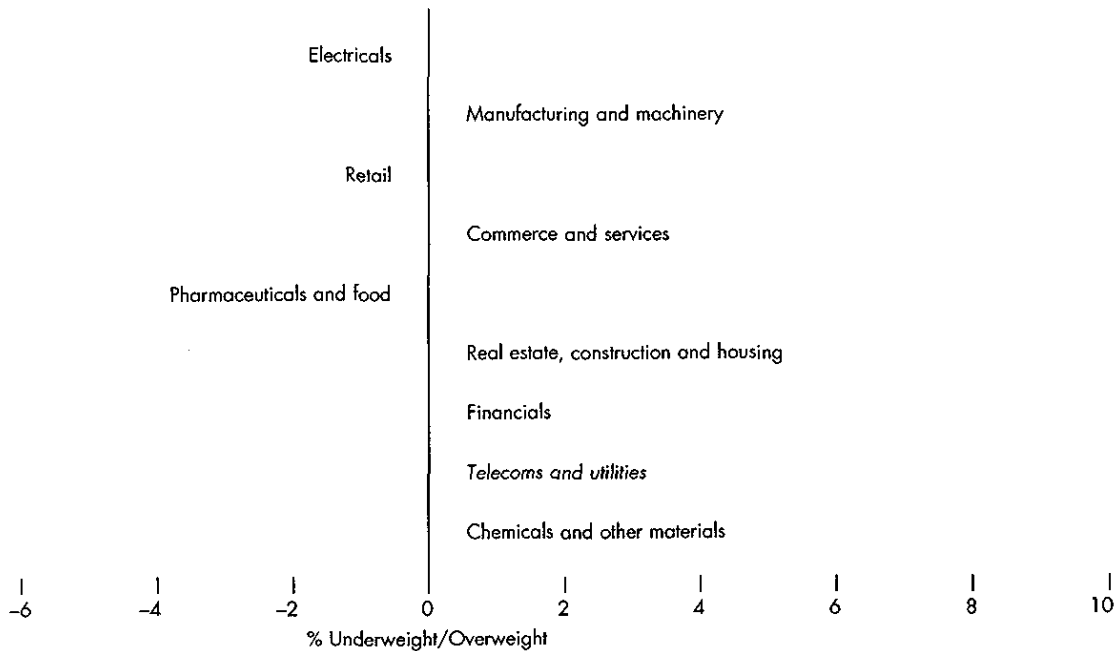
**DISTRIBUTION OF PORTFOLIO**

**Industry 2000 (1999)**

**Listing 2000 (1999)**



**INDUSTRY RELATIVE TO COMPOSITE BENCHMARK**



TWENTY LARGEST EQUITY HOLDINGS

Name	Business	Market value £'000	% of total assets
Rohm	Specialist semiconductors	6,709	3.5
Kyocera	Telecoms and electronics	5,890	3.1
Fast Retailing	Casual wear retailer	5,517	2.9
Nippon Broadcasting System	Radio and TV broadcasting	5,470	2.9
Sumitomo Bakelite	Specialist electronic materials	5,453	2.8
Taiyo Yuden	Capacitors and electronic parts	5,391	2.8
Promise	Consumer finance	5,095	2.7
Yamatake Corporation	Control systems	5,093	2.7
Matsumotokiyoshi	Pharmacy retail chain	4,950	2.6
DDI	Telecoms operator	4,873	2.5
Fanuc	Robot and equipment manufacturer	4,860	2.5
Nichicon	Capacitors	4,818	2.5
Chugai Pharmaceutical	Pharmaceutical manufacturer	4,653	2.5
Kobayashi Pharmaceutical	Household products	4,435	2.3
Minebea	Miniature bearings	4,180	2.2
Takeda Chemical Industries	Pharmaceutical manufacturer	4,067	2.1
Takefuji	Consumer finance	3,969	2.1
Murata Manufacturing	Electrical components	3,968	2.1
Capcom	Games software	3,935	2.0
H.I.S.	Discount travel agency	3,921	2.0
		97,247	50.8

# Review of Investments

A review of the Company's ten largest investments together with some of the Company's new acquisitions is given below and on the following three pages. We thank the various companies concerned for supplying photographs of their activities.

## TOP TEN HOLDINGS

### Rohm

3.5% of total assets

Rohm is one of the most successful and dynamic manufacturers of semiconductor devices and other electronic components in Japan. It has focused its business on certain key areas, concentrating on customised semiconductor components, and hence has enjoyed high profit margins. Earnings growth has

averaged 22% per annum over the past 5 years. Rohm is not overly reliant on any single industry or product and management has shown a consistent ability to adapt and improve the company. We believe that Rohm can continue to generate superior returns for shareholders.

### Kyocera Corporation

3.1% of total assets

Kyocera Corporation is a leading manufacturer of a range of electronic components and semiconductor devices. It also makes telecommunication equipment, cellular phone handsets, and has a minority stake in the Japanese telecom operator KDDI. Recent order flow has been very strong, driven by rising

demand for Kyocera's semiconductor components and parts for mobile phones. The recent purchase of Qualcomm's cellular handset business in the USA strengthens Kyocera's world-wide position in that market. Given the strength of demand, we believe that Kyocera will continue to enjoy above average profits growth.

### Fast Retailing

2.9% of total assets

Fast Retailing has established itself in a short space of time as Japan's leading retailer of low-priced, basic, casual clothing. Its success has been founded on a simple strategy: it sources well-made, low-priced goods from China, does all of its own distribution thus cutting costs, and sells the clothes through a nationwide

chain of branded stores. In the year to the end of August, earnings are likely to have quadrupled. We are confident that Fast Retailing will continue to gain market share from its higher-priced rivals and thus enjoy superior earnings growth in the medium term.

### Nippon Broadcasting System

2.9% of total assets

NBS is the top radio broadcaster in the Tokyo region. Its radio business has been weak because of falling radio advertising, although volumes have recently been increasing again. NBS's most important asset is not its core radio business but its 34% stake in Fuji TV, one of the three top TV companies in Japan. Fuji TV is especially strong in drama production

and has a stake in the satellite company, SkyPerfectTV. It has a young, dynamic management team and has been benefiting from rising advertising rates on TV, as well as from cutting costs. We believe that the stockmarket is significantly undervaluing NBS given the value of its stake in Fuji TV.

*Retailing is Japan's foremost retailer of priced casual clothing*

*Broadcasting's headquarters in Tokyo the Rainbow Bridge*

**Sumitomo Bakelite**

2.8% of total assets

Sumitomo Bakelite is the global market leader in the production of semiconductor sealant materials, with a market share in excess of 30%. This division has been the main driver of sales and profits. It is now using its technical expertise in semiconductor sealants to diversify into other markets, such as consumer electronics

and computers. Profitability improved sharply last year as the company successfully cut costs and withdrew from some unprofitable materials businesses. The new president has been focussing more on profitability and we believe that the company should continue to enjoy good earnings growth.

**Taiyo Yuden**

2.8% of total assets

Taiyo Yuden is an electronic components maker. The company's products include inductors, capacitors, and recordable compact discs. Taiyo Yuden has been a beneficiary of the shift from analogue to digital technology in consumer electronic

products. The company delivered very strong results for the year to March 2000, when operating profit rose by 230% from the previous year. Order flow in the first half of this year has also been robust, so profits should continue to rise rapidly.

**Promise**

2.7% of total assets

Promise provides unsecured loan facilities to consumers. This is a segment of the market that has not been served effectively by banks in Japan, allowing specialist companies such as Promise to achieve consistently strong lending growth and high profit margins. Recent data suggests the company is performing better than its competitors. A new corporate logo and advertising

campaign has led to a sharp increase in new customer growth, while better credit monitoring has reduced bad loan provisions, so profits are exceeding expectations. Meanwhile, the unsecured lending market overall continues to expand at a double digit rate. Promise's valuation is relatively low compared to the strength of its earnings growth.

- 1 *A Taiyo Yuden plant for the manufacture of electronic components in Gunma prefecture*
- 2 *Promise makes unsecured loans for consumers through a nationwide network of branches*

**Yamatake Corporation**

2.7% of total assets

Yamatake is 22%-owned by Honeywell of the US and manufactures control systems for buildings (air-conditioning, heating and security), as well as control equipment and systems for use by manufacturers. The building systems business should benefit from a replacement cycle, as Yamatake's equipment is already installed in

19,000 buildings. The industrial control business is geared to capital expenditure, which is rising rapidly, and there is scope for a significant improvement in margins in this segment. Valuations on the shares are not high given the growth prospects, and the balance sheet is very strong, which will allow Yamatake to improve its product range through acquisition.

**Matsumotokiyoshi**

2.6% of total assets

Matsumotokiyoshi runs a chain of chemist shops and is a clear leader in the drug-store industry in Japan. It has been successfully gaining market share from the smaller independent pharmacies and attracting new customers in urban areas. The company's strategy is to open stores in prime locations and use television advertising to emphasise its wide

range of products sold at low prices. This has enabled it to establish a strong brand name and to generate significant customer drawing power. Management plans to increase the number of stores to 500 in the greater Tokyo region by March 2002, which should feed through to continued double digit earnings growth.

**DDI**

2.5% of total assets

DDI was established in 1985 as a long-distance domestic telecommunications operator and subsequently diversified into the cellular telephone business. On October 1 2000, it merged with KDD, the international telecommunications operator and with IDO, an unlisted cellular operator, to form KDDI. The new company will have strong positions in all segments

of the Japanese telecoms market and should derive considerable synergy benefits. It will cross-sell its products, particularly to corporate clients, will derive significant cost savings and will create a new nationwide brand, 'Au', for its cellular phone division. We expect profits to recover robustly and feel that the stock market is being too pessimistic about the outlook for the new company.

**NEW HOLDINGS**

**Capcom**

2.0% of total assets

Capcom develops game software and coin operated game machines as well as operating amusement arcades. It has undergone significant restructuring in recent years, focusing on profitability by introducing control systems based on company division, software title and return on investment. Management has continuously paid down debt, so that all loans should be repaid by the end

of this year. Capcom has had considerable success with one or two game software titles such as *Dino Crisis* and *Resident Evil* while not being over-reliant on one game. The launch of Sony's *PlayStation 2* game console should significantly boost Capcom's sales. Valuations on the shares appear undemanding given the likelihood of above average profits growth.

Smart Electromagnet Flowmeter  
#7000

relaunched its cellular telephone division  
- the brand name 'Au' in October 2000

**Mitsumi Electric**  
2.0% of total assets

Mitsumi Electric manufactures and assembles electronic parts and peripherals such as integrated circuits, drives and remote controls. The company has become involved in several exciting growth areas such as voice ports used in cable TV boxes and components for rewriteable CDs and DVDs. These newer products

carry much higher margins than more traditional areas and the company should post a strong recovery in profitability after two years of declines. The company's competitive position within the new segments is strong and the rating on the stock is relatively undemanding within the sector.

**Daiwa Securities Group**  
1.6% of total assets

Daiwa is one of Japan's leading securities companies, with particular strength in retail broking. Conditions for Japanese brokers have improved sharply after several poor years. Rising stock exchange trading volumes have boosted profitability in the short term, while structural growth in high margin investment trust sales

and investment banking activities is helping to build more sustainable revenue streams for these companies. Daiwa is attractively valued against its counterparts, and should gain substantial new business from the merger of its affiliate Sumitomo Bank with Sakura Bank.

**Toys R Us Japan**  
1.5% of total assets

Toys R Us Japan was listed in April of this year on the OTC market. The company is 48% owned by Toys R Us US. The company's strategy is very similar to the US parent's category-killer approach and is based on everyday-low pricing, lots of variety and full inventories. Japan is the second largest toy market in the world at ¥1.15trn behind the US's ¥2.94trn (1999 figures). The company has been very successful in its pricing strategy (typically more than 10%

below the recommended retail price) and is now Japan's leading toy retailer with a market share of over 10%. It has enjoyed cumulative sales growth of 30% per annum over the last five years. Much of the market share gain has been at the expense of weaker rivals such as Chiyoda and Marutomi. We believe the company can continue to take its market share higher despite a dull outlook for the overall Japanese toy market.

<sup>1</sup> Mitsumi Electric's mold component numerically controlled electric discharge machining

<sup>2</sup> A newly opened Toys R Us store in Odaiba, Tokyo

LIST OF INVESTMENTS AS AT 31 AUGUST 2000

Name	Where listed	Business	Market value £'000	% of total assets
<b>ELECTRICALS</b>				
Alpine Electronics	TOPIX Mid	Car audio and navigation systems	2,340	
Kyocera	TOPIX Large	Telecoms and electronics	5,890	
Matsushita Kotobuki Electronics	TOPIX Mid	HDD manufacturer	2,887	
Mitsumi Electric	TOPIX Mid	Electronic parts	3,877	
Murata Manufacturing	TOPIX Core	Electrical components	3,968	
Nichicon	TOPIX Mid	Capacitors	4,818	
#Nidec Corporation	Regional	Specialist industrial components	1,308	
Nikon	TOPIX Mid	Cameras and semiconductor production equipment	2,908	
Rohm	TOPIX Core	Specialist semiconductors	6,709	
Taiyo Yuden	TOPIX Mid	Capacitors and electronic parts	5,391	
Tokyo Electron	TOPIX Large	Semiconductor production equipment	3,862	
Yamatate Corporation	TOPIX Mid	Control systems	5,093	
			<u>49,051</u>	25.6
<b>MANUFACTURING AND MACHINERY</b>				
Fanuc	TOPIX Large	Robot and equipment manufacturer	4,860	
Fuji Heavy Industries	TOPIX Mid	Maker of Subaru brand automobiles	3,536	
Keihin	TOPIX Mid	Automobile parts	683	
Kokuyo	TOPIX Mid	Automobile parts	2,065	
Minebea	TOPIX Mid	Miniature bearings	4,180	
Sankyo (Pachinko)	TOPIX Mid	Pachinko machinery	1,933	
SMC	TOPIX Large	Pneumatic control equipment	3,045	
Suzuki Motor	TOPIX Mid	Automobiles and motorcycles	1,239	
THK	OTC	Linear motion bearings	3,739	
			<u>25,280</u>	13.2
<b>RETAIL</b>				
Fast Retailing	TOPIX Mid	Casual wear retailer	5,517	
Matsumotokiyoshi	Other	Pharmacy retail chain	4,950	
Shimachu	TOPIX Mid	Furniture and DIY stores	1,273	
Toys R Us Japan	OTC	Toy retail chain	2,900	
#Yamada Denki	OTC	Consumer electronics retailer	3,787	
			<u>18,427</u>	9.6
<b>COMMERCE AND SERVICES</b>				
Benesse	Regional	Education by correspondence	3,683	
Capcom	Regional	Games software	3,935	
Fujitsu Support & Services	Tokyo 2nd	Software development	1,877	
H.I.S.	OTC	Discount travel agency	3,921	
Japan Airlines	TOPIX Large	Airline	1,481	
Nippon Broadcasting System	Tokyo 2nd	Radio and TV broadcasting	5,470	
Onward Kashiwama	TOPIX Mid	Apparel manufacturer	2,929	
Otsuka Shokai	TOPIX Small	Software and office machinery sales	1,861	
World	Regional	Women's apparel manufacturer	935	
			<u>26,092</u>	13.6

LIST OF INVESTMENTS

Name	Where listed	Business	Market value £'000	% of total assets
<b>PHARMACEUTICALS AND FOOD</b>				
Chugai Pharmaceutical	TOPIX Mid	Pharmaceutical manufacturer	4,653	
Ito En	TOPIX Mid	Tea and soft drinks producer	1,527	
Kobayashi Pharmaceutical	Regional	Household products	4,435	
#Kuraya Sanseido Inc.	TOPIX Small	Pharmaceutical wholesaler	2,683	
Takeda Chemical Industries	TOPIX Core	Pharmaceutical manufacturer	4,067	
			<u>17,365</u>	9.1
<b>REAL ESTATE, CONSTRUCTION AND HOUSING</b>				
Noritz	TOPIX Small	Kitchen and bath manufacturer	3,845	
Okumura	TOPIX Mid	Construction and civil engineering	1,968	
			<u>5,813</u>	3.0
<b>FINANCIALS AND UTILITIES</b>				
Credit Saison	TOPIX Mid	Retail credit cards	3,319	
Daiwa Securities Group	TOPIX Large	Broker	2,966	
#Kokusai Securities	TOPIX Mid	Broker	1,391	
Promise	TOPIX Large	Consumer finance	5,095	
Seventy-Seven Bank	TOPIX Mid	Regional bank	2,140	
Takefuji	TOPIX Mid	Consumer finance	3,969	
			<u>18,880</u>	9.9
<b>TELECOMS AND INTERNET</b>				
DDI	TOPIX Large	Telecoms operator	4,873	
Japan Telecom	TOPIX Mid	Telecoms operator	3,384	
			<u>8,257</u>	4.3
<b>CHEMICALS AND OTHER MATERIALS</b>				
Rengo	TOPIX Small	Cardboard manufacturer	2,526	
Sumitomo Bakelite	TOPIX Mid	Specialist electronic materials	5,453	
Unicharm	TOPIX Mid	Nappy manufacturer	3,008	
			<u>10,987</u>	5.7
		Value of equity stocks	175,321	
		Convertible loan stocks having an element of equity	<u>4,831</u>	
<b>TOTAL EQUITY INVESTMENTS</b>			180,152	94.0
<b>NET LIQUID ASSETS</b>			11,581	6.0
<b>TOTAL ASSETS AT MARKET VALUE (before deduction of bank loans)</b>			<u>191,733</u>	100.0
<b>BANK LOANS</b>			<u>(26,425)</u>	(13.8)
<b>EQUITY SHAREHOLDERS' FUNDS</b>			<u>165,308</u>	86.2

# denotes holding partly or wholly in convertibles

# Directors' Report

The Directors submit their Annual Report together with the results of the Company for the year to 31 August 2000.

## 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' Report and the Review of Investments on the preceding pages.

## Dividend

The Board does not recommend any dividend for the year.

The accumulated revenue deficit is increased by £1,597,000 to £5,260,000.

## Status

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 August 1998. In the opinion of the Directors the Company has subsequently conducted its affairs so as to enable it to continue to obtain such approval.

The Company will continue to seek approval under section 842 of the Income and Corporation Taxes Act 1988 each year. However, under Corporation Tax Self Assessment, which applies to accounting periods ended after 30 June 1999, the Inland Revenue will no longer be obliged to give written approval. Instead the Inland Revenue have twelve months after the return filing date in which to give notice that they intend to enquire into the return but if no such notice is given then approval may be assumed to have been obtained.

## Corporate Governance

The Committee on Corporate Governance published its report on the principles of good governance and code of best practice ('the Combined Code') in June 1998.

The Board has considered the principles set out in the Combined 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 Combined Code.

### *The Principles of Good Governance*

#### *The Board*

The Board's regular meetings take place every two months. It has a number of matters reserved for its approval, including investment policy, borrowings, treasury matters and dividend policy. The Board also reviews the financial statements, investment transactions, revenue budgets and performance.

The Board currently comprises four Directors, all of whom are non-executive and three of whom are independent of the Company's Managers. Mr G Veitch is a partner of Baillie Gifford & Co. 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. Mr GM Murray was appointed Chairman in 1981 and is also the senior independent member. Given the size and composition of the Board it is not felt necessary to separate the roles of Chairman and senior independent member. The Directors all have appropriate business and financial experience with which to conduct the business of the Board. Information about them can be found on page 5.

Given the non-executive nature of the Board a separate nomination committee has not been established. It is the view of the Board that the appointment of new Directors should be a matter for consideration by the Board as a whole. Upon appointment each Director is provided with a summary of the responsibilities and duties of directors, together with relevant background information on the Company. Consistent with the recommendation of the Code of Best Practice, the Board will provide appropriate training for new Directors where necessary.

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 that they submit themselves for re-election. In order to ensure compliance with the spirit of this provision, the Board has resolved further that no Director shall serve for a period of greater than three consecutive years without submitting himself for re-election.

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

#### *Remuneration*

Since all Directors are non-executive, the Company is not required to comply with principles B.1 to B.3 of the Combined Code in respect of executive Directors' remuneration. There is no separate remuneration committee and the Board as a whole considers changes in Directors' fees from time to time.

In setting Directors' fee levels, it is the Company's policy to take account of fees paid by comparable investment trusts to ensure that remuneration is sufficient to attract Directors of the appropriate quality and experience.

No Director has a contract of service and there is no notice period. Directors' fees are detailed in note 4 on page 30; no other benefits are provided.

#### *Internal Controls*

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 The Bank of New York Europe Limited and The Fuji Bank, Limited as independent custodians of the Company's investments.

Baillie Gifford & Co has a long established compliance function in accordance with IMRO 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. Baillie Gifford & Co has expanded its compliance department to establish an internal audit function responsible for ensuring that all significant strategic, commercial relationship, investment and operational risks are controlled effectively by management.

The Directors acknowledge their responsibility for the Company's system of internal financial controls, which is designed to provide reasonable but not absolute assurance against material misstatement or loss, and confirm that they have reviewed the effectiveness of the system.

In limiting their review to internal financial controls, the Directors have adopted the transitional approach recommended by the UK Listing Authority of the Financial Services Authority in respect of the implementation of the guidance "Internal Control: Guidance for Directors on the Combined Code" (the Turnbull guidance).

The Board has undertaken a full review of all aspects of the Turnbull recommendations. The Board confirms that, by formalising its review of the effectiveness of internal controls, it has established the procedures necessary to implement the guidance on the wider aspects of internal controls (the Turnbull guidance). To ensure that risk management and internal controls are considered on a regular basis and that a full risk and control assessment is undertaken, by 31 August 2000, 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 those risks are confirmed as in place and operating effectively.
- Reporting procedures for the internal audit function and compliance department, with regard to their respective risk framework and regulatory monitoring programmes, are defined and formalised within a service level agreement.

## DIRECTORS' REPORT

- Regular reports on internal controls are submitted for Board review.

In setting internal control policies, the Board has reviewed the guidance provided by the Association of Investment Trust Companies and has adopted their recommendations as they relate to a wholly non-executive Board, where the executive functions of investment management and administration have been delegated to third parties.

### *Accountability and Audit*

The respective responsibilities of the Directors and the auditors in connection with the Financial Statements are set out on pages 24 and 25.

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 all independent non-executive Directors. Its authority and duties are clearly defined within its written terms of reference. The Chairman of the Board has been appointed Chairman of the Audit Committee. The committee meets periodically to review the Company's interim and annual financial statements. It meets at least annually with the external auditors and approves the level of fees for audit and non-audit services.

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 and the Audit Committee regularly reviews the terms of the management agreement.

### *Relations with Shareholders*

The Company's Managers meet regularly with institutional shareholders and report to the Board. The Company's Annual General Meeting provides a forum for communication with private shareholders and the Board announces the level of proxies lodged. The notice period for the Annual General Meeting is twenty working days.

### *Compliance*

The Board considers that throughout the year it has complied with the Code of Best Practice published by the Committee on the Financial Aspects of Corporate Governance. In addition, the Board considers that throughout the year the Company has been in compliance with the Combined Code Provisions set out in Section 1 of the Combined Code on Corporate Governance issued by the UK Listing Authority of the Financial Services Authority, with the exception of the appointment of a nomination committee, the absence of which has been explained above.

As permitted by the UK Listing Authority of the Financial Services Authority, the Company has complied with the Combined Code provision D.2.1 on internal controls by reporting on internal financial controls in accordance with the guidance for directors on internal controls and financial reporting that was issued in December 1994.

### Directors

The Directors during the year under review, and their interests in the Company, were as follows:

Name	Nature of interest	Ordinary 25p shares held at	
		31 August 2000	31 August 1999
† GM Murray	Beneficial	4,210	4,210
† RA Barfield	Beneficial	1,193	1,193
† AGS McCallum	Beneficial	2,679	2,679
G Veitch	Beneficial	1,320	1,320

† Member of the Audit Committee

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

There have been no changes intimated in the Directors' interests up to 4 October 2000.

No Director has a contract of service with the Company.

### Substantial Holdings

The following information has been intimated to the Company as at 4 October 2000 in compliance with section 198 of the Companies Act 1985:

Name	Number of ordinary 25p shares held	% of issue
Scottish Equitable plc	1,158,490	9.09
Co-operative Insurance Society Ltd	606,883	4.76
The Scottish Life Assurance Company	440,440	3.45
Royal Liver Assurance Ltd	386,224	3.03

### Repurchase of Shares

At the last Annual General Meeting the Company was granted authority to purchase up to 1,911,225 ordinary shares (equivalent to 14.99% of its issued share capital), such authority to expire at the Annual General Meeting of the Company to be held in 2000.

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 demand for Baillie Gifford Japan's shares that results in a difference between the published net asset value per share and the quoted market price.

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 issue at the date of passing of the resolution, such authority to expire at the Annual General Meeting of the Company to be held in 2001. Under the Listing Rules of the London Stock Exchange, 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 five business days immediately preceding the date of purchase. The minimum price that may be paid will be 25p per share (or on the sub-division of each ordinary share of 25p each in the share capital of the Company into five ordinary shares of 5p, as described more fully below, the minimum price that may be paid will be 5p per share). Purchases of shares will be made within guidelines established, from time to time, by the Board. Your attention is drawn to Special Business, Resolution No. 8, in the Notice of Annual General Meeting.

### Share Capital

The Directors propose that each of the ordinary shares of 25p each in the share capital of the Company be sub-divided into five ordinary shares of 5p each, having the same rights attached to the ordinary shares of 25p each as set out in the Articles of Association of the Company. Whilst this will not affect the underlying value of an individual's shareholding in the Company, the Directors believe that this division will assist the marketability of the shares. Application for admission to the Official List of the UK Listing Authority and for trading on the main market of the London Stock Exchange will be made in respect of the ordinary shares of 5p. Trading in the ordinary shares will commence as soon as is practicable following the passing of the resolution. Your attention is drawn to Special Business, Resolution No. 6, in the Notice of Annual General Meeting.

### Share Certificates

The Directors are seeking greater flexibility in dealing with the issue of share certificates. This is of particular importance at this time to help minimise the cost of issuing new certificates to members following the sub division of share capital mentioned above. It is anticipated that new certificates will be sent no later than 1 December 2000 to those members who appear on the register of members on 24 November 2000. Thereafter existing share certificates in respect of ordinary shares of 25p each will cease to have any value and should be destroyed. Your attention is drawn to Special Business, Resolution No. 9, in the Notice of Annual General Meeting.

### Other Amendments to the Articles

The amendments to the Company's Articles of Association which are being proposed in Resolution No. 10 in the Notice of Annual General Meeting are designed to enable the Company to obtain investment company status even if any repurchase of ordinary shares is financed out of the Company's realised capital reserves. This takes account of a recent change in the Companies Act which enables investment companies to buy back shares from capital profits.

## DIRECTORS' REPORT

An investment company also has the benefit of being able to pay dividends out of net revenue profits without regard to capital profits or losses. These matters are not of major importance to the Company at this time but the Directors believe it is helpful to have as much flexibility as possible in such matters. There is also a minor administrative benefit in being an investment company in the preparation of the Company's Annual Report and Accounts. To qualify as an investment company, the distribution of capital profits except for the purchase of the Company's own shares, must be prohibited by the Company's Memorandum or Articles of Association.

### Directors' Remuneration

Shareholders will be asked at the Annual General Meeting to exercise the power vested in them under article 78 of the Articles of Association to increase the authorised sum payable to Directors from a sum not exceeding £50,000 in each year to a sum not exceeding £75,000 in each year. Your attention is drawn to Special Business, Resolution No. 7, in the Notice of Annual General Meeting.

### Continuation of the Company

The Company's Articles of Association give shareholders the right to vote annually at the Annual General Meeting of the Company on whether to continue the Company. The Directors wish to draw your attention to Special Business, Resolution No. 5, in the Notice of Annual General Meeting, which proposes that the Company be continued until the Annual General Meeting of the Company to be held in respect of the year ending 31 August 2001.

### 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 either 31 August 1999 or 31 August 2000.

### Auditors

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

By order of the Board

BAILLIE GIFFORD & Co  
Managers and Secretaries  
5 October 2000



## 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 ensuring that proper accounting records are kept which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the accounts 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.

# Auditors' Report

TO THE MEMBERS OF THE BAILLIE GIFFORD JAPAN TRUST PLC

We have audited the financial statements on pages 26 to 35.

## Respective responsibilities of Directors and Auditors

The Directors are responsible for preparing the Annual Report. As described on page 24, this includes responsibility for preparing the financial statements in accordance with applicable United Kingdom 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 our profession's ethical guidance.

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

We read the other information contained in the Annual Report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

We review whether the statement on pages 20 to 22 reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all the risks and controls, or to form an opinion on the effectiveness of the Company's corporate governance procedures or its risk and control procedures.


## Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

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

## Opinion

In our opinion the financial statements give a true and fair view of the state of the Company's affairs at 31 August 2000 and of its total return and cash flows for the year then ended and have been properly prepared in accordance with the Companies Act 1985.



PricewaterhouseCoopers  
Chartered Accountants and Registered Auditors  
Edinburgh  
5 October 2000

**STATEMENT OF TOTAL RETURN**  
(incorporating the revenue account\*)

	Notes	for the year ended 31 August 2000			for the year ended 31 August 1999		
		Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
Gains on investments	8	-	38,925	38,925	-	79,093	79,093
Currency losses	15	-	(2,524)	(2,524)	-	(4,009)	(4,009)
Income	2	866	-	866	1,149	-	1,149
Investment management fee	3	(1,751)	-	(1,751)	(933)	-	(933)
Other administrative expenses	4	(227)	-	(227)	(213)	-	(213)
<b>NET RETURN BEFORE FINANCE COSTS AND TAXATION</b>		<b>(1,112)</b>	<b>36,401</b>	<b>35,289</b>	<b>3</b>	<b>75,084</b>	<b>75,087</b>
Finance costs of borrowings	5	(360)	-	(360)	(243)	-	(243)
<b>RETURN ON ORDINARY ACTIVITIES BEFORE TAXATION</b>		<b>(1,472)</b>	<b>36,401</b>	<b>34,929</b>	<b>(240)</b>	<b>75,084</b>	<b>74,844</b>
Tax on ordinary activities	6	(125)	-	(125)	(85)	-	(85)
<b>RETURN ON ORDINARY ACTIVITIES AFTER TAXATION</b> <i>for the financial year attributable to equity shareholders</i>		<b>(1,597)</b>	<b>36,401</b>	<b>34,804</b>	<b>(325)</b>	<b>75,084</b>	<b>74,759</b>
<b>TRANSFER (FROM)/TO RESERVES</b>		<b>(1,597)</b>	<b>36,401</b>	<b>34,804</b>	<b>(325)</b>	<b>75,084</b>	<b>74,759</b>
<b>RETURN PER ORDINARY SHARE</b>	7	<b>(12.53p)</b>	<b>285.50p</b>	<b>272.97p</b>	<b>(2.47p)</b>	<b>571.16p</b>	<b>568.69p</b>

\* The revenue column of this statement is the profit and loss account of the Company.  
All revenue and capital items in the above statement derive from continuing operations.  
The accompanying notes on pages 29 to 35 are an integral part of this statement.

## BALANCE SHEET

		at 31 August 2000		at 31 August 1999	
	Notes	£'000	£'000	£'000	£'000
<b>FIXED ASSETS</b>					
Investments	8		180,152		154,616
<b>CURRENT ASSETS</b>					
Debtors	9	182		306	
Cash at bank and in hand		11,872		521	
		<u>12,054</u>		<u>827</u>	
<b>CREDITORS</b>					
Amounts falling due within one year	11	<u>(20,453)</u>		<u>(1,684)</u>	
<b>NET CURRENT LIABILITIES</b>			<b>(8,399)</b>	<b>(857)</b>	
<b>TOTAL ASSETS</b>					
less current liabilities			<u>171,753</u>		<u>153,759</u>
<b>CREDITORS</b>					
Amounts falling due after more than one year	12		<u>(6,445)</u>		<u>(23,255)</u>
			<u>165,308</u>		<u>130,504</u>
<b>CAPITAL AND RESERVES</b>					
Called-up share capital	14		3,188		3,188
Share premium			22,110		22,110
Capital redemption reserve			112		112
Capital reserve – realised	15		91,931		43,168
Capital reserve – unrealised	15		53,227		65,589
Revenue reserve	15		(5,260)		(3,663)
<b>EQUITY SHAREHOLDERS' FUNDS</b>	17		<u>165,308</u>		<u>130,504</u>
<b>NET ASSET VALUE PER ORDINARY SHARE</b>					
	16		1,296.5p		1,023.6p

The Accounts were approved by the Board and signed on their behalf on 5 October 2000.

  
Chairman

The accompanying notes on pages 29 to 35 are an integral part of this statement.

## CASH FLOW STATEMENT

		for the year ended 31 August 2000		for the year ended 31 August 1999	
	Notes	£'000	£'000	£'000	£'000
NET CASH (OUTFLOW)/INFLOW FROM OPERATING ACTIVITIES	18		(1,067)		465
<b>SERVICING OF FINANCE</b>					
Interest paid		(356)		(269)	
NET CASH OUTFLOW FROM SERVICING OF FINANCE			(356)		(269)
<b>TAXATION</b>					
Income tax repaid/(paid)		99		(101)	
Overseas tax suffered		(122)		(83)	
TOTAL TAX PAID			(23)		(184)
<b>FINANCIAL INVESTMENT</b>					
Acquisitions of investments		(87,110)		(48,812)	
Disposals of investments		100,559		39,136	
Realised currency gain		217		390	
NET CASH INFLOW/(OUTFLOW) FROM FINANCIAL INVESTMENT			13,666		(9,286)
NET CASH INFLOW/(OUTFLOW) BEFORE FINANCING			12,220		(9,274)
<b>FINANCING</b>					
Shares repurchased		(881)		(2,650)	
Bank loans drawn down		892		12,658	
Bank loans repaid		(880)		(2,690)	
NET CASH (OUTFLOW)/INFLOW FROM FINANCING			(869)		7,318
INCREASE/(DECREASE) IN CASH	19		11,351		(1,956)
<b>RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET DEBT</b>					
Increase/(decrease) in cash in the period	19		11,351		(1,956)
Net cash received from bank loans drawn down			(12)		(9,968)
Exchange movement on bank loans			(3,158)		(3,982)
MOVEMENT IN NET DEBT IN THE PERIOD			8,181		(15,906)
NET DEBT AT 1 SEPTEMBER 1999			(22,734)		(6,828)
NET DEBT AT 31 AUGUST 2000			(14,553)		(22,734)

The accompanying notes on pages 29 to 35 are an integral part of this statement.

## 1 PRINCIPAL ACCOUNTING POLICIES

A summary of the principal accounting policies is set out below. They are unchanged from last year and have been applied consistently, except for the adoption of FRS16 'Current Tax', which requires that UK dividend income is accounted for net of tax. As the Company had no UK dividend income in the period under review the introduction of FRS16 had no impact on the accounts in either 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 Statement of Recommended Practice 'Financial Statements of Investment Trust Companies'.

#### *True and fair view override*

The Company is not an investment company within the meaning of section 266 of the Companies Act 1985. However, it continues to conduct its affairs as an investment trust for taxation purposes under section 842 of the Income and Corporation Taxes Act 1988, and the Articles of the Company prohibit capital profits from being distributed by way of a dividend. As such, the Directors consider it appropriate to continue to present the accounts in accordance with the Statement of Recommended Practice 'Financial Statements of Investment Trust Companies' (the SORP). Under the SORP, the financial performance of the Company is presented in a statement of total return in which the revenue column is the profit and loss account of the Company. The revenue column excludes certain capital items which, since the Company is not an investment company, the Companies Act and FRS 3 would ordinarily require to be included in the profit and loss account: gains on disposal of investments, calculated by reference to their previous carrying amount of £12,594,000 (1999 – £5,929,000) and realised currency gains of £646,000 (1999 – losses of £69,000). In the opinion of the Directors the inclusion of these items in the profit and loss account would be misleading because they would obscure and distort both the revenue and capital performance of the Company, and would not show clearly the revenue profits emerging to be distributable by way of dividend. The Directors therefore consider that these departures from the specific provisions of Schedule 4 of the Companies Act relating to the form and content of accounts for companies other than investment companies and these departures from accounting standards are necessary to give a true and fair view. The departures have no effect on total return or on the balance sheet.

### (b) INVESTMENTS

UK Listed investments are shown at middle market value.

Listed investments and unlisted investments quoted on the Japanese Over-The-Counter market are shown at closing market prices. Other 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.

(iii) Unfranked investment income includes taxes deducted at source.

(iv) Interest receivable on bank deposits is dealt with on an accruals basis.

### (d) EXPENSES

All expenses are accounted for on an accruals basis and are charged through the revenue account except 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.

### (e) FINANCE COSTS

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

### (f) 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, with the exception of forward exchange contracts which are valued at the forward rate ruling 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.

### (g) CAPITAL RESERVES

Realised: Gains and losses on realisation of investments and realised exchange differences of a capital nature are dealt with in this reserve.

Unrealised: Unrealised appreciation/depreciation represents the amount by which the market value of assets and liabilities differs from their book value and is dealt with in this reserve.

## NOTES TO ACCOUNTS

	2000	1999
	£'000	£'000
<b>2 INCOME</b>		
<b>INCOME FROM INVESTMENTS</b>		
UK listed interest	-	557
Listed overseas dividends	786	517
Unlisted overseas dividends	45	48
Listed overseas interest	16	8
	<u>847</u>	<u>1,130</u>
<b>OTHER INCOME</b>		
Deposit interest	19	19
<b>TOTAL INCOME</b>	<u>866</u>	<u>1,149</u>
<b>3 INVESTMENT MANAGEMENT FEE – all charged to revenue</b>		
Investment management fee	1,732	893
Irrecoverable VAT thereon	19	40
	<u>1,751</u>	<u>933</u>

Baillie Gifford & Co are employed by the Company as Managers and Secretaries under a management agreement which is terminable on not less than twelve months' notice or on shorter notice in certain circumstances. Their fee in respect of each quarter is 0.25% of the total net assets of the Company attributable to its shareholders on the last day of that quarter.

Mr G Veitch, a Director of the Company, is a partner of Baillie Gifford & Co.

<b>4 OTHER ADMINISTRATIVE EXPENSES – all charged to revenue</b>		
General administrative expenses	186	170
Directors' fees	35	37
Auditors' remuneration – audit services	6	6
	<u>227</u>	<u>213</u>

General administrative expenses includes the Company's contribution to the AITC campaign of £49,000 (1999 – £9,000).

The Chairman's emoluments amounted to £11,000 (1999 – £11,000). The three other Directors who served on the Board throughout the year each received fees of £8,000 (1999 – £8,000) per annum. In the year to 31 August 1999, Mr DCP McDougall, who retired on 18 November 1998, received fees of £1,746. No pension contributions were made in respect of Directors.

<b>5 FINANCE COSTS OF BORROWINGS – all charged to revenue</b>		
On bank loans	<u>360</u>	<u>243</u>
<b>6 TAX ON ORDINARY ACTIVITIES</b>		
Overseas taxation	<u>125</u>	<u>85</u>

Unrelieved management expenses are available to be carried forward and may be offset against future taxable profits.

7 RETURN PER ORDINARY SHARE	2000			1999		
	Revenue	Capital	Total	Revenue	Capital	Total
	(12.53p)	285.50p	272.97p	(2.47p)	571.16p	568.69p

Revenue return per ordinary share is based on the net deficit on ordinary activities after taxation of £1,597,000 (1999 – £325,000) and on 12,750,000 (1999 – 13,146,027) 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 gains for the financial year of £36,401,000 (1999 – £75,084,000) and on 12,750,000 (1999 – 13,146,027) ordinary shares, being the weighted average number of ordinary shares in issue during the year.

	2000	1999
	£'000	£'000
<b>8 FIXED ASSETS – INVESTMENTS</b>		
Listed at market value – overseas	165,805	139,230
Unlisted – traded on the Japanese Over-The-Counter market	14,347	15,386
	<u>180,152</u>	<u>154,616</u>

	Listed overseas £'000	Unlisted £'000	Total £'000
Cost of investments held at 1 September 1999	83,609	6,741	90,350
Unrealised appreciation at 1 September 1999	55,621	8,645	64,266
Value of investments held at 1 September 1999	139,230	15,386	154,616
Movements in year:			
Purchases at cost	80,466	6,644	87,110
Sales – proceeds	(98,630)	(1,869)	(100,499)
– realised gains/(losses) on sales	49,777	(1,660)	48,117
Decrease in unrealised appreciation	(6,859)	(2,333)	(9,192)
Change in listing	1,821	(1,821)	–
Value of investments held at 31 August 2000	<u>165,805</u>	<u>14,347</u>	<u>180,152</u>
Cost of investments held at 31 August 2000	117,043	8,035	125,078
Unrealised appreciation at 31 August 2000	48,762	6,312	55,074
Value of investments held at 31 August 2000	<u>165,805</u>	<u>14,347</u>	<u>180,152</u>

	2000 £'000	1999 £'000
<b>GAINS ON INVESTMENTS</b>		
Realised gains on sales	48,117	3,356
(Decrease)/increase in unrealised appreciation	(9,192)	75,737
	<u>38,925</u>	<u>79,093</u>

	2000	1999
<b>9 DEBTORS</b>		
<i>Due within one year:</i>		
Income accrued	47	39
UK and withholding taxes deductible therefrom	(7)	(4)
	<u>40</u>	<u>35</u>
Sales for subsequent settlement	33	93
Taxation recoverable	2	101
Other debtors	107	77
	<u>182</u>	<u>306</u>

## NOTES TO ACCOUNTS

### 10 FINANCIAL ASSETS

A full list of the Company's investments is given on pages 18 and 19. In addition, an analysis of the equity portfolio by broad industrial or commercial sector is shown on page 12 and a list of the twenty largest equity investments by their aggregate market value is shown on page 13. All financial assets and liabilities are included in the accounts at market value (see note 1).

Exposure to currency risk is restricted, in the main, to fluctuations in the Japanese yen except where noted below.

	2000		1999	
	Market value £'000	Weighted average period until maturity	Market value £'000	Weighted average period until maturity
<i>Warrants:</i>				
Swiss francs	-	-	44	19 months
US dollars	-	-	1,072	5 months

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

	2000			1999		
	Market value £'000	Weighted average interest rate	Weighted average period until maturity	Market value £'000	Weighted average interest rate	Weighted average period until maturity
<i>Fixed rate Japanese convertible bonds:</i>						
Japanese yen denominated	2,997	0.3%	9 years	4,118	0.8%	6 years
Swiss franc denominated	1,834	0.1%	2 years	1,216	0.1%	3 years

	2000	1999
	£'000	£'000
<i>Cash:</i>		
UK deposits	575	238
Japanese yen deposits	11,297	283
	<u>11,872</u>	<u>521</u>

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.

### 11 CREDITORS

*Amounts falling due within one year:*

Bank loans (see note 12)	19,980	-
Amounts payable on shares repurchased	-	881
Forward contracts	-	417
Other creditors	473	386
	<u>20,453</u>	<u>1,684</u>

Included in other creditors is £413,000 (1999 - £326,000) in respect of the investment management fee.

	2000	1999
	£'000	£'000
<b>12 CREDITORS</b>		
<i>Amounts falling due after more than one year:</i>		
Bank loans	<u>6,445</u>	<u>23,255</u>

Bank loans of ¥4.1 billion (1999 – ¥4.1 billion) have been drawn down under yen loan facilities which are repayable between 29 November 2000 and 30 November 2001. The interest rate risk and maturity profiles of the bank loans are shown in note 13.

### 13 FINANCIAL LIABILITIES

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

	2000			1999		
	Market value £'000	Weighted average interest rate	Weighted average period until maturity	Market value £'000	Weighted average interest rate	Weighted average period until maturity
<i>Bank loans:</i>						
Yen denominated – fixed rate	<u>26,425</u>	1.4%	6 months	<u>23,255</u>	1.4%	18 months

	2000 £'000	1999 £'000
<i>Maturity profile:</i>		
In one year or less, or on demand	19,980	–
In more than one year, but not more than two years	6,445	17,583
In more than two years, but not more than five years	–	5,672
	<u>26,425</u>	<u>23,255</u>

All borrowings are stated at market value.

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

#### *Gains and losses on hedges*

At 31 August 2000 there were no unrecognised gains/losses on hedges. Realised currency profits/losses are taken to capital reserve and are not reflected in the profit and loss account unless they are of a revenue nature.

14 CALLED-UP SHARE CAPITAL	At 31 August 2000		At 31 August 1999	
	Number	£'000	Number	£'000
Authorised ordinary shares of 25p each	<u>13,200,000</u>	<u>3,300</u>	<u>13,200,000</u>	<u>3,300</u>
Allotted, issued and fully paid ordinary shares of 25p each	<u>12,750,000</u>	<u>3,188</u>	<u>12,750,000</u>	<u>3,188</u>

At the AGM in November 1999 shareholders granted the Company authority to purchase shares in the market up to 1,911,225 ordinary shares (equivalent to 14.99% of its issued share capital at that date). No ordinary shares were bought back during the year and, therefore at 31 August 2000 the Company's authority to buy back shares remained unchanged at 1,911,225.

Under the provisions of the Company's Articles share buy-backs are funded from the realised capital reserve. The nominal value of the share capital is maintained by the provision of a capital redemption reserve.

## NOTES TO ACCOUNTS

	Capital reserve – realised £'000	Capital reserve – unrealised £'000	Revenue reserve £'000
<b>15 RESERVES</b>			
At 1 September 1999	43,168	65,589	(3,663)
Net gain on realisation of investments	48,117	–	–
Decrease in unrealised appreciation on investments	–	(9,192)	–
Exchange differences on bank loans	12	(3,170)	–
Other exchange differences	634	–	–
Retained net deficit for the year	–	–	(1,597)
At 31 August 2000	<u>91,931</u>	<u>53,227</u>	<u>(5,260)</u>

### 16 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:

	2000	1999	2000 £'000	1999 £'000
<i>Ordinary shares</i>	<u>1,296.5p</u>	<u>1,023.6p</u>	<u>165,308</u>	<u>130,504</u>

The movements during the year of the assets attributable to the ordinary shares are shown in note 17.

Net asset value per ordinary share is based on the net assets as shown above and 12,750,000 (1999 – 12,750,000) ordinary shares, being the number of ordinary shares in issue at each date.

### 17 RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS

Shareholders' funds at 1 September 1999	130,504	59,276
Total recognised gains and losses for the year	34,804	74,759
Shares repurchased in the year	–	(3,531)
Shareholders' funds at 31 August 2000	<u>165,308</u>	<u>130,504</u>

### 18 RECONCILIATION OF NET REVENUE BEFORE FINANCE COSTS AND TAXATION TO NET

#### CASH (OUTFLOW)/INFLOW FROM OPERATING ACTIVITIES

Net return on ordinary activities before finance costs and taxation	(1,112)	3
(Increase)/decrease in accrued income	(8)	353
Increase in debtors	(30)	(64)
Increase in creditors	83	173
	<u>(1,067)</u>	<u>465</u>

	At 1 September 1999 £'000	Cash flows £'000	Other non- cash changes £'000	Exchange movement £'000	At 31 August 2000 £'000
<b>19 ANALYSIS OF CHANGE IN NET DEBT</b>					
Cash at bank and in hand	521	11,351	-	-	11,872
Loans due within one year	-	(12)	(17,583)	(2,385)	(19,980)
Loans due after one year	(23,255)	-	17,583	(773)	(6,445)
	<u>(22,734)</u>	<u>11,339</u>	<u>-</u>	<u>(3,158)</u>	<u>(14,553)</u>

**20 CONTINGENCIES, GUARANTEES AND FINANCIAL COMMITMENTS**

There were no contingent liabilities at either year end.

**21 DIRECTORS' INTERESTS 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.

Mr G Veitch, a Director of the Company, is a partner of Baillie Gifford & Co.

**22 DERIVATIVES AND OTHER FINANCIAL INSTRUMENTS**

The Company operates as an Investment Trust Company in accordance with Section 842 of the Taxes Act 1988. The 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.

*The Company makes use of gearing (long and short term borrowings) to achieve improved performance in rising markets.*

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 bank borrowings, cash and liquid resources. In addition, the Company maintains financial assets comprising a portfolio of Japanese equities and corporate bonds as part of its investment strategy.

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

The Company has precisely defined guidelines to govern transactions involving futures, contracts for differences and options. No transactions involving futures, contracts for differences or options, were undertaken 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 main risks arising from the Company's financial instruments are interest rate risk, liquidity risk and foreign currency risk. 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.*

*Interest Rate Risk*

The Company finances its operations by means of realised capital profits and bank borrowings.

The Company has negotiated yen bank borrowings, repayable between November 2000 and November 2001, at fixed rates of interest. In addition, the Company maintains a £4 million undrawn overdraft facility with The Bank of New York Europe Limited.

*Liquidity Risk*

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

The Company's assets comprise mainly readily realisable securities which can be sold freely to meet funding commitments if necessary.

*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 hedge against yen weakness through forward sales of yen.*

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

## NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that the nineteenth Annual General Meeting of The Baillie Gifford Japan Trust PLC will be held within the offices of Baillie Gifford & Co, 1 Rutland Court, Edinburgh EH3 8EY, on Friday, 24 November 2000 at 12.00 noon for the following purposes:

### Ordinary Business

1. To approve the Accounts of the Company for the year to 31 August 2000 with the Reports of the Directors and of the Auditors thereon.
2. To re-elect Mr RA Barfield as a Director.
3. To reappoint PricewaterhouseCoopers as Auditors.
4. To authorise the Directors to fix the remuneration of the Auditors.

### Special Business

To consider and, if thought fit, to pass the following resolutions as ordinary resolutions:

5. That, pursuant to article 148 of the Articles of Association of the Company, this meeting hereby approves the continuance of the Company until the Annual General Meeting of the Company held in respect of the year ending 31 August 2001.
6. THAT:
  - (a) each of the existing ordinary shares of 25p in the share capital of the Company be and hereby is subdivided into five ordinary shares of 5p ('Ordinary Shares'), such Ordinary Shares (both issued and unissued) having the rights set out in the Articles of Association of the Company; and
  - (b) the Articles of Association of the Company be and are hereby amended by the deletion of Article 3 and its substitution with the following Article 3:

"The share capital of the Company is £3,300,000 divided into 66,000,000 Ordinary Shares of 5p each."
7. That, with effect from 1 September 2000, a sum, not exceeding £75,000, will be set aside in each year and shall be applied by the Directors in payment for their remuneration.

To consider and, if thought fit, to pass the following resolutions as Special Resolutions:

8. That 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 (or on the passing of ordinary resolution 6 to be proposed at the Annual General Meeting of the Company to be held on 24 November 2000, ordinary shares of 5p each) in the capital of the Company ('Shares'), provided that:
  - (a) the maximum number of Shares hereby authorised to be purchased shall be 14.99% of the issued share capital on the date on which this resolution is passed;
  - (b) the minimum price which may be paid for a Share shall be 25p (or on the passing of ordinary resolution 6 to be proposed at the Annual General Meeting of the Company to be held on 24 November 2000, 5p);
  - (c) the maximum price (exclusive of expenses) which may be paid for a Share shall be 105% of the average of the middle market quotations (as derived from the Daily Official List of the UK Listing Authority) for the Shares for the five business days immediately preceding the date of purchase; and
  - (d) unless previously varied, revoked or renewed, the authority hereby conferred shall expire at the conclusion of the Annual General Meeting of the Company to be held in 2001, save that the Company may, prior to such expiry, enter into a contract to purchase Shares under such authority which will or might be executed wholly or partly after the expiration of such authority and may make a purchase of Shares pursuant to any such contract.

9. That the Articles of Association of the Company be amended by the deletion of Article 19(E) and the insertion of the following in its place:

“(E) Notwithstanding any other article, the Directors may from time to time determine, either generally or in any particular case, the method by which any share certificate issued by the Company in respect of the Company’s shares, stock, debentures or other securities shall be authenticated or executed by or on behalf of the Company and, in particular:

- (a) the Directors may dispense with the need to affix the common seal, or any official seal, of the Company to such certificate;
- (b) the Directors may determine the manner, and by whom, any such certificate is to be signed, and may dispense with the need for such certificate to be signed or executed in any way;
- (c) the Directors may permit the signature or a facsimile of the signature of any person to be applied to such share certificate by any mechanical or electronic means in place of that person’s actual signature.

And any certificate issued in accordance with the requirements of the Directors shall, as against the Company, be sufficient evidence of the title of the person named in that certificate to the shares comprised in it notwithstanding any rule of law to the contrary.”

10. That the Articles of Association of the Company be amended by re-numbering the existing Article 132 as Article 132(A) and by inserting immediately thereafter the following additional paragraphs (B) and (C):

“(B) The Directors shall establish a capital reserve and carry to the credit of the capital reserve or apply in providing for depreciation or a sinking fund or contingencies all capital appreciation arising on the sale, transposition, payment off or revaluation of any investments or other capital assets of the Company in excess of the book value thereof. Any loss realised on the sale, transposition, repayment or payment off of any investments or other capital assets and any premium or excess over the issue price of any debentures or loan stock payable on the redemption of such debentures or loan stock may be carried to the debit of the capital reserve except in so far as the Directors may, in their discretion, decide to make good the same out of other reserves of the Company. All sums carried to, and standing at the credit of, the capital reserve may be applied for any of the purposes to which such sums standing to the credit of any revenue reserve are applicable: Provided that no part of the capital reserve or any other moneys in the nature of accretions to capital shall in any event be available for distribution as dividend or any other distribution (within the meaning ascribed thereto by section 263(2) of the Companies Act 1985) otherwise than by way of a redemption or purchase of the Company’s own shares in accordance with sections 160 and 162 of the Companies Act 1985.

(C) The Directors may, subject to applicable legislation and practice, determine whether any amount received by the Company (including the dividends or interest received in respect of any shares or other securities purchased *cum* dividend or interest) is to be dealt with as, and whether any sum paid by the Company shall be charged against, income or capital or partly one and partly the other.”

By Order of the Board

BAILLIE GIFFORD & Co  
Managers and Secretaries  
25 October 2000

*Baillie Gifford*

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 is enclosed.
- 2 Only holders of ordinary shares are entitled to attend or be represented at the meeting.
- 3 Shareholders participating in the Baillie Gifford Investment Trust Share Plan and/or the Baillie Gifford Investment Trust ISA/PEP may vote and/or attend the meeting on application to Baillie Gifford Savings Management Limited (see contact details on inside back cover of this report).
- 4 No Director has a contract of service with the Company.

## HOW TO FIND US

The Annual General Meeting of the Company will be held at the offices of Baillie Gifford & Co at 1 Rutland Court, Edinburgh EH3 8EY on Friday, 24 November 2000 at 12.00 noon.

If you have any queries as to how to vote or how to attend the meeting, please call us on 0800 917 2112.

## ANALYSIS OF SHAREHOLDERS

### ANALYSIS OF SHAREHOLDERS AT 31 AUGUST 2000

	Ordinary shares held		Shareholders	
	Number	%	Number	%
Individuals	464,327	3.6	565	28.3
Baillie Gifford Share Plan/PEP/ISA	222,422	1.7	653	32.7
Nominee Companies and Banks	8,989,120	70.5	605	30.3
Insurance Companies	1,262,733	9.9	21	1.1
Other holders	1,811,398	14.3	152	7.6
	<b>12,750,000</b>	<b>100.0</b>	<b>1,996</b>	<b>100.0</b>

- **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 Investment Trust Share Plan (of which details follow on the inside back cover of this report).
- **Sources of Further Information on the Trust** The price of shares is quoted daily in the *Financial Times*, *The Scotsman* and *The Herald*. The share price can also be found on the Baillie Gifford website at [www.bailliegifford.co.uk](http://www.bailliegifford.co.uk), *Trustnet* at [www.trustnet.co.uk](http://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** Baillie Gifford Japan publishes quarterly progress reports. The Annual Report and Accounts are normally issued in October and the AGM is normally held in November.
- **CGT** The cost for capital gains taxation purposes to shareholders who subscribed for ordinary shares (with warrants attached) is apportioned between the ordinary shares and the warrants on the following basis:

Cost of each ordinary share	96.548p
Cost of fraction for warrant	3.452p
	<u>100.000p</u>

The market value of the ordinary shares on 31 March 1982 (for indexation purposes) was 77p.

The market values on 20 November 1991 (first day of dealing of new warrants) were as follows:

Ordinary shares	600p
Warrants	130p

- **Share Register Enquiries** Computershare Services PLC currently 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, investors can check their holding on the Registrar's web site: [www.cshare.co.uk](http://www.cshare.co.uk)

**Baillie Gifford Japan is an investment trust. Investment trusts offer investors the following advantages:**

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

Shares in Baillie Gifford Japan are also available within an ISA or PEP Transfer wrapper or through Baillie Gifford's Investment Trust Share Plan as detailed on the inside back cover of this report. These products can also be used to invest in the five other investment trusts managed by Baillie Gifford:

- Baillie Gifford Shin Nippon PLC
- Mid Wynd International Investment Trust PLC
- Pacific Horizon Investment Trust PLC
- The Monks Investment Trust PLC
- The Scottish Mortgage and Trust PLC.

These accounts have been approved by the Directors of The Baillie Gifford Japan Trust PLC. The information about the ISA, PEP and Share Plan has been approved by Baillie Gifford Savings Management Limited. 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. Baillie Gifford Savings Management Limited is wholly owned by Baillie Gifford & Co. Both are regulated by FRC. Baillie Gifford only provides information about its products and does not provide investment advice. The staff of Baillie Gifford may have positions in investment trusts managed by Baillie Gifford 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 not necessarily a guide to 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.

### **Baillie Gifford's Investment Trust Share Plan**

You can invest from £250 or from £30 per month in any of the six investment trusts managed by Baillie Gifford through the Baillie Gifford Investment Trust Share Plan. The only charges are stamp duty at 0.5%, market maker's spread and a selling charge of £10 plus VAT.

### **Baillie Gifford's Investment Trust ISA**

You can put any of our trusts in a tax efficient wrapper by investing from £2,000 or £250 per month or by transferring an ISA from your existing manager.

### **Baillie Gifford's Investment Trust PEP Transfer**

You can transfer an existing PEP to access different markets through our investment trusts or to change your *investment manager*.

### **Further Information**

Retail Investments Department  
Baillie Gifford Savings Management Limited  
1 Rutland Court  
EDINBURGH EH3 8EY

0800 027 0133  
We may record your call

[its@bailliegifford.co.uk](mailto:its@bailliegifford.co.uk)

Fax: 0131 474 3248

**DIRECTORS**

*Chairman*  
G Malcolm Murray CBE  
  
Richard A Barfield  
A Graham S McCallum CBE  
George Veitch

**MANAGERS, SECRETARIES  
AND REGISTERED OFFICE**

Baillie Gifford & Co  
1 Rutland Court  
Edinburgh EH3 8EY  
Telephone: 0131 222 4000  
Website: [www.bailliegifford.co.uk](http://www.bailliegifford.co.uk)

**REGISTRARS**

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Owen House  
8 Bankhead Crossway North  
Edinburgh EH11 4BR  
Telephone: 0870 702 0010

**BROKERS**

HSBC Investment Bank plc  
Vintners Place  
68 Upper Thames Street  
London EC4V 3BJ

**AUDITORS**

PricewaterhouseCoopers  
Chartered Accountants and  
Registered Auditors  
Erskine House  
PO Box 90  
68-73 Queen Street  
Edinburgh EH2 4NH

Company Registration No. 75954