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ANNUAL REPORT

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# Baring Emerging Europe PLC

*For the year ended*  
30 September 2006

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## DIRECTORS AND OFFICERS

### Directors

Iain Saunders, Chairman  
Steven Bates  
John Cousins  
Josephine Dixon  
Saul Estrin

### Secretary

M. J. Nokes, F.C.A.

### Registered Office

155 Bishopsgate  
London EC2M 3XY

### Company Number

4560726

### Investment Manager

Baring Asset Management Limited  
155 Bishopsgate  
London EC2M 3XY  
Telephone: 020 7628 6000  
Facsimile: 020 7638 7928

### Stockbroker

UBS Warburg  
1 Finsbury Avenue  
London EC2M 2PA

### Auditor

KPMG Audit Plc  
8 Salisbury Square  
London EC4Y 8BB

### Custodian

State Street Bank & Trust Company Limited  
One Canada Square  
London E14 5AF

### Administrator

Northern Trust International Fund  
Administration Services (UK) Limited  
50 Bank Street  
Canary Wharf  
London E14 5NT  
Telephone: 0207 982 2000

### Registrars and Transfer Office

Capita Registrars  
The Registry  
34 Beckenham Road  
Beckenham, Kent BR3 4TU  
Telephone: 0870 162 3100

### Website

[www.bee-plc.com](http://www.bee-plc.com)

## FINANCIAL HIGHLIGHTS

	2006	Restated* 2005
Net asset value per ordinary share ("NAV")	<b>675.07p</b>	586.85p
Earnings per ordinary share	<b>3.00p</b>	2.07p
Dividends per ordinary share	<b>2.70p</b>	1.50p
Share price	<b>605.00p</b>	586.75p
Expense ratio (based on average monthly NAV):		
Excluding Performance Fee	<b>1.38%</b>	1.43%
Including Performance Fee	<b>1.38%</b>	1.80%

\* Restated to reflect the valuation of the portfolio at 30 September 2005 at bid market prices and the removal of the creditor at that date for the annual dividend for 2005 that was paid in February 2006.

## PERFORMANCE

	% change
Net asset value per ordinary share	<b>+15.0</b>
Share price	<b>+3.1</b>
Benchmark <sup>(i)</sup>	<b>+17.4</b>

(i) The benchmark is the FTSE Custom All World Emerging Europe Index (but with Russia weighted at 70% and Turkey weighted at 30% of the actual market weightings).

## DISCOUNT AT 30 SEPTEMBER

	2006	2005
Discount to net asset value per share	<b>11.6%</b>	0.4%

## INVESTMENT OBJECTIVE

The investment objective of the Company is to achieve long-term capital growth, principally through investment in Emerging European securities.

## THE INVESTMENT MANAGER

The Investment Manager is Baring Asset Management Limited which is authorised and regulated by the Financial Services Authority.

## FINANCIAL CALENDAR

<b>Annual General Meeting for 2006</b>	16 January 2007
<b>Announcement of interim results</b>	May
<b>Announcement of final results</b>	November
<b>Interim report posted</b>	May
<b>Annual report posted</b>	December

The Company's share price is published in the *Financial Times*.

## SPECIAL CONSIDERATIONS AND RISK FACTORS

Shareholders should be aware that the value of the Company's Shares and the income from them may fluctuate. In addition, there is no guarantee that the market prices of shares in investment trusts will fully reflect their underlying Net Asset Value.

The risks inherent in investment by the Company in Emerging Europe are of a nature and degree not typically encountered in investing in securities of companies listed on the major securities markets. Such risks are both political and economic and in addition to the normal risks inherent in any equity investment.

Investment in the Company should be regarded as long-term in nature. There can be no guarantee that the Company's investment objectives will be achieved.

## CHAIRMAN'S STATEMENT

### COMPANY PERFORMANCE

The year to 30 September 2006 was another positive year for your Company. Regional markets performed well and your Company's net asset value rose by 15.0%. This compared favourably with the competition, though it was short of the 17.4% increase in the benchmark.

For shareholders this return was reduced to 3.1% because the discount as at 30 September 2006 was 11.6% as compared with 0.4% at the 30 September 2005. The Board has an active discount management policy and it so happens that the former was close to the upper limit and the later close to the lower limit the Board considers to be satisfactory. For the year as a whole the discount averaged 5.5%.

The dividend income from the underlying portfolio rose by over 40% compared to the previous year so that the income available for distribution increased from 2.07p per share in the year to 30 September 2005 to 3.00p per share out of which the Directors are recommending a dividend of 2.70p per share.

### INVESTMENT MANAGER

On 26 April 2006 we announced that Stuart Richards, the Fund's portfolio manager would be leaving Baring Asset Management ("Barings") in October 2006. On 26 September 2006 we announced that Barings had appointed Martin Majdaniuk as Investment Manager within its Emerging European Equities team. Mr Majdaniuk joins from Nordea Investment Management in Copenhagen where he has been a portfolio manager for the last eight years. He will report to Dr Ghadir Abu Leil-Cooper, Head of Emerging Europe Equities at Barings, and will take responsibility for the Company's portfolio from January. In the meantime Dr Ghadir Abu Leil-Cooper has assumed responsibility for the Company's portfolio.

### ADOPTION OF NEW FINANCIAL REPORTING STANDARDS

UK GAAP is converging with International Reporting Standards and from 1 October 2005 the Company has adopted FRS 25 "Financial Instruments: Disclosure and Presentation", FRS 26 "Financial Instrument: Measurement" and FRS 21 "Events after the balance sheet date". The main impacts on the financial statements are firstly that the portfolio is valued at bid market prices whereas in prior periods it was valued at middle-market prices and secondly that the provision for the Company's final dividend is only recognised in the financial statements when it has been approved by shareholders at the Annual General Meeting.

### BENCHMARK REVIEW

The primary objective of the Company as set by the Board is to outperform the competition. It is therefore necessary to ensure that the Company's benchmark remains close to the average asset allocation of competitors' portfolios. A review of the benchmark was undertaken during the year by the Investment Manager and changes made from the end of March 2006. The weighting in Russia was increased to 70% (previously 50%) and in Turkey to 30% (previously 15%) of actual market weightings and a cap was placed on the largest stocks to restrict their weight to 10%. The Board will continue to monitor the appropriateness of the benchmark closely.

## **CHAIRMAN'S STATEMENT**

continued

### **ANNUAL GENERAL MEETING**

The next Annual General Meeting will be held on Tuesday 16 January 2007 at 155 Bishopsgate, London EC2 commencing at 2.30pm. The formal business will be followed by a presentation from the Investment Manager, after which there will be an opportunity for shareholders to raise any specific issues with the Investment Manager or with any member of the Board.

### **OUTLOOK**

Your Board continues to see value in the region and remain enthusiastic by the longer term opportunities as the markets develop.

**Iain Saunders**

Chairman

6 December 2006

## **REPORT OF THE INVESTMENT MANAGER**

for the year ended 30 September 2006

### **INTRODUCTION**

#### **Investment Approach**

At Baring Asset Management, we believe that a sound research process is the starting point of any successful investment approach. Some investment managers like to concentrate their research resources either on analysing companies, or on an assessment of which countries offer the most attractive returns. In our view it is most effective to analyse both companies and countries, with the goal of investing in the most attractive companies in the most attractive countries. Further, we look at both companies and countries in the same way, in order to identify the optimal mix.

Our research focuses on growth at a reasonable price, on sensitivity to currency movements, and to other external factors; on the soundness or otherwise of government policy (in the case of a country), or business plan (in the case of a company); and last but not least, on the level of valuation.

This research gives rise to an assessment of the fundamental drivers of return and to this we add our own judgement as to the level of return we expect from each asset in which we might invest. We also check that the resulting rankings are consistent with the broader thematic developments we expect as a firm. These rankings then allow us to construct a disciplined, concentrated portfolio of our most attractive candidates.

Construction of the portfolio also takes into account the risk side of the equation. Your board has laid down for us certain limits and guidelines on the Company's investments which are designed to control excessive risk. We also pay close attention to the need to run a diversified portfolio, which is at the core of any approach to risk management. We invest in relatively volatile markets, and it is important that your Company is not excessively exposed to any one company, country or sector. You will see the practical effect of this policy in the charts on pages 12 and 13.

#### **REVIEW OF THE PAST YEAR**

During the year under review, the NAV per share of the Company increased by 15.0% from 586.85p (restated) to 675.07p. This compares with a rise of the Company's benchmark of 17.4% in Sterling terms. The benchmark included concentrations of stocks to levels not available to the Company or its peer group and achieved top decile performance.

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## REPORT OF THE INVESTMENT MANAGER

continued

### a) Markets

During the previous reporting period low global interest rates, particularly in the United States, were very supportive of equity markets, especially in Emerging Europe. However, the last twelve months have generally been characterised by a reversal in this trend. Fears that continued US interest rate hikes would drain liquidity from global financial markets as well as lead to a slowdown in global growth rates meant that, as we predicted last year, market volatility was high. This can be seen in the chart of the Company's NAV development over the twelve month period.

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### Central Europe

The Czech Republic was the best performing market in Central Europe. Economic growth continued to exceed market expectations as GDP increased at an annualised rate of 7.1% and 6.2% in the first and second quarters of 2006 respectively. This growth was predominantly driven by net exports and investments but was also boosted by household consumption. It is estimated that at least 1% growth in GDP alone has been generated by the opening of the new Peugeot-Toyota-Citroen car production plant, indicating that foreign direct investment is still a positive driver in the region. The increased growth triggered some inflation concerns but these were partially alleviated by the Central Bank raising interest rates to 2.5%. General Elections in June 2006 led to a hung parliament with both main parties winning 100 seats but being unable to form a government. The political environment, however, had a limited impact on the market. The electricity utility, CEZ, remains the principal investment in the Czech Republic.

The Hungarian market was the worst performing market as the country suffered both economic and political problems. The market had previously ignored the ongoing concerns regarding Hungary's growing twin current account and fiscal deficits but continuing deterioration finally manifested itself in weakness in the Hungarian forint. The Central Bank initially refused to raise interest rates, further stoking the currency volatility, though they were forced to increase them from 6% to 7.75% by the end of the period. The situation was exacerbated by General Elections which were held in April and brought to power a new Socialist-Liberal coalition. The new government quickly announced a much needed fiscal austerity package. However, the changes aimed at reducing the deficit were all based on raising revenues rather than reducing expenditure which led to further market volatility and the expectation that the result would have a negative impact on growth without reducing inflation. The Company benefited from the underweight position relative to the benchmark maintained throughout the period while contribution from stock selection was limited.

## REPORT OF THE INVESTMENT MANAGER

continued

The Polish market produced a positive return but underperformed the region as a whole over the reporting period. Politics took centre stage as the Law & Justice Party, who had won elections in September 2005, were able to form only a fragile minority government. There was a brief period of political stability when a coalition was formed in May with minor populist parties, but this collapsed in September returning Poland to a period of political uncertainty. Despite the political environment, the Polish economy recovered strongly, growing over 5% in the first half of 2006, helped by investment and a pick-up in domestic demand as wages grew and unemployment began to fall while inflation remained low. The positive fundamental picture supported an appreciation in the zloty which would have been greater but for the political situation. Despite the improving fundamentals we were net sellers of Polish stocks and the portfolio benefited from holding an underweight position.

### Russia

The Russian market was the best performing market in the region, driven by the strength in commodity prices which increased domestic liquidity. Economic growth continues at a very rapid pace. Expectations are for GDP growth of 7% this year driven by external demand for oil and gas and other commodities as well as a thriving domestic economy.

The strength in the economy has allowed the balances of both the Central Bank and the Government to strengthen, with foreign exchange reserves at an all time high despite the repayment of all Soviet era debt. Russia continues to have an impressive budget and current account surplus and this has led rating agencies to upgrade Russia's credit rating. Russian debt remains investment grade. Furthermore, some progress has been achieved on the reforms front such as moving to full rouble convertibility. We have also finally seen some progress on the liberalisation of the electricity sector. The Company benefited from having an overweight position in the market.

At the start of this year, the Russian government removed restrictions on investment in the gas giant Gazprom. Gazprom, currently the largest weight in MSCI emerging markets index, has attracted both foreign and local investment to the market and was responsible for some of Russia's strong performance this year.

### Turkey

The Turkish market was very volatile and finished the reporting period slightly down. The market initially performed strongly buoyed by the commencement of European Union accession talks and generally supportive macro developments. The disinflation programme remained on track and growth was robust, driven by foreign investment and domestic consumption. The problem area was the current account deficit which continued to grow swiftly, reaching 8% of GDP. This vulnerability was exposed during the sell-off in emerging markets in May and June with the currency, in particular, coming under severe pressure. The weakness in the lira was intensified by the slow response of the new Central Bank governor. The Central Bank was finally forced to increase interest rates aggressively by 4.25%, this helped stabilise the currency but the weakness in the currency had a negative short-term impact on inflation which has meant the Central Bank's targets for 2006 will be missed.

### b) Portfolio

When we look at how your Company performed, we focus on the two major sources of value added relative to our benchmark: asset allocation, or how countries contributed to return; and stock selection, or which companies contributed, both positively and negatively to return; both relative to the benchmark. For this period asset allocation was positive but stock selection was negative and overall the Company underperformed the benchmark.

## REPORT OF THE INVESTMENT MANAGER

continued

In terms of asset allocation, the overweight position held in Russia throughout the period has been the main source of outperformance with the Company's exposure increasing from 41% at the start of the year to 54% at the close. The underweight positions in both Hungary and Poland were also sources of positive attribution and the Company was a net seller of both markets during the period. On the negative side, the overweight position in Turkey hurt, as did the residual holding in cash.

Despite the positive asset allocation effect, Russian stock selection was the largest detractor from performance. As mentioned in the Chairman's statement, there was a change in our benchmark on the 31 March. This change put a cap on the largest Russian stocks to restrict their weight to no more than 10%. This inflated some stock weightings in the benchmark. As a result of this rebalancing, some of the Company's larger overweight positions became underweight and the Manager opted to minimise portfolio transactions by keeping the holdings roughly where they had been. This had the effect of hurting performance albeit offset by the decision to overweight the country. Finally, in Poland, stock selection was also negative mainly due to the underweight in banks which performed well due to the macro improvement. The Company remains underweight in this sector, as the banks are the most expensive in our region.

### OUTLOOK

This has been the fourth consecutive year of good returns in the markets where your Company invests. It is entirely reasonable to question whether this strong performance will continue, and in this section, we will attempt an answer.

We think of our investment universe as comprising three regions and, while the rationale for investing in each is slightly different, we feel all continue to offer long term potential investment opportunities.

#### a) Central Europe

The investment attraction of the major markets (Poland, Hungary, Czech Republic) has centred on the so called convergence story. This thesis reflects the convergence of the local economies with the EU's, and with membership of the union now fully embedded, we would argue that the first phase of the process is complete.

This first phase took the form of a decline in sovereign risk as these countries became less risky places to invest, allowing interest rates to fall, and economic activity, especially investment, to accelerate. In our view, the second phase is just beginning and will last for some years. The main driver will be continued inward private sector investment coupled with significant official capital flows or subsidies from the European Union. The private flows reflect, *inter alia*, the much lower cost of labour in Central Europe, and the competitive pressures that Western European companies are experiencing to relocate manufacturing to lower cost locations. This continued investment, both publicly and privately funded, will help maintain growth rates in Central Europe which should outstrip those experienced in the wider EU market. Despite a volatile political environment in the region, economies are doing well. While in Hungary the macro situation remains difficult, we believe the Hungarian Government is currently trying to tackle the budget and current account deficits which should bode well for the country in the medium term.

#### b) Russia

The economy in Russia is very strong, principally due to high global oil prices, but also high prices in other resources where the country is a major producer. Unlike in the past the growth triggered by this boom is not being squandered or siphoned off-shore, but reinvested both in the resources sector and, importantly, into the wider economy. As a result, abundant domestic liquidity is driving domestic consumption. Meanwhile the fiscal surplus being generated from the commodity boom is being kept in a reserve fund which should provide

## REPORT OF THE INVESTMENT MANAGER

continued

a cushion to the economy if needed. There will continue to be, to Western eyes, political setbacks, corporate scandals and so on, but the institutional framework in Russia is more robust than is generally perceived. This is vital to ensure the continued decline in the level of flight capital and has broadened and deepened the capital markets. The investment potential in Russia will take decades to unlock fully and despite its recent outperformance, the market remains undervalued by global standards. Furthermore, the investment opportunity continues to widen with a barrage of public offerings currently coming to the market in all sectors.

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### Turkey – Concerns over inflation and the currency are overdone

The Turkish market was the weakest in the region recently. We believe the fundamental story of improving macro-economic indicators and macro-economic management is still valid, which should reduce the investment risk in the medium to long term. Despite the volatility seen this year, the economy is much less susceptible to the boom bust cycles. A combination of the EU accession promise and better macro management has led to a deepening of the economy. Turkey remains on a growth path with the prospects of interest rates being reduced as inflation is again brought back under control. Whether or not Turkey ends up joining the EU, it is set on a convergence path which we believe offers excellent prospects for investors.

### Company Weighting versus Benchmark on Country Level at 30 September 2006

	Company	Customised Benchmark
Czech Republic	8.5	9.9
Hungary	11.9	14.0
Poland	11.3	19.3
Russia	54.3	50.7
Turkey	9.3	6.0
Kazakhstan	2.3	–
Cash	2.4	0.1
	100.0	100.0

Source: Barings, FTSE

**REPORT OF THE INVESTMENT MANAGER**

continued

**PORTFOLIO REVIEW**

The Company's twenty largest holdings, which represented 83.3% of the portfolio at 30 September 2006, are set out in the following table:

**Twenty Largest Holdings at 30 September 2006**

Rank	Holding	Country	Market Value £000	% of Portfolio
1	Lukoil Holdings	Russia	24,759	8.7
2	CEZ	Czech Republic	23,507	8.2
3	Gazprom	Russia	23,225	8.1
4	Sberbank	Russia	21,726	7.6
5	Norilsk Nickel	Russia	18,069	6.3
6	Unified Energy Systems	Russia	15,861	5.6
7	MOL	Hungary	15,693	5.5
8	OTP Bank	Hungary	14,847	5.2
9	Surgutneftegaz	Russia	12,977	4.5
10	Polski Koncern Naftowy	Poland	10,425	3.7
11	Bank Pekao	Poland	9,222	3.2
12	Mobile Telesystems	Russia	6,906	2.4
13	Kazakhmys	Kazakhstan	6,684	2.3
14	Vimpel Comm	Russia	6,499	2.3
15	KGHM Polska	Poland	5,687	2.0
16	Polyus Gold	Russia	5,248	1.8
17	Akbank	Turkey	5,148	1.8
18	Richter Gedeon	Hungary	4,203	1.5
19	IS Bank	Turkey	3,675	1.3
20	Sistema	Russia	3,641	1.3
			238,002	83.3
<b>Other holdings</b>			<b>47,413</b>	<b>16.7</b>
<b>Total investments</b>			<b>285,415</b>	<b>100.0</b>

**REPORT OF THE INVESTMENT MANAGER**

continued

**CLASSIFICATION OF ASSETS**

The Sector Split of the Company's Portfolio as per MSCI Sector at 30 September 2006 was:

**Percentage Classification of Assets Based on Valuation**

	Russia	Hungary	Poland	Czech Republic	Turkey	Other Countries	Net Current Assets/(Liabilities)	Total 2006	Total 2005
Consumer Discretionary	0.1	—	0.8	0.5	1.7	—	—	3.1	2.7
Consumer Staples	0.4	—	0.2	—	—	—	—	0.6	0.5
Energy	27.8	5.4	4.0	—	1.0	—	—	38.2	39.9
Financials	7.5	5.1	3.1	—	5.5	—	—	21.2	24.7
Healthcare	—	1.4	—	—	—	—	—	1.4	1.9
Industrials	—	—	—	—	1.0	—	—	1.0	3.0
Information Technology	1.2	—	—	—	—	—	—	1.2	0.8
Materials	8.6	—	2.0	—	—	2.3	—	12.9	3.9
Telecommunication									
Services	5.8	—	1.2	—	0.1	—	—	7.1	15.2
Utilities	2.9	—	—	8.0	—	—	—	10.9	8.3
<b>Total equity investment</b>	<b>54.3</b>	<b>11.9</b>	<b>11.3</b>	<b>8.5</b>	<b>9.3</b>	<b>2.3</b>	<b>—</b>	<b>97.6</b>	<b>100.2</b>
<b>Net current assets/(liabilities)</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>2.4</b>	<b>2.4</b>	<b>(0.2)</b>
<b>Total 2006</b>	<b>54.3</b>	<b>11.9</b>	<b>11.3</b>	<b>8.5</b>	<b>9.3</b>	<b>2.3</b>	<b>2.4</b>	<b>100.0</b>	<b>—</b>
<b>Total 2005</b>	<b>41.7</b>	<b>19.8</b>	<b>18.6</b>	<b>9.3</b>	<b>10.8</b>	<b>—</b>	<b>(0.2)</b>	<b>—</b>	<b>100.0</b>

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**REPORT OF THE INVESTMENT MANAGER**

continued

**PERFORMANCE**

The year's performance of the Company against the benchmark index is shown in the following graph:

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**Baring Asset Management Limited**

6 December 2006

**REPORT OF THE DIRECTORS  
INCORPORATING THE BUSINESS REVIEW**

for the year ended 30 September 2006

The Directors submit to the shareholders their business review, report and the audited financial statements of the Company for the year ended 30 September 2006.

**1. BUSINESS REVIEW**

**Business and Tax Status**

The Company carries on business as an investment trust and as such it has received specific approval from the Inland Revenue under the provisions contained in Section 842 of the Income and Corporation Taxes Act 1988. Approval for the year ended 30 September 2005 is subject to there being no subsequent enquiry under Corporate Self Assessment. In the opinion of the Directors the Company has subsequently directed its affairs so as to enable it to continue to seek such approval.

The Company is an investment company as defined in Section 266 of the Companies Act 1985.

The Company is managed by external parties in respect of investment management, custodial services and the day-to-day accounting and company secretarial requirements. Investment management services are provided by Baring Asset Management Limited ("Barings") and details of the agreement with Barings are given in note 3 to the accounts. The Custodian is State Street Bank & Trust Company Limited. Secretarial services are provided by Northern Trust International Fund Administration Services (UK) Limited. The Company has no employees. The Directors are all non-executive.

**Investment Objective and Benchmark**

The Company carries on business as an investment trust. The investment objective is to achieve long-term capital growth, principally through investment in securities listed on or traded on an Emerging European securities market or in securities listed or traded elsewhere, the majority of whose revenues and/or profits are, or are expected to be, derived from activities in Emerging Europe.

The primary objective of the Company as set by the Board is to outperform the competition. The Company's benchmark was a customised benchmark based on the FTSE Greater Europe with Turkey Index, and is periodically reviewed to ensure that it remains close to the average asset allocation of competitors' portfolios. Following the last review it was agreed to amend the benchmark from 1 April 2006 to the FTSE Custom All World Emerging Europe Index but with Russia weighted at 70% and Turkey weighted at 30% of actual market weightings and the weighting of individual stocks capped at 10% of the benchmark. Previously Russia had been weighted at 50% and Turkey at 15% of actual market weightings with no cap on individual stocks. These changes reflect the developments in the markets of emerging Europe since the original benchmark was introduced.

**Investment Policy**

The Company mainly invests in a diversified portfolio of Emerging European equity securities, concentrating on countries and shares with the most attractive prospects. The Company currently invests in Russia, the Czech Republic, Hungary, Poland, Turkey and Kazakhstan. The Company may from time to time invest in unquoted securities, but the amount of such investment is not expected to be material. At present the Company has less than 0.1% of its gross assets invested in unquoted securities. The Company does not invest more than 15% of its gross assets in other UK listed investment companies (including investment trusts). At present the Company does not hold any investments in UK listed investment companies.

**Dividends**

The Board does not seek to target any particular level of dividend, and intends rather to distribute by way of dividend most of the net earnings available for this purpose. The Board recommends an annual dividend of 2.7p per share compared with 1.5p for the previous period. Subject to the approval of the Annual General Meeting, the recommended annual dividend will be paid on 7 February 2007 to members on the register at the close of business on 12 January 2007. The shares will be marked ex-dividend on 10 January 2007.

## REPORT OF THE DIRECTORS

continued

### Gearing

The Board believes that the markets in which the Company invests are not as yet sufficiently developed to warrant long-term gearing. Since November 2003, the Company has had a US\$10 million unsecured loan and overdraft facility with State Street Bank and Trust Company which is principally used to cover timing differences on portfolio transactions.

### Discount

The Directors have adopted a firm policy with regard to the market rating of the Company's shares. At all times the Board will seek to limit the discount to NAV at which the Company's shares trade to a level significantly lower than the 12% trigger level referred to in the paragraph below, using as necessary the Company's share repurchase authority. No shares were repurchased during the year ended 30 September 2006. Any shares repurchased may be held in treasury and may be issued at a later date at or above net asset value.

If the average closing mid-market price at which the Company's shares trade in the market in the period of ninety days prior to the publication of the Company's preliminary results each year represents a discount to NAV which exceeds 12% the Company will offer to repurchase, by way of tender, available to all shareholders, up to 15% of the outstanding issued share capital at 95% of NAV (after taking account of any expenses including the costs of selling investments in order to fund the repurchase).

### Performance

At each Board meeting, the Directors consider a number of performance measures to assess the Company's success in achieving its objectives.

The key performance indicators ("KPIs") used to measure the progress and performance of the Company over time are as follows:

- **Performance against the peer group**  
The Board monitors performance relative to a broad range of competitor funds, as defined by the S&P Global Equity Europe Emerging markets universe. In the year ended 30 September 2006 the Company was ranked 35th out of 130 funds in this universe.
- **Performance against the benchmark index**  
A chart of NAV performance versus benchmark since inception (total return) is set out in the Directors' Remuneration Report on page 26.
- **Discount to net asset value ("NAV")**  
In the year ended 30 September 2006 the shares traded at an average discount of 5.5%.
- **Total expense ratio ("TER")**  
The TER is an expression of the Company's management fees and other operating expenses as a percentage of average net assets over the year. The TER for the year ended 30 September 2006 was 1.38% excluding performance fee (2005: 1.43%). No performance fee was payable in respect of the year ended 30 September 2006. The TER including the performance fee for the year ended 30 September 2005 was 1.80%. The Board reviews each year an analysis of the Company's TER and a comparison with its peers.

### Principal Risks

The key risks to the Company fall broadly under the following categories:

- **Investment and Strategy:** The Board regularly reviews the investment mandate and long-term investment strategy in relation to the market and economic conditions. The Board also regularly monitors the Company's investment performance against the benchmark and the peer group and its compliance with the investment guidelines.

## REPORT OF THE DIRECTORS

continued

- **Accounting, Legal and Regulatory:** In order to qualify as an investment trust, the Company must comply with Section 842 of the Income and Corporation Taxes Act 1988 ("Section 842"). A breach of Section 842 could lead to the Company being subject to capital gains tax on gains within the Company's portfolio. Section 842 qualification criteria are continually monitored by Baring Asset Management Limited and the results reported to the Board at its regular meetings. The Company must also comply with The Companies Act 1985 and the UKLA Listing Rules. The Board relies on the services of the administrator, Northern Trust International Fund Administration Services (UK) Limited and its professional advisers to ensure compliance with the Companies Act 1985 and the UKLA Listing Rules.
- **Financial:** The financial risks faced by the Company are disclosed in note 20 on page 42.

### Financial Statements

In the year under review the Company has had to comply with a number of new Financial reporting Standards which were introduced as part of the UK convergence programme with International Financial Reporting Standards. The main changes to the Company's financial statements resulting from these new standards are (i) that investments are now valued at bid prices rather than mid and (ii) dividends declared after the period end are no longer treated as a liability. These changes are explained in more detail in note 1 on pages 34 and 35.

## 2. DIRECTORS

The present Directors are listed below and on page 2. They are all non-executive and have all served throughout the year.

**Iain Saunders** (59) spent 30 years with the Fleming group until his retirement in 2001, latterly as deputy chairman of Robert Fleming Asset Management. He is at present a director of JPMorgan Fleming Indian Investment Trust PLC and the Czech & Slovak Investment Corporation. He was appointed Chairman of Baring Emerging Europe PLC on 11 October 2002 and had been a director of the predecessor company, The Baring Emerging Europe Trust PLC, since 2001.

**Steven Bates** (49) spent 18 years with the Fleming group until 2002, latterly as co-head of emerging markets of JPMorgan Fleming Asset Management. He has extensive experience in both emerging and developed markets. He is a director of Zephyr Management UK Limited which is a specialist asset management business and is also on the board of a number of financial companies involved in emerging markets. He was appointed a director of Baring Emerging Europe PLC on 27 January 2003.

**John Cousins** (66) was formerly chief executive of BZW Puget Mahé in Paris and managing director of BZW Equities in London. Prior to that, he held various posts with Kleinwort Benson and has over 30 years of experience in international equity investment. He is a former chairman of the International Equity Rules and Compliance Committee of the London Stock Exchange. He was appointed a director of Baring Emerging Europe PLC on 11 October 2002 and had been a director of The Baring Emerging Europe Trust PLC since 1994.

**Josephine Dixon** (47) is a Director of Finsbury Worldwide Pharmaceutical Trust PLC, and is a Chartered Accountant who has previously held a number of senior executive positions, including that of finance director in a publicly quoted company. She is also a member of Durham University Business School Advisory Board. She was appointed a Director of Baring Emerging Europe PLC on 5 July 2004.

**Saul Estrin** (54) is a Professor of Management at the London School of Economics. He was formerly a Professor at the London Business School and Research Director of the Centre for New and Emerging Markets, which analyses the prospects for private sector development and business opportunities in emerging markets. He has written numerous books and articles on emerging economies. He was appointed a Director of Baring Emerging Europe PLC on 5 July 2004.

## REPORT OF THE DIRECTORS

continued

In accordance with the Articles of Association Iain Saunders and John Cousins retire by rotation and being eligible, offer themselves for re-election.

The Directors' interests in the Company's shares, as shown in the register kept pursuant to Section 325 of the Companies Act 1985, are stated below:

	1 December 2006	30 September 2006	30 September 2005
<b>Beneficial:</b>			
Iain Saunders	60,000	60,000	60,000
Steven Bates	3,000	3,000	–
John Cousins	–	–	–
Josephine Dixon	2,325	2,325	–
Saul Estrin	1,000	1,000	–

There were no contracts or arrangements subsisting during or at the end of the financial year in which any Director is or was materially interested. No Director held a shareholding in any of the investments in the Company's portfolio during the year ended 30 September 2006.

### 3. SUBSTANTIAL SHAREHOLDINGS

At 1 December 2006, the Company had received notification of the following disclosable interests in the ordinary share capital of the Company:

Sarasin Investment Funds - Emerging SAR	2,913,880 shares	6.57%
Legal & General Group plc	1,406,000 shares	3.17%

### 4. CORPORATE GOVERNANCE

#### Introduction

The Board is accountable to the Company's shareholders for the governance of the Company's affairs and this statement describes how the principles of the Combined Code on Corporate Governance ("the Code") issued by the Financial Reporting Council in July 2003 have been applied to the affairs of the Company. In applying the principles of the Code, the directors have also taken account of the Code of Corporate Governance published by the Association of Investment Companies ("the AIC Code"), which has established a framework of best practice specifically for the Boards of investment trust companies. There is some overlap in the principles laid down by the two Codes and there are some areas where the AIC Code is more flexible for investment trust companies.

#### Applications of the Code's Principles

The Board is committed to high standards of corporate governance and seeks to observe the principles and supporting principles identified in the Code and, where appropriate, the principles identified in the AIC Code. It should be noted that, as an investment trust, most of the Company's day-to-day responsibilities are delegated to third parties and the Directors are all non-executive. Thus not all the provisions of the Code are directly applicable to the Company.

#### The Board

The Board currently consists of five non-executive Directors and is chaired by Iain Saunders. All the Directors are considered by the Board to be independent of the Investment Manager. Their biographies are set out on

## REPORT OF THE DIRECTORS

continued

page 17. Collectively the Board has the requisite range of business and financial experience which enables it to provide clear and effective leadership and proper stewardship of the Company.

The number of meetings of the Board, and the Audit Committee held during the financial year and the attendance of individual Directors are shown below:

	Board	Audit
<b>Number of meetings in the year</b>	4	2
Iain Saunders	4	2
Steven Bates	4	2
John Cousins	4	2
Josephine Dixon	4	2
Saul Estrin	4	2
Prince Abbas Hilmi (retired as a Director on 26 January 2006)	1	–

All of the Directors attended the Annual General Meeting held in January 2006.

The Board deals with the Company's affairs, including the consideration of overall strategy, the setting and monitoring of investment policy and the review of investment performance. The Investment Manager takes decisions as to asset allocation and the purchase and sale of individual investments. The Board papers circulated before each meeting contain full information on the financial condition of the Company. Key representatives of the Investment Manager attend most of the Board meetings, enabling Directors to probe further or seek clarification on matters of concern.

Matters specifically reserved for discussion by the full Board have been defined and a procedure adopted for the Directors to take independent professional advice if necessary at the Company's expense.

The Chairman of the Company is a non-executive Director. A senior non-executive Director has not been identified as the Board is comprised entirely of non-executive Directors.

In accordance with the Articles of Association new Directors stand for election at the first Annual General Meeting following their appointment. The Articles require that one third of the Directors retire by rotation each year and seek re-election at the Annual General Meeting. In addition, all Directors are required to submit themselves for re-election at least every three years and will seek annual re-election if they have already served for more than nine years or are aged over 70.

### Performance Evaluation/Re-Election of Directors

An appraisal process has been established in order to review the effectiveness of the Board, the Committees and individual directors. This process involves the consideration by the Chairman and the Board of responses from individual directors to a questionnaire which is completed on an annual basis. In addition the other directors meet collectively once a year to evaluate the performance of the Chairman. As a result of this evaluation the Nomination Committee recommends the re-election of Iain Saunders and John Cousins who retire by rotation and offer themselves for re-election at the Annual General Meeting. John Cousins is required to seek annual re-election to the Board as he has served for more than nine years when his service on the board of The Baring Emerging Europe Trust PLC (the predecessor company) is included. Mr Cousins continues to make significant contributions to the Board's deliberations and the Nomination Committee is satisfied that his independence is not affected by his length of service.

The performance of the Company is considered in detail at each Board meeting.

## REPORT OF THE DIRECTORS

continued

### **Board Committees**

The Board believes that the interests of shareholders in an investment trust company are best served by limiting its size such that all Directors are able to participate fully in all the activities of the Board. It is for this reason that the membership of the Audit and Nomination Committees is the same as that for the Board as a whole.

#### *Audit Committee*

Miss Dixon took over as Chairman of the committee from Mr Cousins on 26 January 2006. The committee meets at least twice a year and is responsible for reviewing the annual and interim reports, the nature and scope of the external audit and the findings therefrom, and the terms of appointment of the Auditors, including their remuneration and the provision of any non-audit services. Non audit services provided by the Auditors mainly comprised work on the Company's taxation affairs. The committee has considered the independence of the Auditors and the objectivity of the audit process and is satisfied that KPMG Audit Plc has fulfilled its obligations to shareholders. It also regularly reviews the terms of the different service providers to the Company including contracts with the Investment Manager, the Company Secretary and the Custodian. The audit committee meets representatives of the Investment Manager and its Compliance Officer who report as to the proper conduct of business in accordance with the regulatory environment in which both the Company and the Investment Manager operate. The Company's external Auditors also attend this committee at its request and report on their findings in relation to the Company's statutory audit.

As the Company has no employees section C.3.4 of the Code, which deals with arrangements for staff to raise concerns in confidence about possible improprieties in respect of financial reporting or other matters, is not directly relevant to it. The Audit Committee has however, confirmed with the Investment Manager and the administrator that they do have "whistle blowing" policies in place for their staff.

The Chairman of the Audit Committee will be present at the AGM to deal with questions relating to the financial statements.

#### *Nomination Committee*

The Committee, which meets at least annually, reviews the Board's size and structure and is responsible for Board succession planning.

### **Remuneration**

The Board as a whole considers Directors' remuneration and therefore has not appointed a separate remuneration committee. As the Company is an investment trust and all Directors are non-executive, the Company is not required to comply with the Code in respect of executive Directors' remuneration. Directors' fees are detailed in the Directors' Remuneration Report on page 25.

### **Internal Controls**

The Board has established a process for identifying, evaluating and managing significant risks faced by the Company. The process is subject to regular review by the Board and accords with "Internal Control: Guidance for Directors on the Combined Code" ("The Turnbull guidance") which was issued in September 1999 and revised in September 2005.

The Directors are responsible for the Company's system of internal control which is designed to safeguard shareholders' investment and the Company's assets. These systems of internal control are designed to provide reasonable but not absolute assurance against material misstatement or loss.

The Turnbull guidance recommends a risk-based approach to the assessment of internal controls. The Board has completed a risk map for the Company and established procedures for the monitoring and review of the risks identified. The Board as a whole is primarily responsible for the monitoring and review of risks associated with investment matters and the audit committee is primarily responsible for other risks.

## REPORT OF THE DIRECTORS

continued

As the Board has contractually delegated to external parties the investment management, the custodial services and the day-to-day accounting and company secretarial requirements, the Company relies significantly upon the internal controls operated by those companies. Therefore the Directors have concluded that the Company should not establish its own internal audit function. The Board continues to monitor its system of internal control in order to ensure it operates as intended and the directors review annually whether an internal audit function is required. Investment management services are provided by Baring Asset Management Limited ("Barings") and details of the agreement with Barings are given in note 3 to the accounts. The Custodian is State Street Bank & Trust Company Limited. Secretarial services are provided by Northern Trust International Fund Administration Services (UK) Limited.

The risk map has been considered at all regular meetings of the Board and audit committee. As part of the risk review process, regular reports are received from the Investment Manager on all investment matters including compliance with the investment mandate, the performance of the portfolio compared with the benchmark and compliance with investment trust status requirements.

The Board also receives and reviews annual reports from the Investment Manager and the Custodian on their internal controls and their operation. These reports are designed to provide details of the internal control procedures operated by the relevant entity and include a report by an independent reporting accountant.

The Board confirms that appropriate procedures to review the effectiveness of the Company's system of internal control have been in place which cover all controls including financial, operational and compliance controls and risk management. An assessment of internal control, which includes a review of the Company's risk map, an assessment of the quality of reports on internal control from the service providers and the effectiveness of the Company's reporting process, is carried out on an annual basis.

### **Accountability and Audit**

Set out on page 27 is a statement by the Directors of their responsibilities in respect of the accounts. The Directors believe that it is appropriate to continue to adopt the going concern basis in preparing the accounts, as the assets of the Company consist mainly of securities which are readily realisable.

As noted earlier, an audit committee has been established consisting of independent Directors.

The Board as a whole regularly reviews the terms of the management and secretarial contracts.

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's Auditors are unaware; and each Director has taken all the steps that they ought to have taken as Directors to make themselves aware of any relevant audit information and to establish that the Company's Auditors are aware of that information.

The Directors were covered by director's and officers insurance that was in place during the financial year and at the date of this report.

### **Relations with Shareholders**

The Board regularly reviews the Investment Manager's contacts with the Company's shareholders and monitors its shareholder profile. The Board supplements this with some direct contact with shareholders and is available to speak with any shareholder who wishes to do so. The Board supports the principle that the Annual General Meeting be used to communicate with private investors. The full Board attends the Annual General Meeting and the Chairman of the Board chairs the meeting. Details of the proxy votes received in respect of each resolution are made available to shareholders at the meeting. The Investment Manager attends to give a presentation to the meeting. A quarterly newsletter is produced by the Investment Manager and is available to shareholders.

## REPORT OF THE DIRECTORS

continued

If a shareholder would like to contact the Board directly, he or she should write to the Chairman at 155 Bishopsgate, London EC2M 3XY and mark their letter private and confidential.

### **Evaluation of Performance of Investment Manager**

The investment performance is reviewed at each regular Board meeting at which representatives of the Investment Manager are required to provide answers to any questions raised by the Board. The Board has instigated an annual formal review of the Investment Manager which includes consideration of:

- performance compared with benchmark and peer group;
- investment resources dedicated to the Company;
- investment management fee arrangements and notice period compared with the peer group; and
- marketing effort and resources provided to the Company.

The Board believes that Baring Asset Management Limited has served the Company well both in terms of investment performance and general support and will continue its appointment.

### **Statement of Compliance**

The Board considers that it has complied with all the material provisions set out in Section 1 of the Code throughout the year. It did not, however, comply with the following provisions as explained above:

- due to the small size of the Board and nature of the business a separate remuneration committee has not been established;
- a senior non-executive Director has not been identified; and
- the Chairman is a member of the Audit Committee.

### **5. CREDITOR PAYMENT POLICY**

It is the Company's payment policy to obtain the best possible terms for all business and therefore there is no consistent policy as to the terms used. In general, the Company agrees with its suppliers the terms on which business will take place and it is its policy to abide by the terms. As an investment trust, the Company does not transact business of a trading nature. There were no trade creditors at 30 September 2006.

### **6. SOCIALLY RESPONSIBLE INVESTMENT**

The Board has delegated the investment management function to Baring Asset Management Limited. The Investment Manager's primary objective is to produce superior financial returns to investors. It believes that over the long term sound social, environmental and ethical policies make good business sense and takes these issues into account when, in its view, they have a material impact on either the investment risk or the expected return from an investment.

### **7. EXERCISE OF VOTING POWERS**

The Board has delegated authority to the Investment Manager to vote the shares held by the Company in accordance with current best practice. Wherever practical the Investment Manager does vote the shares but in the markets where the Company invests this is not always feasible. The Investment Manager may refer to the Board on any matters of a contentious nature.

### **8. AUTHORITY TO ALLOT SHARES**

Under Resolution 7 of the Annual General Meeting, the Directors seek a general power from shareholders to allot new securities up to an aggregate par value of £216,299 representing approximately 5% of the issued share capital of the Company as at the date of this document excluding shares held in treasury. Such authority, if granted, will expire at the conclusion of the next Annual General Meeting.

## REPORT OF THE DIRECTORS

continued

Resolution 8 of the AGM will, if passed, empower the Directors to make allotments of shares (including sales of shares held in treasury) for cash on a non pre-emptive basis up to an aggregate of (i) 5% of the issued ordinary share capital of the Company less the aggregate nominal value of the shares held in treasury as at the date of this document and (ii) the aggregate nominal value of shares held in treasury as at that date.

These Resolutions will provide the Directors with flexibility to act in the best interests of shareholders. Under the requirements of the UK Listing Authority, unless authorised by shareholders, shares may not be issued for cash at a price below the net asset value per share unless they are first offered pro rata to existing holders of shares of that class.

### 9. PURCHASE BY THE COMPANY OF ITS OWN SHARES AND TREASURY SHARES

At the Annual General Meeting held on 26 January 2006 a special resolution was passed giving the Directors authority until the conclusion of the earlier of the 2007 Annual General Meeting, and 23 July 2007, to make market purchases of the Company's own issued ordinary shares up to a maximum of 6,484,659 ordinary shares. During the year ended 30 September 2006 no market purchases were made.

The Board proposes that the Company should be given renewed authority to purchase ordinary shares in the market either for cancellation or to be held, sold, transferred or otherwise dealt with as treasury shares in accordance with the Companies Act. Resolution 9 of the Annual General Meeting, which is a special resolution, is being proposed for this purpose.

The Board remains committed to exploring methods by which shareholder value can be enhanced. The purchase and cancellation or holding in treasury by the Company of its shares at a cost below the net asset value of those shares enhances the net asset value of the remaining shares. This additional demand for shares may reduce the discount at which the shares trade.

It is proposed that the Company be authorised to purchase on the London Stock Exchange up to 6,484,659 ordinary shares (being 14.99% of the Company's issued share capital as at the date of this document excluding shares held in treasury). Any such purchases will be completed by the delivery to the Company of shares which will then be cancelled immediately or held, sold, transferred or otherwise dealt with as treasury shares in accordance with the Companies Act.

Under London Stock Exchange rules, the maximum price to be paid on any exercise of the authority must not exceed 105% of the average of the middle market quotations for a share for the five business days immediately preceding the date of purchase.

Purchases of shares will be made within guidelines set from time to time by the Board, and will only be made in the market at prices below the prevailing net asset value attributable to a share and, in any event, the minimum price paid may not be below £0.10 per share.

No shares will be purchased by the Company during prohibited periods imposed by the UK Listing Authority unless dispensation is first obtained. These are currently (i) the period of two months immediately preceding the preliminary announcement of the Company's annual results (or from the year-end to the date of the announcement, if less than two months) and (ii) the period of one month immediately preceding the publication of the Company's half-yearly report (or from the half-year date to the date of publication, if less than one month).

Any exercise by the Company of the authority to purchase shares will occur only when market conditions are appropriate.

The authority to purchase shares will last until the Annual General Meeting of the Company in 2008, or 15 July 2008, whichever is the earlier. The authority may be renewed by shareholders at an Extraordinary General Meeting.

## REPORT OF THE DIRECTORS

continued

Purchases will be funded either by using available cash resources, debt or by selling investments.

### Effect on Shareholders

The effect of the implementation of this proposal will be to enhance the net asset value of the remaining shares, as shares will only be acquired in the market for less than their underlying net asset value.

### 10. INVESTMENT POLICY

Following the publication of the Investment Entities (Listing Rules and Conduct of Business) Instrument 2003, the Board has announced that the investment policy of the Company is not to invest more than 15% of its gross assets in other UK listed investment companies (including listed investment trusts).

### 11. AUDITORS

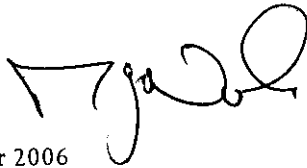
The Company's Auditors, KPMG Audit Plc, have indicated their willingness to continue in office. A resolution for their re-appointment and remuneration will be proposed at the Annual General Meeting.

By order of the Board

M. J. Nokes

Secretary

6 December 2006



## DIRECTORS' REMUNERATION REPORT

for the year ended 30 September 2006

This report is presented in accordance with Schedule 7a of the Companies Act 1985. As the Board of Directors is comprised solely of non-executive Directors, it is exempt under the Listing Rules from appointing a Remuneration Committee. The determination of the level of fees paid to Directors, which are reviewed on a periodic basis, is dealt with by the whole Board.

The Company's Articles of Association limits the aggregate fees payable to the Board of Directors to a total of £175,000. Subject to this overall limit, it is the Company's policy to determine the level of Directors' fees having regard to fees payable to non-executive Directors in the industry generally, the role that individual Directors fulfil, and the time committed to the Company's affairs.

No Director has a service contract with the Company.

### Directors' Fees (Audited)

The information in this section has been subject to audit.

The Chairman receives a fee of £25,000 per annum, the Chairman of the Audit Committee receives a fee of £22,500 per annum and other Directors £20,000 per annum. The fees paid to Directors for the year are set out in the following table:

	2006 £000	2005 £000
Iain Saunders	25	25
Steven Bates	20	20
John Cousins (retired as Chairman of Audit Committee on 26 January 2006)	21	22
Josephine Dixon (appointed as Chairman of Audit Committee on 26 January 2006)	22	20
Saul Estrin	20	20
Prince Abbas Hilmi (retired as a Director on 26 January 2006)	6	20
<b>Total</b>	<b>114</b>	<b>127</b>

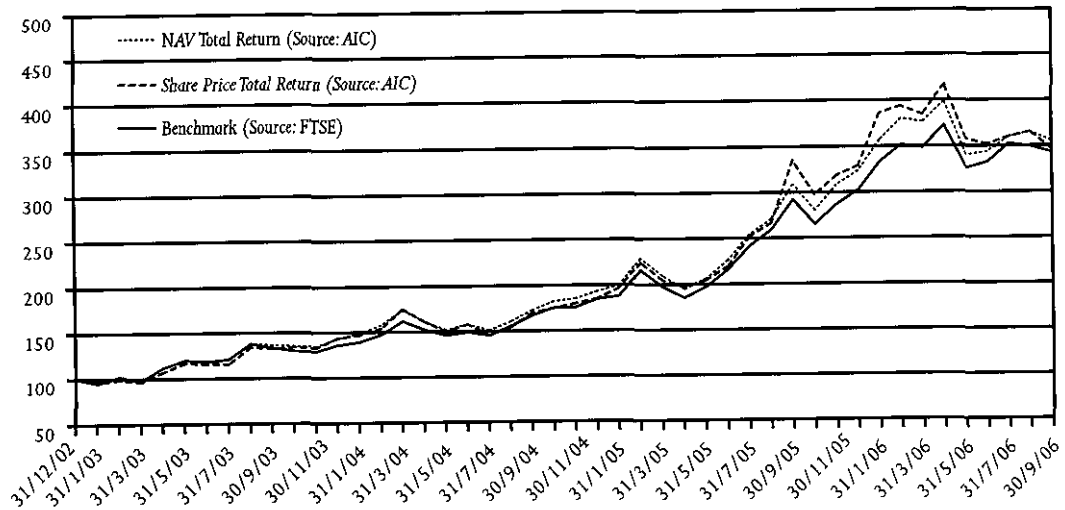
The Company does not provide pension benefits, share options or long-term incentive schemes for Directors.

## DIRECTORS' REMUNERATION REPORT

continued

The performance of the Company is measured against a benchmark which is a customised benchmark based on the FTSE Custom All World Emerging Europe Index. The following graph compares the share price and net asset value performance against the benchmark:

**Performance Versus Benchmark Since Inception**



A resolution for the approval of the Directors' Remuneration Report for the year ended 30 September 2006 will be proposed at the Annual General Meeting.

By order of the Board

M. J. Nokes  
Secretary

6 December 2006

## **STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ANNUAL REPORT AND THE FINANCIAL STATEMENTS**

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

The financial statements are required by law to give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing these financial statements, the Directors are required to:

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

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

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that comply with that law and those regulations. They are also responsible for ensuring that the Annual Report includes information required by the Listing Rules of The Financial Services Authority.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

## **INDEPENDENT AUDITORS' REPORT**

to the members of Baring Emerging Europe PLC

We have audited the financial statements of Baring Emerging Europe PLC for the year ended 30 September 2006 which comprise the Income Statement, the Balance Sheet, the Cash Flow Statement, the Reconciliation of Movement in Shareholders' Funds and the related notes. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an Auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

### **Respective Responsibilities of Directors and Auditors**

The Directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the financial statements in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities on page 27.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and other transactions is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the 2003 FRC Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Company's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

### **Basis of Audit Opinion**

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

## INDEPENDENT AUDITORS' REPORT

continued

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

### Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of the Company's affairs as at 30 September 2006 and of its profit for the year then ended;
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

*KPMG Audit Plc*

**KPMG Audit Plc**

Chartered Accountants and Registered Auditor

London

6 December 2006

## INCOME STATEMENT

(incorporating the Revenue Account\*) for the year ended 30 September 2006

	Notes	Year ended 30 September 2006			Year ended 30 September 2005		
		Revenue £000	Capital £000	Total £000	Revenue £000	Capital £000	Total £000
Gains on investments	9	–	37,493	37,493	–	110,690	110,690
Gains/(losses) on foreign exchange	10	–	–	–	–	169	169
Income	2	5,838	–	5,838	4,102	–	4,102
Investment management fee	3	(2,661)	21	(2,640)	(1,593)	(678)	(2,271)
Other expenses	4	(1,142)	–	(1,142)	(1,016)	–	(1,016)
<b>Net return before interest payable and taxation</b>		2,035	37,514	39,549	1,493	110,181	111,674
Interest payable	5	(5)	–	(5)	(23)	–	(23)
<b>Return on ordinary activities before taxation</b>		2,030	37,514	39,544	1,470	110,181	111,651
Taxation	6	(731)	–	(731)	(572)	–	(572)
<b>Return attributable to ordinary shareholders</b>		1,299	37,514	38,813	898	110,181	111,079
		Revenue	Capital	Total	Revenue	Capital	Total
<b>Return per ordinary share</b>	8	3.00p	86.45p	89.45p	2.07p	253.90p	255.97p

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

†Refer to note 1a for an explanation of the restatement of the 2005 balances.

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

The annexed notes on pages 34 to 42 form part of these accounts.

The supplementary revenue and capital columns are both prepared under the guidance published by the Association of Investment Companies.

A Statement of Total Recognised Gains and Losses is not required as all gains and losses of the Company have been reflected in the above statement.

**BALANCE SHEET**

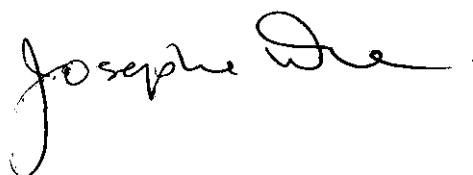
as at 30 September 2006

	Notes	2006 £000	Restated† 2005 £000
<b>Fixed assets</b>			
Investments at fair value through profit or loss	9	285,415	253,549
<b>Current assets</b>			
Debtors	11	1,901	656
Cash at bank and in hand		5,326	3,444
		7,227	4,100
<b>Creditors: amounts falling due within one year</b>	12	(606)	(3,777)
<b>Net current assets</b>		6,621	323
<b>Net assets</b>		292,036	253,872
<b>Capital and reserves</b>			
Called-up share capital		4,436	4,436
Share premium account		1,411	1,411
Special reserve		79,917	79,917
Redemption reserve		352	352
Capital reserve – realised		84,187	41,794
Capital reserve – unrealised		123,237	128,116
Revenue reserve		2,034	1,384
Own shares held		(3,538)	(3,538)
<b>Total equity shareholders' funds</b>		292,036	253,872
<b>Net asset value per share</b>	14	675.07p	586.85p

The financial statements on pages 30 to 42 were approved by the Board on 6 December 2006 and signed on its behalf by:

**Josephine Dixon**

Director



†Refer to note 1a for an explanation of the restatement of the 2005 balances.

The annexed notes on pages 34 to 42 form part of these accounts.

**RECONCILIATION OF MOVEMENT IN SHAREHOLDERS' FUNDS**

for the year ended 30 September 2006

	Called-up share capital £000	Share premium account £000	Special reserve £000	Redemption reserve £000	Capital reserve realised £000	Capital reserve unrealised £000	Revenue reserve £000	Own shares held £000	Total £000
<b>For the year ended 30 September 2006</b>									
Balance at 30 September 2005 as originally reported	4,436	1,411	79,917	352	41,794	128,782	735	(3,538)	253,889
Restatements	-	-	-	-	-	(666)	649	-	(17)
Balance at 30 September 2005 (restated)	4,436	1,411	79,917	352	41,794	128,116	1,384	(3,538)	253,872
Net gain on realisation of investments	-	-	-	-	42,372	-	-	-	42,372
Unrealised movement on investments	-	-	-	-	-	(4,879)	-	-	(4,879)
Capital Management charges	-	-	-	-	21	-	-	-	21
Net revenue retained for the year	-	-	-	-	-	-	1,299	-	1,299
Dividends paid	-	-	-	-	-	-	(649)	-	(649)
<b>Balance at 30 September 2006</b>	<b>4,436</b>	<b>1,411</b>	<b>79,917</b>	<b>352</b>	<b>84,187</b>	<b>123,237</b>	<b>2,034</b>	<b>(3,538)</b>	<b>292,036</b>
<b>For the year ended 30 September 2005</b>									
Beginning of year	4,436	1,411	79,917	352	29,904	29,825	1,351	-	147,196
Net gain on realisation of investments	-	-	-	-	12,399	-	-	-	12,399
Unrealised appreciation on investments (restated)	-	-	-	-	-	98,291	-	-	98,291
Net gain on realisation of foreign currency	-	-	-	-	169	-	-	-	169
Capital management charges	-	-	-	-	(678)	-	-	-	(678)
Net revenue retained for the year	-	-	-	-	-	-	898	-	898
Buy back of own shares held in treasury	-	-	-	-	-	-	-	(3,538)	(3,538)
Dividends paid	-	-	-	-	-	-	(865)	-	(865)
<b>Balance at 30 September 2005 (restated)</b>	<b>4,436</b>	<b>1,411</b>	<b>79,917</b>	<b>352</b>	<b>41,794</b>	<b>128,116</b>	<b>1,384</b>	<b>(3,538)</b>	<b>253,872</b>

**CASHFLOW STATEMENT**

for the year ended 30 September 2006

	Notes	Year ended 30 September 2006 £000	Restated Year ended 30 September 2005 £000
<b>Operating activities</b>			
Income received from investments		4,848	4,174
Interest received		53	5
Investment management fees paid		(3,288)	(1,622)
Other cash payments		(1,045)	(955)
Net cash inflow from operating activities	15	568	1,602
<b>Servicing of finance</b>			
Interest paid		(5)	(23)
<b>Taxation</b>			
Overseas tax paid		(731)	(572)
<b>Financial investments</b>			
Purchases of investments		(101,037)	(75,649)
Sales of investments		103,736	82,035
Net cash inflow from financial investments		2,699	6,386
Equity dividends paid		(649)	(865)
<b>Financing</b>			
Buyback of ordinary shares		-	(3,538)
Net cash outflow from financing		-	(3,538)
<b>Increase in cash</b>	16	1,882	2,990

The annexed notes on pages 34 to 42 form part of these accounts.

## NOTES TO THE ACCOUNTS

### 1. ACCOUNTING POLICIES

A summary of the principal policies, all of which have been applied consistently throughout the year, is set out below:

#### **(a) Basis of Accounting**

These financial statements are prepared under the historical cost convention as modified by the revaluation of fixed asset investments and in accordance with applicable United Kingdom accounting standards and with the Statement of Recommended Practice 2003 (revised 2005) regarding the Financial Statements of Investment Trust Companies ("SORP"). The Company has adopted FRS 25 "Financial Instruments: Disclosure and Presentation", FRS 26 "Financial Instruments: Measurement" and FRS 21 "Events after the Balance Sheet Date" in these financial statements. The significant accounting impact on these financial statements is set out below:

- Listed investments are now valued at fair value deemed to be their bid market prices whereas in prior periods they had been valued at middle market prices. The effect of this change is to decrease the value of listed investments as previously reported at 30 September 2005 by £666,000, comparative balances have been restated accordingly.
- Dividends on the Company's Ordinary shares will not be recognised in the financial statements until they have been declared whereas in prior periods they were recognised in the period to which they relate. As a result the Balance Sheet "Creditors: amounts falling due within one year" as at 30 September 2005 has been restated by reducing it by £649,000. The revenue reserve at 30 September 2005 has been increased by a similar amount.

With the exception of the changes stated above the accounting policies in the 2005 financial statements remain unchanged.

#### **(b) Valuation of Investments**

Quoted investments have been valued at bid market prices. Unquoted investments are included at a valuation determined by the Directors after discussion with the Investment Manager on the basis of the latest accounting and other relevant information.

The differences between the cost of investments and their valuation at the Balance Sheet date have been treated as unrealised appreciation/depreciation and have been taken to capital reserve – unrealised.

Profits and losses on realisation of investments have been taken to capital reserve – realised.

Year-end exchange rates are used to translate the value of investments which are denominated in foreign currencies.

#### **(c) Foreign Currency**

Transactions denominated in foreign currencies are translated into sterling at actual exchange rates as at the date of the transaction or, where appropriate, at the rate of exchange in a related forward exchange contract. Monetary assets and liabilities denominated in foreign currencies at the year-end are reported at the rates of exchange prevailing at the year-end or, where appropriate, at the rate of exchange in a related forward exchange contract. Any gain or loss arising from a change in exchange rates subsequent to the date of the transaction is included as an exchange gain or loss in capital reserve – unrealised. Foreign exchange movements on fixed asset investments are included in the Income Statement within gains on investments.

## NOTES TO THE ACCOUNTS

continued

### (d) Income

Investment income, which includes related taxation, has been accounted for on an ex-dividend basis or when the Company's right to the income is established.

Interest receivable on deposits is accounted for on an accruals basis.

### (e) Expenses

All expenses are accounted for on an accruals basis and are charged as follows:

- the basic investment management fee is charged wholly to revenue;
- any investment performance bonus payable to Baring Asset Management Limited is charged wholly to capital reserve – realised;
- dealing costs are charged wholly to capital; and
- other expenses are charged wholly to revenue.

### (f) Interest Payable

Interest payable is accounted for on an accruals basis, and is charged wholly to revenue.

### (g) Capital Reserve – Realised

The following are accounted for in this reserve:

- realised gains or losses on the disposal of investments;
- realised exchange differences on the disposal of foreign currency balances; and
- any investment performance bonus payable to Baring Asset Management Limited.

### (h) Capital Reserve – Unrealised

The following are accounted for in this reserve:

- unrealised increases or decreases in the valuation of investments held at the year-end; and
- unrealised exchange differences in the valuation of foreign currency balances and forward foreign exchange contracts in existence at the year end.

### (i) Special reserve

Pursuant to a special resolution passed on 8 November 2002, the Company's application to reduce its share premium account was approved by the High Court and registered with the Registrar of Companies on 18 December 2002. The amount of the reduction was £86,624,982, representing the share premium arising on the issue of shares by the Company on 17 December 2002. This amount was transferred to a special reserve which is available for the repurchase by the Company of its own shares.

### (j) Taxation

The charge for taxation is based upon the net revenue for the year. The tax charge is allocated to the revenue and capital accounts according to the marginal basis whereby revenue expenses are first matched against taxable income arising in the revenue account; the effect of this for the year ended 30 September 2006 was that all the deductions for tax purposes went to the revenue account.

Deferred taxation will be recognised as an asset or a liability if transactions have occurred at the balance sheet date that give rise to an obligation to pay more taxation in the future, or a right to pay less taxation in the future. An asset will not be recognised to the extent that the transfer of economic benefit is uncertain.

**NOTES TO THE ACCOUNTS**

continued

**2. INCOME**

	2006 £000	2005 £000
<b>Income from investments</b>		
Unfranked – Quoted	5,785	4,097
<b>Other income</b>		
Deposit interest	53	5
	<b>5,838</b>	<b>4,102</b>

**3. INVESTMENT MANAGEMENT FEE**

Baring Asset Management Limited (“Barings”) acts as Investment Manager of the Company under an agreement terminable by either party giving not less than one months’ written notice. Under this agreement Barings receives a basic fee (charged to revenue) which is calculated monthly and payable at an annual rate of 0.8% of the net asset value of the Company. The Directors have decided upon a policy of non-allocation of the investment management fees and as such they have been charged wholly to the revenue account.

In addition under the agreement Barings is entitled to a performance fee (charged to capital) which is payable at the rate of 10% of the amount by which the change in the Company’s net asset value exceeds the benchmark. The performance fee is capped at 0.6% of the net asset value of the Company on the first day of the performance period. The performance fee is calculated annually on 30 September. The whole of the performance fee is charged to the capital account as it is deemed to have arisen entirely as a result of the capital performance of the Company.

The Board has agreed with the Investment Manager that as a total return benchmark is used to measure performance it would be more equitable to base the performance fee on the total return of the portfolio to include both capital and net revenue. This ensures that the performance fee is payable on the out-performance of the benchmark on a comparable basis. In 2005 as a result, it was agreed to pay an additional performance fee of £39,000 during the 2005 period to reflect the 2p per share dividend paid for the year ended 30 September 2005. No performance fee is payable for the year ended 30 September 2006.

The investment management fee comprises:

	2006 £000	2005 £000
Basic fee (charged to revenue)	2,331	1,465
Performance fee (charged to capital):		
– provision for year	–	588
– additional payment in respect of prior year	–	39
– overaccrual for the prior year	(21)	–
	<b>2,310</b>	<b>2,092</b>
Irrecoverable VAT thereon	330	179
	<b>2,640</b>	<b>2,271</b>

At 30 September 2006, £237,000 (30 September 2005: £888,000) of this fee remained outstanding.

**NOTES TO THE ACCOUNTS**

continued

**4. OTHER EXPENSES**

	2006 £000	2005 £000
Custody and administration expenses	1,003	865
Auditor's remuneration for:		
– audit	20	19
– other services	5	5
Directors' fees	114	127
	<b>1,142</b>	<b>1,016</b>

**5. INTEREST PAYABLE**

	2006 £000	2005 £000
(All charged to revenue)		
On short-term loan and overdraft facility with State Street Bank & Trust Company repayable within 5 years, not by installments		
Bank overdraft	5	16
Commitment fee on unused loan facility	–	7
	<b>5</b>	<b>23</b>

**6. TAXATION**

	2006 £000	2005 £000
(All charged to revenue)		
Current tax charge for the period:		
Overseas taxation	731	572

The tax rate assessed for the year is different to the standard rate of corporation tax. The differences are explained below:

	2006 £000	2005 £000
Return on ordinary activities before taxation	2,030	1,470
Return on ordinary activities multiplied by the standard rate of corporation tax of 30%	609	441
<b>Effect of:</b>		
Overseas taxation not utilised in the year	116	334
Expenses charged to capital available to be utilised	6	(203)
	<b>731</b>	<b>572</b>

The Company is not liable to tax on capital gains due to its status as an investment trust company.

**NOTES TO THE ACCOUNTS**

continued

**7. DIVIDEND**

	2006 Per share	2006 £000	2005 Per share	2005 £000
Annual dividend per ordinary share – proposed	2.70p	1,172	1.50p	649
Prior year dividend not paid due to repurchase of shares held in treasury	–	–	–	(22)
	<b>2.70p</b>	<b>1,172</b>	<b>1.50p</b>	<b>627</b>

**8. RETURN PER ORDINARY SHARE**

	Revenue	Capital	Total 2006	Revenue	Capital	Restated Total 2005
Return per ordinary share	3.00p	86.45p	89.45p	2.07p	253.90p	255.97p

Revenue return (earnings) per ordinary share is based on the net revenue on ordinary activities after taxation of £1,299,000 (2005: £898,000).

Capital return per ordinary share is based on net capital profits for the financial year of £37,514,000 (2005: £110,181,000).

These calculations are based on the 43,259,906 (2005: weighted average 43,395,523) ordinary shares in issue during the year.

At 30 September 2006 there were 43,259,906 ordinary shares of 10p each in issue (2005: 43,259,906) which excludes 1,100,000 ordinary shares held in treasury (2005: 1,100,000 shares held in treasury). The shares held in treasury are treated as not being in issue when calculating the weighted average of ordinary shares in issue during the year. Shares held in treasury are non-voting and not eligible for receipt of dividends.

**9. (i) FIXED ASSET INVESTMENTS**

Country	Quoted overseas £000	Unquoted £000	Total 2006 £000	Restated		Total 2005 £000
				Quoted overseas £000	Unquoted £000	
Czech Republic	23,507	134	23,641	23,402	141	23,543
Hungary	34,743	–	34,743	50,191	–	50,191
Poland	33,087	–	33,087	47,144	–	47,144
Russia	159,806	–	159,806	105,800	–	105,800
Turkey	27,454	–	27,454	26,871	–	26,871
Kazakhstan	6,684	–	6,684	–	–	–
<b>Total</b>	<b>285,281</b>	<b>134</b>	<b>285,415</b>	<b>253,408</b>	<b>141</b>	<b>253,549</b>

**NOTES TO THE ACCOUNTS**

continued

**9. (ii) MOVEMENTS IN THE YEAR**

	Restated					
	Quoted overseas	Unquoted	Total	Quoted	Unquoted	Total
	£000	£000	£000	£000	£000	£000
Book cost at beginning of year	125,275	157	125,432	116,692	157	116,849
Unrealised appreciation	128,132	(16)	128,116	29,844	(19)	29,825
Valuation at beginning of year	253,407	141	253,548	146,536	138	146,674
Purchases at cost	98,454	-	98,454	77,137	-	77,137
Sales:						
- proceeds	(104,080)	-	(104,080)	(80,952)	-	(80,952)
- realised gains	42,372	-	42,372	12,399	-	12,399
Unrealised movement	(4,872)	(7)	(4,879)	98,288	3	98,291
Valuation at end of year	285,281	134	285,415	253,408	141	253,549

Expenses incidental to the purchase or sale of investments are included within the purchase cost or deducted from sales proceeds. These expenses amounted to £346,000 for the year ended 30 September 2006 (2005: £387,000).

**9. (iii) GAINS ON INVESTMENTS**

	Restated	
	2006 £000	2005 £000
Realised gains on sales	42,372	12,399
Unrealised appreciation	(4,879)	98,291
	37,493	110,690

A list of the Company's twenty largest investments by market value is shown on page 12 and a geographical and industrial classification of the investment portfolio is shown on page 13.

**10. GAINS ON FOREIGN EXCHANGE**

	2006 £000	2005 £000
<b>Realised</b>		
Foreign currency bank balances	-	169

The Company maintains a US dollar bank account for settling its investment transactions and paying expenses.

**NOTES TO THE ACCOUNTS**

continued

**11. DEBTORS**

	2006 £000	2005 £000
<b>Amounts due within one year</b>		
Amounts due from brokers	345	–
Prepayments and accrued income	1,431	512
Other debtors	125	144
	<b>1,901</b>	<b>656</b>

**12. CREDITORS**

	2006 £000	Restated 2005 £000
<b>Amounts falling due within one year</b>		
Purchases for future settlement	–	2,583
Other creditors	606	1,194
	<b>606</b>	<b>3,777</b>

Since November 2003, the Company has had a US\$10 million unsecured loan and overdraft facility with State Street Bank and Trust Company. Under this facility, the Company may draw up to a maximum principal amount of US\$10 million in varying proportions and for varying periods at prevailing interest rates.

**13. CALLED-UP SHARE CAPITAL**

	2006 £000	2005 £000
<b>Authorised</b>		
199,500,000 ordinary shares of £0.10	19,950	19,950
50,000 redeemable preference shares of £1.00	50	50
	<b>20,000</b>	<b>20,000</b>
	<b>2006 £000</b>	<b>2005 £000</b>

**Authorised, issued and fully paid up**

44,359,906 ordinary shares of £0.10 (fully paid)	4,436	4,436
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No ordinary shares were repurchased during the year (during 2005: 1,100,000 ordinary shares were repurchased for £3,538,000). The Company holds 1,100,000 ordinary shares in treasury which are treated as not being in issue when calculating the number of ordinary shares in issue during the year. Shares held in treasury are non-voting and not eligible for receipt of dividends.

**NOTES TO THE ACCOUNTS**

continued

**14. NET ASSET VALUE PER SHARE**

Total shareholders' funds and the net asset value per share attributable to the ordinary shareholders at the year-end calculated in accordance with the Articles of Association were as follows:

	2006	Restated 2005
Total shareholders' funds (£000)	292,036	253,872
Net asset value (pence per share)	675.07p	586.85p

The net asset value per share is based on total shareholders' funds above, and on 43,259,906 shares in issue at the year-end (2005: 43,259,906) which excludes 1,100,000 ordinary shares held in treasury. The shares held in treasury are treated as not being in issue when calculating the net asset value per share. Shares in treasury are non-voting and not eligible for receipt of dividends. The net asset value at 30 September 2005 has been restated to reflect the valuation of the portfolio at 30 September 2005 at bid market prices and the removal of the creditor at that date for the annual dividend for 2005 that was paid in February 2006.

**15. RECONCILIATION OF NET REVENUE BEFORE INTEREST PAYABLE AND TAX TO NET CASH OUTFLOW FROM OPERATING ACTIVITIES**

	2006 £000	2005 £000
Net revenue before interest payable and taxation	2,035	1,493
(Decrease)/increase in accrued income	(937)	77
(Decrease)/increase in sundry creditors	(588)	780
Increase/(decrease) in debtors	37	(70)
Management fee capitalised	21	(678)
Net cash inflow from operating activities	568	1,602

**16. ANALYSIS OF CHANGES IN CASH DURING THE YEAR**

	2006 £000	2005 £000
Beginning of year	3,444	285
Net cash inflow	1,882	2,990
Realised foreign exchange differences	-	169
End of year	5,326	3,444

**Analysis of balance:**

Bank balance	5,326	3,444
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**17. FINANCIAL COMMITMENTS**

At 30 September 2006, there were no outstanding capital commitments (2005: nil).

## NOTES TO THE ACCOUNTS

continued

### 18. CUSTODIAN'S LIEN

Under the terms of the custody agreement with State Street Bank & Trust Company ("State Street"), the Company has granted a lien over its securities and other assets that are deposited with State Street to cover all sums due in connection with the custody agreement.

### 19. RELATED PARTY DISCLOSURES

Under FRS 8, the Company is required to provide additional information concerning its relationship with the Investment Manager, Barings, and details of the investment management fee charged by Barings are set out in note 3. The ultimate holding company of Barings is Massachusetts Mutual Life Insurance Company.

### 20. RISK MANAGEMENT AND FINANCIAL INSTRUMENTS

#### **The Company's Financial Instruments comprise:**

- Shares, bonds and cash with international exposure. These are held in accordance with the Company's investment objective set out on page 3. The investments held by the Company, which are held at fair value, are shown in note 9.
- Short-term bank overdraft and loan facility held to cover short-term timing differences on investment trades and to provide finance for the Company's operations.

The Company does not use derivative instruments to hedge the investment portfolio against market risk or foreign currency risk.

The main risks associated with the Company are market risk (incorporating liquidity risk), foreign currency risk and interest rate risk, described below.

#### **Market Risk**

Special considerations and risk factors associated with the Company's investments are discussed on page 4. Market risk arises from, amongst others, political or economic changes, changes in interest rates, uncertainty about future prices of the financial securities held and the liquidity of such instruments. Market risk is managed through the investment guidelines and asset allocation restrictions agreed by the Board and the Investment Manager and reviewed at each Board meeting.

#### **Foreign Currency Risk**

Foreign currency risk arises from changes in the rate of exchange between sterling and the currencies of the countries in which the Company invests, which are identified in the table shown in note 9. In addition as certain of the Company's investments are held in ADR's and GDR's there is also a currency exposure to either US dollars or euros. The Company's uninvested cash balances earn interest at floating rates, linked to current short-term market rates.

#### **Interest Rate Risk**

During the year, the Company's average liquidity was approximately 1.8% (2005: 0.4%) of average net asset value. Such liquidity was invested in short-term deposits at floating rates.

The Board regularly reviews the amount drawn down under the overdraft and loan facility to ensure that borrowings are appropriate to prevailing market conditions.

## NOTICE OF ANNUAL GENERAL MEETING

Notice is hereby given that the Annual General Meeting of the Company will be held at 155 Bishopsgate, London EC2M 3XY on Tuesday, 16 January 2007, at 2.30pm to consider and, if thought fit, pass the following resolutions, which will be proposed as to resolutions 1, 2, 3, 4, 5, 6 and 7 as ordinary resolutions, and as to resolutions 8 and 9 as special resolutions:

1. To approve the Directors' Remuneration Report for the year ended 30 September 2006.
2. To receive the Directors' Report and statement of accounts for the year ended 30 September 2006.
3. To declare the annual dividend.
4. To re-elect Iain Saunders as a Director of the Company.
5. To re-elect John Cousins as a Director of the Company.
6. To re-appoint KPMG Audit Plc as Auditors of the Company and to authorise the Board to determine their remuneration.

### SPECIAL BUSINESS

To consider the following resolutions:

7. Authority to allot new ordinary shares – Ordinary Resolution:

That, the Board be and it is hereby generally and unconditionally authorised to exercise all powers of the Company to allot relevant securities (within the meaning of Section 80 of the Companies Act 1985) up to an aggregate nominal amount of £216,299 (being approximately 5% of the issued share capital of the Company as at the date of this document excluding shares held in treasury at that date) PROVIDED THAT this authority shall expire at the conclusion of the next Annual General Meeting of the Company after the passing of this resolution, save that the Company may before such expiry make one or more offers or agreements which would or might require relevant securities to be allotted after such expiry and the Board may allot relevant securities in pursuance of such offers or agreements as if the authority conferred hereby had not expired.

8. Authority to disapply pre-emption rights on allotment of ordinary shares - Special Resolution

That, subject to the passing of Resolution 7 set out in the notice convening the Annual General Meeting of the Company dated 6 December 2006, the Board be and is hereby empowered pursuant to Section 95 of the Companies Act 1985 to allot equity securities (within the meaning of Section 94 of the said Act) for cash pursuant to the authority conferred by Resolution 7 and/or where such allotment constitutes an allotment of equity securities by virtue of Section 94(3A) of the said Act\*, as if sub-section (1) of Section 89 of the said Act did not apply to any such allotment, PROVIDED THAT this power shall be limited:

- (a) to the allotment of equity securities in the Company whether by way of rights issue, open offer or any other pre-emptive offer to holders of the ordinary shares (excluding any shareholder holding shares as treasury shares) where the equity securities respectively attributable to the interest of such holders of ordinary shares on a fixed record date are proportionate (as nearly as may be) to the respective numbers of ordinary shares held by them subject to such exclusions or other arrangements as the Board may deem necessary or expedient in relation to fractional entitlements or legal or practical problems arising in any overseas territory the requirements of any regulatory body or any stock exchange in any territory or any other matter whatsoever;

\* Section 94(3A) provides that an allotment of equity securities also includes the sale of any relevant shares held by the Company as treasury shares. See also paragraph 8 on pages 22 and 23.

## NOTICE OF ANNUAL GENERAL MEETING

continued

- (b) to the allotment (otherwise than pursuant to sub-paragraph (a) above) of equity securities up to an aggregate nominal value of £326,299 (being the aggregate of (i) 5% of the issued share capital as at the date of this document less the aggregate nominal value of shares held in treasury as at the date of this document and (ii) the aggregate nominal value of shares held in treasury as at the date of this document) at a price not less than net asset value per share at the close of business on the business day which is two business days immediately preceding the day on which the earlier of the agreement to allot such share is made or such share is allotted;

and shall expire at the conclusion of the next Annual General Meeting of the Company after the passing of this Resolution, save that the Company may before such expiry make an offer or agreement which would or might require equity securities to be allotted after such expiry and the Board may allot equity securities in pursuance of such an offer or agreement as if the power conferred hereby had not expired.

### 9. Authority to repurchase the Company's shares – Special Resolution:

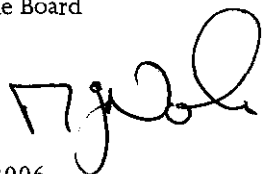
That, the Company be and is hereby generally and unconditionally authorised in accordance with Section 166 of the Companies Act 1985 (the "Act") to make market purchases (within the meaning of Section 163 of the Act) of ordinary shares of £0.10 each in the capital of the Company (the "shares") provided that:

- (a) the maximum number of shares hereby authorised to be purchased shall be 6,484,659 (being approximately 14.99% of the issued share capital of the Company as at the date of this document, excluding shares held in treasury);
- (b) the minimum price (exclusive of any expenses) which may be paid for a share is £0.10;
- (c) the maximum price (exclusive of any expenses) which may be paid for a share is an amount equal to 105% of the average of the middle market quotations for a share taken from the London Stock Exchange Daily Official List for the 5 business days immediately preceding the day on which the share is purchased;
- (d) the authority hereby conferred shall expire at the earlier of the conclusion of the Annual General Meeting of the Company in 2008 and 15 July 2008, unless such authority is renewed prior to such time;
- (e) the Company may make a contract to purchase shares under the authority hereby conferred prior to the expiry of such authority which will be or may be executed wholly or partly after the expiration of such authority and may make a purchase of shares pursuant to any such contract; and
- (f) all shares purchased pursuant to the said authority shall be either:
- (i) cancelled immediately upon completion of the purchase; or
- (ii) held, sold, transferred or otherwise dealt with as treasury shares in accordance with the provisions of the Act.

By order of the Board

M. J. Nokes  
Secretary

6 December 2006



155 Bishopsgate  
London EC2M 3XY

## NOTES TO NOTICE OF MEETING

1. A member of the Company entitled to attend and vote at the meeting may appoint one or more proxies to attend and, on a poll, to vote on his or her behalf. A proxy need not be a shareholder of the Company.
2. Pursuant to Regulation 41 of the Uncertificated Securities Regulations 2001, the Company gives notice that only those shareholders entered on the register of members of the Company at the close of business on 12 January 2007 will be entitled to attend and vote at the aforesaid meeting in respect of the number of shares registered in their name at that time. Changes to the entries on the register after that time will be disregarded in determining the rights of any person to attend or vote at the meeting.
3. A form of proxy is enclosed for use by shareholders. To be effective, the form of proxy for use at the meeting and the power of attorney or other authority (if any) under which it is signed, or a notarially certified copy of such power or authority, must be deposited at the office of the Company's registrars, Capita Registrars, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4TU not less than 48 hours before the time appointed for holding the meeting or any adjournment thereof.
4. Completion and return of a form of proxy will not prevent shareholders from attending the meeting and voting in person if they so wish.
5. The register of interests of the Directors and connected persons in the share capital of the Company, giving details of all transactions of each Director and his family interests in the shares of the Company, will be available for inspection at 155 Bishopsgate, London EC2M 3XY during usual business hours on any weekday (Saturdays and public holidays excepted). It will also be available for inspection at the Annual General Meeting.
6. No Director has any contract of service with the Company.

## ISA & SAVINGS SCHEME

The Company's shares can be purchased through the Baring Emerging Europe ISA & Savings Scheme which provides a simple and cost-effective method for investing either lump sums or on a regular basis.

The Baring Emerging Europe ISA is available as both a Maxi – ISA and a Mini – ISA.

The investment limits are:

	Maxi – ISA		Mini – ISA
	Minimum	Maximum	Investment
Regular investment	£250 per month	£583.33 per month	£250 per month
Lump sum investment	£3,000	£7,000	£3,000

The Baring Emerging Europe Savings Scheme has a minimum regular investment of £50 per month or a minimum lump sum investment of £250.

### Further Information

For further information on the ISA & Savings Scheme, please return the prepaid form printed on the following page or write to:

Baring Asset Management Limited  
c/o NTIFAS  
50 Bank Street  
London E14 5NT  
Telephone: 0870 870 8450

Alternatively information can be obtained from the Company's website: [www.bee-plc.com](http://www.bee-plc.com)

Please remember that the value of an investment and the income from it can fall as well as rise as a result of market and currency fluctuations and you may not get back the amount originally invested. Past performance is not a guarantee of future performance.

Baring Asset Management Limited, the Manager of the Baring Investment Trust ISA & Savings Scheme, is authorised and regulated by the Financial Services Authority.

## REQUEST FOR FURTHER INFORMATION

If you would like to receive further information on the Baring Emerging Europe ISA & Savings Scheme, please complete and return this reply paid form.

TITLE SURNAME

FORENAME(S)

ADDRESS

POSTCODE

DAYTIME TELEPHONE NUMBER



First fold

Second fold

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Baring Asset Management Limited  
c/o NTIFAS  
50 Bank Street  
LONDON  
E14 5NT

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