

# CALEDONIAN TRUST PLC

## Directors' Report and Financial Statements 30 June 2003

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## Company Information

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<b>Board of Directors</b>	I. D. Lowe (Chairman and Chief Executive) M. J. Baynham L.L.B.(Hons) J. N. Little B. J. Rankin C.A.
<b>Secretary</b>	M. J. Baynham L.L.B.(Hons)
<b>Head Office</b>	61 North Castle Street Edinburgh EH2 3LJ
<b>Registered Office</b>	St Ann's Wharf 112 Quayside Newcastle upon Tyne NE99 1SB
<b>Auditors</b>	KPMG Audit Plc Saltire Court 20 Castle Terrace Edinburgh EH1 2EG
<b>Nominated Advisers</b>	Noble & Company Limited 76 George Street Edinburgh EH2 3BU
<b>Nominated Brokers</b>	Numis Securities Limited Cheapside House 138 Cheapside London EC2V 6LH
<b>Bankers</b>	Bank of Scotland Head Office PO Box 5 The Mound Edinburgh EH1 1YZ
<b>Registrars</b>	Lloyds TSB Registrars Scotland PO Box 28448 Finance House Orchard Brae Edinburgh EH4 1WQ <a href="http://www.shareview.co.uk">www.shareview.co.uk</a>
<b>Registered No.</b>	1040126

## Chairman's Statement

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*for the year ended 30 June 2003*

### Introduction

The Group made a profit of £507,967 in the year to 30 June 2003 compared to £3,237,578 last year which included £2,589,353 from the sales of investment property. NAV per share on 30 June 2003 increased by 7.1p to 170.6p compared to 163.5p last year.

Rent and service charges were £962,587, £1,768,109 lower than last year due primarily to the sales of St Magnus House in April 2002 and Stoneywood during 2002 and the determination of the lease of St Margaret's House, Edinburgh on 28 November 2002. Net interest payable fell by £705,989 due to lower borrowings and increased interest received of £344,264, while administration expenses fell by £146,845. On 30 June 2003 bank loans and overdrafts were £3,479,983 and cash at bank was £5,233,211. During the year average base rate fell to 3.90% from 4.32% last year.

On 30 June 2003 the Group's portfolio comprised by value 57.89% office investment property (of which 70.58% is open plan) 10.62% retail property, 27.63% development property and 3.86% trading property.

### Review of Activities

The Group's property activities have been varied. However, there have been no significant changes to our Edinburgh New Town investment portfolio. The La Tasca restaurant in South Charlotte Street appears to trade well and is already highly reversionary. In 61 North Castle Street work started in July 2003 on a structural overhaul and the redevelopment of the upper two floors and attic into two large Georgian style flats entering off the original staircase, 59 North Castle Street. We expect to market these in the Spring.

Our largest investment property in Edinburgh, St Margaret's House, a 92,845 ft<sup>2</sup> open-plan office was let to the Scottish Ministers until November 2002 when the lease determined. The Scottish Parliament operates a dispersal programme whereby there is a presumption against the location of offices for civil servants in Edinburgh where new agencies or departments are formed, or where leases on existing properties determine. In accordance with this policy one of the two occupiers of St Margaret's House relocated to new purpose-built premises in the Scottish Borders near Galashiels, and the second occupier, the Registers of Scotland, has transferred all their staff into their other existing premises.

Plans for refurbishment to varying office specifications are being prepared together with a proposal to remodel the façade. The building can be easily subdivided. Each floor of about 11,000 ft<sup>2</sup> is virtually self-contained and can be further subdivided into two wings of 4,500 ft<sup>2</sup> and 6,500 ft<sup>2</sup> both of which are capable of further subdivision. The floor to ceiling heights are similar to those in St Magnus, Aberdeen, where we carried out a full refurbishment including air handling, suspended ceilings and raised floors to create the BCO award-winning best office fitout of the year in 2001. Clearly the existing space can provide an attractive package of offices in different sizes and specifications to customers' requirements. Total occupation costs, rents, rates and services are budgeted to be significantly below the current central new Grade "A" space. These factors together with very extensive parking of one space per 500 ft<sup>2</sup>, a location near to the new Parliament and the city centre and prominent frontage to the busy A1 will make St Margaret's attractive to a wide range of occupiers.

Our property at Baylis Road/Murphy Street near Waterloo SE1 where the lease determines in March 2004 offers a similar redevelopment/ refurbishment potential to St Margaret's. We have surveyed it and prepared dilapidations schedules and estimated refurbishment costings. The property at Baylis Road is constructed of metal columns and concrete floors and so lends itself well to letting as a whole or in part. Murphy Street is open plan with good access and suitable for office or distribution use.

I reported last year an investment purchase in Glasgow at 100 West Street, currently let to Westcars, a Saab franchisee, on a 1.4 acre island site yielding approximately 7.5%. West Street is in Tradeston, a rapidly improving area adjacent to the M8 and less than 600 yards from the Broomielaw development, Glasgow's "Square Kilometre" financial services zone where 2,000 jobs have been created since 2001 and 18,000 more are targeted by 2011. This site offers very considerable long-term development potential.

## Chairman's Statement (continued)

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We continue to develop and extend our residential sites within the Edinburgh area. At Weir Court, Eskbank, near the City Bypass we completed an elegant development of five four bedroom houses in November 2002, a completion date delayed by the appalling weather last year. One house sold before 30 June 2003 and the others subsequently at prices between £280,000 and £360,000. Our second residential site, for eight detached houses, borders Musselburgh and is within 400 yards of the Main Line station at Wallyford with easy access to the A1 near the junction with the City Bypass. A large contiguous area should gain planning permission early in 2004 for private development of 280 houses and this development should greatly enhance the value on our site. Our third site, lying just east of Dunbar, should accommodate 17 houses in one area where the infrastructure is largely in place and about 29 houses in an adjoining area over which we hold an option. Further extensions of the site are under negotiation. Work on the extension of the A1 dual carriageway from Haddington to Dunbar is well advanced and the new dual carriage road should open next summer.

In Edinburgh at Belford Road, where we hold consent for a 22,500 ft<sup>2</sup> Grade A office, several residential appraisals have been made and we hope to use a recent local precedent to obtain a favourable adjustment to the existing planning envelope.

We made an opportunistic wholesale purchase of three new Edinburgh flats, including an exceptional penthouse, in the late summer from a developer anxious to complete their sales programme. We intend to market these in early Spring.

### **Economic Prospects**

World economic conditions appear much more favourable for the UK at present than they did at this time last year or indeed the previous year. Two years ago the TMT asset bubble had burst leading to an economic downturn and a full blown recession in the USA which threatened the world economy. Last year the major external variables were related to the prospects for, the effects from and the outcome of a war in Iraq. Major concerns included the economic consequences of a prolonged rise in the oil price, widespread destabilisation in the Middle East, the effects of WMD and the possibility of a long "Vietnam" type war of attrition. Fortunately the world economy recovered in 2002 and the fears of the Iraq imbroglio have not materialised.

While economic damage may have been limited, the political and declared security objectives of the Coalition have not yet been achieved. These objectives are threatened by a guerrilla war with a disparate assortment of opposition forces but united by their dislike of the invaders and independent of Saddam with access to sophisticated weaponry. A guerrilla war would represent a political failure reinforcing the failure to find WMD or to demonstrate how the success in Iraq diminishes world terrorist activity. Fortunately the economic consequences of any political failure are unlikely to be severe and the progress of the UK economy will be determined by other variables.

Economic conditions appear propitious. In the last quarter the world economy grew at its fastest pace for twenty years supported by annualised growth in the US of 8.2%, the euro zone and Japan of 1.5% and the UK of 3.1%. Fears of global deflation have subsided.

The Economist Intelligence Unit ("EIU") forecasts world growth rising from 3.3% this year to 3.9% in 2004 and to 4.1% in 2005. The Economist poll of forecasters reports 2004 growth in the USA as 4.2%, up from 3.9% last month, and significantly higher growth in all European Countries than in 2003. The EIU forecasts OECD growth rising from the current 1.9% to 2.6% in 2005 and EU recovery from the present sickly 0.6% to 2.3% in 2005. Against this background Britain's economy is also expected to grow more rapidly rising from an expected 2.0% in 2003 to 2.7% in 2004.

The USA and the UK economic forecasts are highly dependent on a reduction of the share of consumer expenditure in GDP and an increased share in other sectors. The USA has enjoyed the biggest fiscal and monetary stimulus in decades resulting in a change from a budget surplus of 1% of GDP in 2000 to a deficit of 5% this year. In parallel with the fiscal deficit the current account deficit rose to a record 5.1% of GDP earlier this year. Current low interest rates have caused a boom in mortgage refinancing which financed consumer

## Chairman's Statement (continued)

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spending but in consequence household debt and debt servicing have risen to record levels. In spite of the increase in consumer expenditure, US inflation is low because the recovery is taking place in an economy still operating below capacity in which rapid gains in productivity are resulting in employment continuing to fall seven quarters after output started to rise. Low inflation has permitted the Federal Reserve to commit itself to maintain interest rates at 1% for a "considerable period" as it considered that the risks of further disinflation are greater than inflation.

Several factors are likely to effect a rebalancing of the US economy. The recent tax cuts represent a one-off boost to the economy. Historically budget deficits are correlated with long term interest rates and interest rates seem likely to rise in the medium term. The ratio of house prices to income is already above the last boom in the late 1980s and approaching that of the inflationary 1970s, and after these peaks house price inflation fell to 0% and 2% respectively. Fading tax boosts, rising long-term interest rates and the elimination of house price inflation should curb consumption.

The trade deficit will have contributed to the recent dollar weakness causing a fall of about 20% against sterling and 31% against the euro since mid 2001. A dollar fall was presumably the meaning of Alan Greenspan's recent comment that foreign exchange markets are flexible enough to produce "a benign resolution of the US current account imbalance". Increased exports and decreased imports should, together with the fading stimulus from deficit funding, curb the growth in consumer debt and reduce fiscal and foreign exchange deficits. The US Economy should continue to be managed through the aftermath of the recent recession with growth in investment and exports replacing reduced consumer growth.

The future progress of the UK economy is highly dependent on the timing and the extent of the inevitable reduction in the rate of change of house prices. Changes in the UK housing market are even more significant for the UK economy than they are for the US economy. The risk of a significant change is also much greater than in the US as UK houses are estimated by Capital Economics to be 50% overvalued compared with 15% in the USA.

In the UK house prices have continued to rise rapidly, the reported annual increase varying between areas and compilers – Nationwide Q3 17.1%, TSB Scotland Q3 19.2% Edinburgh area Q3 14.8%. New lending and mortgage equity withdrawal ("MEW") have contributed to personal borrowing of £10.7bn in September 2003, three times the level four years ago and monthly mortgage commitments have trebled over these years. MEW has also risen sharply from about nil in 1999 to 7% currently. In November 2002 the Bank of England expected house prices to be stable by November 2004 and in May 2003 "over the next year or so", but in November 2003 reports "the MPC has revised up its central projection for house price inflation, so that it slows more gradually during the next two years" i.e. by November 2005, a year later.

Predictions of future house price changes vary. Nationwide suggest "a gentle slowdown", Bradford and Bingley a 7% rise and Hometrack a rise of 4%, adding, "There is more chance of finding Elvis on the moon than there is of a price crash next year". The Bank of England says of its central projection "there are major risks around the assumed path". The major risk on one side of the path is the prospect of continuing rapid rises in house prices making the inevitable eventual correction even more difficult. The major risk on the other side of the path is the immediate prospect of a sharp correction. Cheap money has fuelled the present escalation of house prices just as cheap equity fuelled the TMT bubble of the late 1990s. On a pessimistic view, just as with the dot-coms, the hangover from the cheap money party could last many years: falling house prices could be to the early years of the 21st century what equity prices were to the last years of the 20th. However the IMF has concluded that housing booms have been followed by busts only 40% of the time.

The IMF also observes that house price falls are often associated with rises in interest rates. A recent Economist headline was "The interest rate squeeze starts" and the MPC minutes noted that "interest rates were below plausible estimates of the neutral rate" i.e. monetary policy is still expansionary. Indeed not since 1988 has the first rise in rates not presaged further rises. Real interest rates at less than 1% are close to the lowest since 1981, the worst recession since WWII and much lower than the 6% prevailing in the 1990s recession. Indeed the forward sterling market indicates rates of over 5% within two years.

## Chairman's Statement (continued)

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Past reversals in the direction of change of interest rates have usually taken place at higher levels, say at 6½%, equal to a variable borrowing cost of say 8%, where a two % point increase in rates costs 25% more in interest, but, at a variable cost of 5%, a two % point rise costs 40% more. The annual payment due on a £100,000 25 year repayment mortgage would rise from £7,095 at 5% to £8,581 at 7% or by £1,486.

A neutral or natural long term interest rate is approximately 5% which is broadly equivalent to real economic growth of 2.5% plus 2.5% inflation. In this context recent and current rates are unsustainably low just as the sterling market indicates. These interest rate rises, or possibly even their expectation, will reduce housing demand and prices but the extent of the change is uncertain. The Bank of England now expects a safe landing with zero house price inflation by 2005 but other commentators are less sanguine and either expect a sharp fall next year or like Capital Economics, expect prices to fall 20% over three years. The sooner prices stabilise the smaller the asset bubble will be and any correction is likely to be shallower and slower.

The gradual elimination of house price inflation is a "Goldilocks" scenario, which according to the OECD would be more likely if interest rates moved very slowly up but started to do so quickly. However, Capital Economics forecasts RPIX inflation at about 2% or less in 2004 and 2005, implying lower interest rates. Contributing to and reinforcing this trend are the possibilities of a higher exchange rate (reducing prices) and of a move to the HICP target of 2% which is equivalent to 2.75% RPIX, up from the current 2.5%. In these circumstances strict observance of the MPC's inflation targeting policy would result in a continuation of the housing boom already considered economically undesirable by most commentators and as a dangerous asset bubble by some.

The independence of the MPC has enabled the Bank of England to set interest rates designed to meet the politically determined objective, an inflation rate of 2.5% RPIX plus or minus 1% point and the achievement of this target has been beneficial. However the choice of 2½% inflation as a target is arbitrary as there is little evidence that such a rate is "better" than say 2% or 3% or even a wider range. Indeed the target has just been arbitrarily changed to an effective rate of 2.75%! The success of the single policy of targeting inflation within a narrow limit does not mean that this policy is the optimal policy especially as inflation now seems less threatening. Previous policies normally widely applauded at the time, included the gold standard, the money supply, the exchange rate and shadowing the Mark: now we have an inflation target!

The recent crash in the TMT sector caused by the bursting of an asset bubble resulted in considerable and widespread economic distress whose worst affects have been mitigated by an exceptionally expansionary monetary policy which policy has in turn led to what may prove to be an asset bubble in residential property prices. As the OECD says "the biggest domestic risk to the [UK] economy is the threat of a sudden drop in house prices leading to a sharp retrenchment of consumer spending which would be all the more likely if house price inflation were to continue at double digit rates well into next year and reinforces the case for a continued, but gradual tightening of monetary policy". A too strictly limited target may not optimise economic conditions.

The Government has recently committed itself to a vast expansion of the public sector budgeting 4.5% per annum growth in the three years until 2005-06 and then 2.8% until 2007-08. However as the NHS growth is to be maintained at 7% in real terms until 2008, less than 2%, half the rate of current expansion, remains for all other public services, including education currently expanding at 6%. The PBR estimates that over the period the current trend growth will be 2.75%, and that the PSNB will be £37bn this year falling slowly to £27bn in 2007. These 2003 PBR estimated deficits represent increases of £10bn on the 2003 Budget figures and subsequent years are all now significantly higher, the cumulative increase reaching £34.1bn, and the resulting total estimated borrowing to be 35.5% of GDP in 2008-2009 only 10% below the Chancellor's 40% ceiling. The Treasury forecasts are based on assumptions of higher growth rates (3-3.5%) than other commentators, including the Bank of England. More pessimistic growth assumptions, 2.3% or so would result in the PSNB being higher. The Government report that the £10bn overshoot in the 2003/2004 PSNB is due to £5.4bn extra public spending costs including Iraq, plus £5.5bn shortfall in revenues, partially offset by £0.9bn "under-spend". In the current forecasts the PBR assumes that while the extra spending will persist, tax revenues will



## Chairman's Statement (continued)

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return to the April 2003 prediction. As the FT says "this forecast opens Mr Brown to the risk of disappointment". Earlier this year the EIU said that unless tax receipts recover faster than currently seems possible . . . the Government will have to choose between raising taxes further or making more modest increases in public expenditure or else jettison compliance with its self-imposed budgetary rules. Clearly if there is a sharp contraction in consumer expenditure rather than a slow down in growth sufficient to allow other sectors to grow more quickly the PSNB will be even larger.

Government policy is predicated on above average economic growth, the recovery in tax receipts, the absence of unexpected demands and the successful rebalancing of the economy away from consumption to other sectors. However if any one of these variables proves unfavourable, their present policy will be untenable: one or more of their policies on tax or spending or the Golden Rule will have to be jettisoned. However with the election due by June 2006 but very possibly to be held within 18 months, current policies can be maintained, even if inappropriate, until then. The most immediate risk of economic dislocation is the outside chance of a sharp correction in the housing market which would result in much lower growth in the short term. The longer high residential price inflation persists the greater this risk becomes. Without such a dislocation growth prospects, until at least the election, are very good.

### Property Prospects

The CB Hillier Parker "CBRE" All Property Yield Index fell 0.1% point to 7.1% in the year to September 2003 due to lower yields in the retail sectors outweighing a 0.1% point rise in office yields. The ten year Gilts yield was 4.5% increasing the yield gap to 2.6% points-down from about 2.9% in early 2003, although the recent rise in gilt yields to 5.1% is likely to have reduced the present gap to 2.0%. The current All Property yield is 0.3% points lower than the recent peak of 7.4% in Q4 2001 but over 5 years it has risen 0.5% points although gilts have fallen 1% points.

The yield gap has risen because of relatively poor rental performance. The CBRE rent index has now fallen for five consecutive quarters giving an annual decline of 2.7% and reducing the 5 year rental growth to 4% per annum. Since the 1990 market peak the All Property rental index has risen by only 14.5% but in real terms has fallen by 19.8%. Central London offices have experienced the greatest fall as rentals have halved in real terms. Retail warehouses have been the only sector to have risen in real terms and by a significant 41.8%.

The Estates Gazette November 2003 survey reported that "rental value growth" was expected to fall 0.6% further in 2004 but to rise by 1.2% in 2005. Yields were expected to be unchanged in 2004 but to fall slightly in 2005. Cluttons forecasts a further 5% fall in office rents in 2004 but all sectors to have a 1% rise in 2005. They forecast that yields will not change in 2004 or 2005. CBRE expect 2004 to give "weaker investment performance compared to the last 18 months" due to two important trends. Higher interest rates are likely to reduce investment demand from highly geared investors, notably private individuals or syndicates, while the expected slowdown in consumer spending will reduce rental growth.

The possibility of low rental growth and rising yield has reduced CBRE's estimate of IPD's Property Total Returns in 2004 to 6%, a return sharply lower than the 10.6% reported by IPD over the last 12 months and the 10% to 11% over the last 5, 10 and 17 years. Equities have returned -0.6% over the last five years but 6.5% over 10 years and Gilts about 7.0% and 5.0% respectively. The recent recovery in the Stock Market has resulted in a 14% rise in equities over 12 months but Gilts have only returned 1.3% due to rising interest rates. This crossover in property and equity returns could represent a significant change in returns among sectors.

In Edinburgh, Ryden report take-up of office space in the 6 months to September 2003 was 401,000 ft<sup>2</sup> up from the 340,000 ft<sup>2</sup> of the two previous equivalent periods but significantly below the average of 603,000 ft<sup>2</sup> in the earlier four years. For the third consecutive period Ryden report an increased record supply, now 2,874,000 ft<sup>2</sup>, of which 70.3% is in units over 10,000 ft<sup>2</sup>, a change from the previous peak in the early 1990s when only 51.1% was available in such large units. City centre headline asking rents are down 10% from the peak to £27 and in other areas have fallen at least 20%. Actual rents, after incentives, are probably significantly less. At these asking levels rents are the same as the previous peak in 1992 in nominal terms, but represent only 74% of them in real terms.

## Chairman's Statement (continued)

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In Aberdeen the take-up of 151,256 ft<sup>2</sup> in the 6 months to September 03 is lower than last year and in Aberdeen supply levels are at the sixth successive high of 1,227,977 ft<sup>2</sup> of which a record 59.9% is suites greater than 10,000 ft<sup>2</sup>. Ryden report business park rents as "maintained". Oil prices have been relatively steady and averaged \$28 over the last year, a high figure compared to some years. In spite of the high prices achieved and forecasts of prices around \$20 in 2004-2005 drilling activity dropped to 33 wells in 2002 compared to about 100 or more each year from 1982 to 1997. The convenor of the Heriot-Watt Petroleum Engineering Institute said "The problem for the North Sea is maintaining that it is still a viable place. You won't find oil if you stop drilling wells". A likely continuing decline in the North Sea Oil sector will reduce demand for office space.

Take up of office space in Glasgow, 336,104 ft<sup>2</sup> in the 6 month period to September 2003, is below that of the previous year, but above the previous 6 month period, unlike Edinburgh and Aberdeen. Supply has risen steadily but is about a third lower than the peak in the early 1990's. Ryden report asking rents as stable at £22 ft<sup>2</sup>, but subject to incentives. Several new developments are nearing completion including the 270,000 ft<sup>2</sup> first stage for the new Broomielaw development on the Clyde, and several more at an earlier stage. Enterprise Glasgow is promoting the City as a financial services centre but until there is a substantial recovery in this sector demand will probably be insufficient to increase rents.

The London office markets have had a torrid time since they peaked in early 2001 with all rents falling 20% to 30%. Jones Lang La Salle ("JLL") report that in the City and Docklands vacancy rates are nearly 15%, a similar level in the City to that of 1993, and City rents are expected to fall further. The West End market is stronger where supply has stabilised at 7% and take-up has increased and JLL forecast that the bottom of this cycle is approaching and that rents should rise in 2005.

Over the last year the CBRE All Property Index has shown a fall in rents but no change in yield. Unsurprisingly the office market has been the worst performing sector with rents falling and yield rising. Industrials and shops have been broadly unchanged and only retail warehouses have improved showing both limited rental growth and a small fall in yield. However the rental value of All Property and of all sectors except retail warehouses remains lower in real terms than those in May 1990, the approximate peak of the last cycle. Moreover in 1990 the Hillier Parker All Property yield was 7.6% but the successor CBRE index on the Hillier Parker basis is now 8.1%. Thus the "All Property" real rental has fallen over the cycle while the investment value of those rents has fallen, a doubly poor performance. Since 1990 property yields have risen 0.5% point although 10 year Gilts have fallen about 7.5% points.

The Irishman, on being asked the way to Tipperary, famously said "Well if I was going to Tipperary, I wouldn't be starting from here". Returns from property depend on the starting position. After the 1990 crash the property market turned in 1993 and since then as the IPD figures demonstrates has given excellent returns. Thus notwithstanding the indifferent performance of property since 1990 and over the last year, increased private investor investment in commercial property is widely reported in a variety of forms. This has been encouraged and facilitated by many factors including severe falls in the equity markets, pensions and endowment insurance shortfalls, concerns on the quality of reported earnings, headline company failures and the increased availability of property investment vehicles and of SIPPs. In contrast to the equity bear market, property has been perceived as giving a "safe long-term yield" and in many cases until now a yield above the cost of borrowing. The increased demand of retail investors has reduced the yield on secondary investment stock and investors in this sector have experienced better returns than those indicated in the CBRE analysis which reports on a "prime synthetic" portfolio. However, CBRE consider there "to be inadequate differential between stocks of differing investment quality, particularly from private buyers . . .". In particular, market reports are that many non traditional investors are buying income, usually secure income, but under conditions where the long-term capital values are likely to be impaired: "jam today".

However these highly geared syndicates will be finding such purchases much less attractive and much more difficult to finance, as they are so dependent on debt. Five year swap rates, an important financing instrument in this market, which were under 4% in June 2003 are now c5.25% increasing interest costs excluding the margin by 31%. Bank debt, the main source of funding, has risen by 21% per annum for the last 5 years and real estate's share of lending has increased from 10.6% in 1997 to 19.9% in early 2003. When Bank policy

## Chairman's Statement (continued)

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changes, funding will be reduced, reinforcing the effect of rising swap rates, and demand for such investments, backed by high debt levels, will fall. In consequence yields on the secondary and debt driven and associated markets will return to their historic position relative to the prime and traditional markets. The prime market in many sectors is cyclically depressed, especially for offices, and should recover but the most recent general recovery did not exceed the real value of the previous cycle. Thus the last cycle has been one that favoured "trading investors" who bought early and sold before the next downswing.

The next property cycle seems likely to be similar to the last one. Economic growth should increase demand for space leading to increased rents. However, in most instances extra supply is readily available due to the present acceptance of a much wider range of location by office occupiers and the usual generous supply of industrial and warehousing sites within acceptable distances. Even retail supply has been relatively generous until recently except for supermarkets and retail warehouses which have as a result become so valuable or unobtainable that the expansion of these outlets is inhibited and the site value has grown rapidly. Thus in most traditional property sectors supply is now more elastic, albeit with a time lag due to the long production cycle time. In the circumstances there is little scarcity value and value is largely dictated by the marginal cost of supply.

Obsolescence is a now major cost. For instance New Town Edinburgh properties served several generations as offices, being refurbished at each change, but are now considered unsuitable for most occupiers. Similarly some "state of the art" 1970s buildings have structural or design characteristics that make them unsuitable and even those without such deficiencies require large investment, particularly in services, to bring them up to acceptable, but never top grade, specification. Landlords' interests have also been damaged by the difficulty in obtaining full FRI leases and at termination, implementing them. Their extra costs are at present borne largely by the owners of the property. As a result of these changes in the market, returns from investment property are becoming relatively less attractive.

The housing market continues to offer the likelihood of high returns on investment. In the Edinburgh area, for instance, households are expected to rise by 65,600 in the 15 years to 2015 or by 19.3%, but supply restrictions are severe. In the City Centre only a few sites remain, mainly brownfield ones or a dwindling number of office reconversions. Outside the City Centre development continues on the very few remaining gap sites and redevelopment occurs on some industrial and commercial premises. Very large developments including about 5000 houses each are proposed at Granton in North Edinburgh centred on the former Gas Works site and in the South East Wedge, an area inside the City Bypass in South Edinburgh and North Midlothian. Further away, large housing estates are being added to existing settlements usually near good road or rail links where they sell for up to 40% less than similar centrally located houses. Historically these very large scale developments fall behind schedule. For example the initial South East Wedge study reported in December 1998 and envisaged adoption of the relevant two local plans in October 2001. More than two years later Shawfair, the more advanced local plan, awaits adoption and the South East Edinburgh plan awaits the report of the Public Inquiry. These delays are due to the convoluted planning system, the need to "consult" more widely and for longer, and the need to reconcile or decide between ever more organised and vocal and often competing interests groups: the LSE is reported as saying "The fundamental problem is that 'the richer we are, the nimbier we become'". Such delays, which seem likely to continue, will constrain the supply of houses and increase their price.

Glasgow's households are expected to increase by 38,540 over this period. The city has a huge reserve of brownfield sites over an extensive area available for development but as in Edinburgh, suitable land close to the City Centre is scarce. Our site on West Street is already very close to the centre and will become ever more accessible when the pedestrian bridge "Neptune's Way" is completed in 2007 linking Tradeston to the Broomielaw, Glasgow's "Square Kilometre" .

### Future Progress

The Group should make a satisfactory profit in the current year. Rental income will continue to fall due to our much reduced investment portfolio and vacancies at prospective development properties, but development

## Chairman's Statement (continued)

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profits from residential property sales will more than compensate for this fall. The full outcome for the financial year will depend crucially on any net change in valuation.

We continue to pursue our claim for over £4m against the Scottish Ministers for dilapidations at St Margaret's when the lease determined on 28 November 2002. A restricted proof was heard in the Court of Session earlier this month and the outcome is awaited. Our future interests are concentrated on the acquisition or creation of development opportunities, realisable within a five year period. The mid-market price is currently 115p, a disappointing discount of 32.6% to the NAV of 170.6p. The Board recommends a final dividend of 1.1p and we intend to increase the dividend at a pace consistent with profitability and with consideration for other opportunities.

No tax is provided for in the current year. The Group currently has losses and allowances of almost £1m of which trading losses of over £0.2m will be allowable against development profits.

### **Conclusion**

Prospects for UK economic growth over the next year are good and should exceed 2.5% unless the current house price bubble deflates quickly and widely. In Scotland growth will continue at a lower rate than the UK but the predominantly service-based Edinburgh economy should equal the UK performance.

The Group's portfolio comprises mostly potential developments in areas with excellent prospects. The Group has substantial cash reserves to effect these developments, to acquire others and to take advantage of opportunistic investments. I envisage continued growth in NAV with the level of profitability dependent on the timing of developments or transactions.

I. D. LOWE

Chairman

18 December 2003

## Directors' Report

The directors present their report together with the audited financial statements of the Company and of the Group for the year ended 30 June 2003.

### Review of year

The results for the year before taxation are a profit of £502,870 (2002 – £3,621,729).

### Principal activities

The Group is principally engaged in property investment holding and development. Additions to and disposals of properties are shown in note 8 to the financial statements.

### Results and dividends

The Group profit for the year after taxation amounted to £507,967. The Group's activities comprise one geographical segment and three classes of business. An interim dividend of 1.0p (2002 – 0.5p) was paid during the year and the directors propose the payment of a final dividend of 1.1p (2002 – 1.0p) per ordinary share.

### Fixed assets

The movements in tangible fixed assets during the year and details of the differences between book and market values of land and buildings are set out in notes 8 and 9 to the financial statements.

### Share capital

On 18 December 2003 the following were registered as being interested in 3% or more of the Company's ordinary share capital:

	No. of shares	Percentage held
Aberdeen City Council Superannuation Fund	349,991	3.0

I. D. Lowe and M. J. Baynham have interests amounting to more than 3% of the Company's ordinary share capital, details of which are disclosed below.

### Directors

The directors who held office during the year and their interests in the Company's share capital are set out below:

#### Beneficial interests – Ordinary Shares of 20p each

	Percentage held	18 December 2003	30 June 2003	30 June 2002
I. D. Lowe	78.8	9,064,582	9,064,582	9,064,582
M. J. Baynham	4.5	520,191	520,191	520,191
B. J. Rankin	0.9	100,000	100,000	100,000
J. N. Little	0.1	16,250	16,250	16,250

#### Beneficial interests – 7.5% convertible unsecured loan stock 1994/2004

I. D. Lowe	0.0	—	—	£1,116,000
M. J. Baynham	0.0	—	—	£18,069
J. N. Little	0.0	—	—	£15,000
Keepname Limited	0.0	—	—	£250,000

B. J. Rankin is a Director and Shareholder in Keepname Limited.

## Directors' Report (continued)

Options have been granted to directors to subscribe for ordinary shares under the terms of The Executive Share Option Scheme as follows:

Option holder	No of shares at 30 June 2002	Options exercised during year	Options granted during year	No of shares at 30 June 2003	Subscription price
I. D. Lowe	60,000	—	—	60,000	60.0p
I. D. Lowe	200,000	—	—	200,000	67.5p
M. J. Baynham	60,000	—	—	60,000	60.0p
M. J. Baynham	150,000	—	—	150,000	67.5p

The options to subscribe for shares at 67.5p can be exercised from 24.3.1998 to 24.3.2005 and the options to subscribe for shares at 60p can be exercised from 8.4.2000 to 8.4.2007.

At 30 June 2003 the Company's share prices was 90.0p, which was also the lowest price reached during the year. The highest price during the year was 123.5p at 1 July 2002.

### Suppliers

It is the Company's policy to settle suppliers' invoices within 60 days of their receipt. There were 10 days billings from suppliers outstanding at the year-end.

### Auditors

In accordance with Section 384 of the Companies Act 1985, a resolution for the re-appointment of KPMG Audit Plc as auditors of the Company is to be proposed at the forthcoming Annual General Meeting.

St Ann's Wharf  
112 Quayside  
Newcastle upon Tyne  
NE99 1SB

By order of the board  
  
M. J. BAYNHAM  
Secretary  
18 December 2003

## Statement of Directors' Responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and Group and of the profit or loss for that period. In preparing those financial statements, the directors are required to:

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

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

# Independent Auditors' Report

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*To the members of Caledonian Trust PLC*

**kpmg**

KPMG Audit Plc  
Saltire Court  
20 Castle Terrace  
Edinburgh  
EH1 2EG

We have audited the financial statements on pages 13 to 28.

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 are responsible for preparing the directors' report and, as described on page 11, the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the group is not disclosed.

We read the other information accompanying the financial statements and consider whether it is consistent with those statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

## **Basis of opinion**

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

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

## **Opinion**

In our opinion the financial statements give a true and fair view of the state of affairs of the company and the group as at 30 June 2003 and of the profit of the group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc  
Chartered Accountants  
Registered Auditor  
18 December 2003

## Consolidated Profit and Loss Account

for the year ended 30 June 2003

	Note	2003 £	2002 £
<b>INCOME – CONTINUING OPERATIONS</b>			
Rents and service charges		962,587	2,730,696
Trading property sales		360,000	—
Other trading sales		367,243	340,328
		<u>1,689,830</u>	<u>3,071,024</u>
<b>OPERATING COSTS</b>			
Property rental outgoings		—	(99,644)
Cost of trading property sales		(160,330)	—
Cost of other sales		(346,761)	(396,129)
Administrative expenses	2	(669,265)	(816,113)
		<u>(1,176,356)</u>	<u>(1,311,886)</u>
<b>OPERATING PROFIT</b>			
		513,474	1,759,138
Profit on disposal of investment property		—	2,589,353
Gain on sale of fixed assets		10,169	—
Interest receivable		344,264	158,527
Interest payable	3	(365,037)	(885,289)
<b>PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION</b>			
		502,870	3,621,729
Taxation	6	5,097	(384,151)
<b>PROFIT FOR THE FINANCIAL YEAR</b>			
DIVIDENDS	7	(241,716)	(172,667)
<b>RETAINED PROFIT FOR THE FINANCIAL YEAR</b>			
Earnings per ordinary share	19	<u>4.41p</u>	<u>27.56p</u>
Diluted earnings per ordinary share	19	<u>4.24p</u>	<u>24.96p</u>
<b>PROFIT FOR THE FINANCIAL YEAR IS RETAINED AS FOLLOWS:</b>			
In holding company		221,669	691,110
In subsidiaries		44,582	2,373,801
		<u>266,251</u>	<u>3,064,911</u>

All activities of the Group are continuing.



## Statement of Total Recognised Gains and Losses

for the year ended 30 June 2003

	2003 £	2002 £
Profit for the financial year	507,967	3,237,578
Unrealised surplus on revaluation of properties	556,575	450,000
Taxation arising on disposal of previously revalued property	—	(860,849)
Total gains recognised since the last annual report	<u>1,064,542</u>	<u>2,826,729</u>

## Note of Historical Cost Profits and Losses

for the year ended 30 June 2003

	2003 £	2002 £
Reported profit on ordinary activities before taxation	502,870	3,621,729
Realised surplus on previously revalued property	—	7,534,683
Historical cost profit on ordinary activities before taxation	502,870	11,156,412
Taxation on profit for year	5,097	(384,151)
Taxation in respect of previously revalued property	—	(860,849)
Historical cost profit for the year after taxation	<u>507,967</u>	<u>9,911,412</u>
Historical cost profit for the year retained after taxation	<u>266,251</u>	<u>9,738,745</u>

## Consolidated Balance Sheet

at 30 June 2003

	Note	2003		2002	
		£	£	£	£
<b>FIXED ASSETS</b>					
Tangible assets:					
Investment properties	8		18,607,844		14,404,759
Other assets	9		8,575		10,439
			<u>18,616,419</u>		<u>14,415,198</u>
Investments	10		20		20
			<u>18,616,439</u>		<u>14,415,218</u>
<b>CURRENT ASSETS</b>					
Debtors	11	306,648		2,532,398	
Cash at bank and in hand	12	5,233,211		8,762,235	
		<u>5,539,859</u>		<u>11,294,633</u>	
CREDITORS: Amounts falling due within one year	13	(2,215,551)		(3,830,372)	
			<u>3,324,308</u>		<u>7,464,261</u>
<b>NET CURRENT ASSETS</b>					
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>					
			<u>21,940,747</u>		<u>21,879,479</u>
CREDITORS: Amounts falling due after more than one year	13		(2,302,500)		(3,064,058)
			<u>19,638,247</u>		<u>18,815,421</u>
<b>NET ASSETS</b>					
<b>CAPITAL AND RESERVES</b>					
Called up share capital	14		2,302,053		2,302,053
Share premium account	15		2,530,753		2,530,753
Capital redemption reserve	15		155,846		155,846
Revaluation reserve	15		563,460		6,885
Profit and loss account	15		14,086,135		13,819,884
			<u>19,638,247</u>		<u>18,815,421</u>
<b>SHAREHOLDERS' FUNDS – EQUITY</b>					
			<u>19,638,247</u>		<u>18,815,421</u>

These financial statements were approved by the Board of Directors on 18 December 2003 and were signed on its behalf by:

I. D. LOWE

Director

## Company Balance Sheet

at 30 June 2003

	Note	2003 £	£	2002 £	£
<b>FIXED ASSETS</b>					
Tangible assets:					
Investment properties	8	4,578,156		3,800,000	
Equipment and vehicles	9	5,055		9,439	
		4,583,211		3,809,439	
Investments	10	13,237,075		15,297,884	
		17,820,286		19,107,323	
<b>CURRENT ASSETS</b>					
Debtors	11	10,841,349		6,821,500	
Cash at bank and in hand	12	5,135,560		8,354,951	
		15,976,909		15,176,451	
CREDITORS: Amounts falling due within one year	13	(12,856,448)		(12,324,295)	
NET CURRENT ASSETS		3,120,461		2,852,156	
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>					
		20,940,747		21,959,479	
CREDITORS: Amounts falling due after more than one year	13	(1,302,500)		(3,064,058)	
NET ASSETS		19,638,247		18,895,421	
<b>CAPITAL AND RESERVES</b>					
Called up share capital	14	2,302,053		2,302,053	
Share premium account	15	2,530,753		2,530,753	
Capital redemption reserve	15	155,846		155,846	
Revaluation reserves					
Property	15	1,199,256		617,290	
Investments	15	3,384,838		5,445,647	
Profit and loss account	15	10,065,501		7,843,832	
SHAREHOLDERS' FUNDS – EQUITY		19,638,247		18,895,421	

These financial statements were approved by the Board of Directors on 18 December 2003 and were signed on its behalf by:

I. D. LOWE  
Director

## Consolidated Cash Flow Statement

for the year ended 30 June 2003

	Note	2003 £	2002 £
NET CASH INFLOW FROM OPERATING ACTIVITIES	(a)	691,545	1,972,072
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE	(b)	(62,658)	(808,758)
CORPORATION TAX		(769,902)	(450,000)
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT	(b)	(1,387,610)	18,994,560
EQUITY DIVIDENDS PAID		(230,206)	(117,653)
CASH (OUTFLOW)/INFLOW BEFORE MANAGEMENT OF LIQUID RESOURCES AND FINANCING		(1,758,831)	19,590,221
FINANCING	(b)	(1,760,193)	(12,197,601)
(DECREASE)/INCREASE IN CASH IN PERIOD		<u>(3,519,024)</u>	<u>7,392,620</u>
RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET DEBT	(c)	£	£
(DECREASE)/INCREASE IN CASH IN PERIOD		(3,519,024)	7,392,620
Cash outflow from decrease in debt		1,760,193	11,699,736
MOVEMENT IN NET DEBT IN THE PERIOD		(1,758,831)	19,092,356
NET DEBT AT THE START OF THE PERIOD		3,512,059	(15,580,298)
NET DEBT AT THE END OF THE PERIOD		<u>1,753,228</u>	<u>3,512,058</u>

## Notes to the Cash Flow Statement

### (a) RECONCILIATION OF OPERATING PROFIT TO NET CASH INFLOW FROM OPERATING ACTIVITIES

	2003 £	2002 £
Operating profit	513,474	1,759,138
Profit on disposal of property	(200,000)	538,102
Depreciation charges	4,384	12,717
Decrease/(increase) in debtors	174,500	(266,189)
(Decrease)/increase in creditors	199,187	(71,696)
Net cash inflow from operating activities	<u>691,545</u>	<u>1,972,072</u>

### (b) ANALYSIS OF CASH FLOWS

	2003 £	2003 £	2002 £	2002 £
RETURNS ON INVESTMENT AND SERVICING OF FINANCE				
Interest received	344,265		158,527	
Interest paid	(406,923)		(967,285)	
		<u>(62,658)</u>		<u>(808,758)</u>
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT				
Purchase of tangible fixed assets	(3,809,029)		(194,907)	
Sale of investment property	2,411,250		19,189,467	
Sale of fixed assets	10,169		—	
		<u>(1,387,610)</u>		<u>18,994,560</u>
FINANCING				
Purchase of ordinary share capital	—		(497,865)	
Debt due within a year				
(Decrease)/increase in short-term	(998,635)		(11,536,331)	
Debt due beyond a year				
Increase/(decrease) in long-term	(761,558)		(163,405)	
		<u>(1,760,193)</u>		<u>(12,197,601)</u>

## Notes to the Cash Flow Statement (continued)

### (c) ANALYSIS OF NET DEBT

	At beginning of year £	Cash flow £	Other non-cash changes £	At end of year £
Cash at bank and in hand	8,762,235	(3,529,024)	—	5,233,211
Overdrafts	(109,729)	10,000	—	(99,729)
		<u>(3,519,024)</u>		
Debt due after one year	(3,064,058)	761,558	—	(2,302,500)
Debt due within one year	(2,076,389)	998,635	—	(1,077,754)
		<u>1,760,193</u>		
TOTAL	<u>3,512,059</u>	<u>(1,758,831)</u>	<u>—</u>	<u>1,753,228</u>

# Notes (forming part of the financial statements)

30 June 2003

## 1 ACCOUNTING POLICIES

The following are the main accounting policies of the Group:

- (a) **Basis of preparation**  
 The financial statements are prepared under the historical cost convention as modified by the revaluation of certain tangible fixed assets and in accordance with applicable accounting standards. The Company has not presented its own profit and loss account in accordance with section 230 of the Companies Act 1985.
- (b) **Basis of consolidation**  
 The consolidated financial statements combine the results of the Company and its subsidiary undertakings for the year ended 30 June 2003, and reflect events occurring up until the date of approval of the financial statements.
- (c) **Goodwill**  
 Negative goodwill purchased prior to the implementation of Financial Reporting Standard 10 has been transferred to the profit and loss reserve and is credited to the profit and loss account on subsequent disposal of the business or assets to which it relates.
- (d) **Income**  
 Rental income represents rent and service charges receivable without taking into account any expenditure borne direct by tenants.
- (e) **Properties**  
 Properties held by the Group are classified within fixed assets, as either investment properties or properties held for development, or current assets if held as trading stock.
- Investment properties**  
 Investment properties are stated at their open market valuation at the balance sheet date, valued either by the directors or by independent professional advisers. Independent professional valuations are prepared at least once every three years.  
 Surpluses or deficits arising on revaluations are taken to the revaluation reserve except in the case of deficits which are considered to be permanent which are taken to the profit and loss account. The revaluation reserve is not distributable.  
 On disposal of an investment property the profit and loss account includes the effect of comparing sales proceeds and the book amount of the asset sold. Any previous revaluation surplus or deficit realised on disposal is transferred from revaluation reserve to accumulated profit and loss reserves.
- Properties held for development**  
 Properties held for development are shown at open market valuation at the balance sheet date as described above. When development commences, costs of such development (including interest thereon) are aggregated in the book amount provided that the anticipated overall book amount following completion would not exceed the anticipated valuation of the property at that date.
- Properties held as stock**  
 Properties held as trading stock are stated at the lower of cost or net realisable value.
- (f) **Investments**  
 Investments in subsidiary undertakings are included in the balance sheet of the Company at net asset value of the undertaking concerned.
- (g) **Depreciation**  
 In accordance with SSAP 19 no depreciation or amortisation is provided in respect of freehold investment properties (including investment properties held for development) or leaseholds with over twenty years to run, including equipment therein. This treatment, as regards certain of the Group's investment properties, may be a departure from the requirements of the Companies Act concerning depreciation of fixed assets. However, these properties are not held for consumption but for investment and the directors consider that systematic annual depreciation would be inappropriate. The accounting policy adopted is therefore necessary for the financial statements to give a true and fair view. Depreciation or amortisation is only one of the many factors reflected in the annual valuation and the amount, which might otherwise have been shown, cannot be separately identified or quantified.  
 Other tangible fixed assets are depreciated by equal instalments over their estimated useful lives at the following rates:
- |                       |          |
|-----------------------|----------|
| Fixtures and fittings | 10%      |
| Office equipment      | 11 – 33% |
| Motor vehicles        | 33½%     |
- (h) **Taxation**  
 The charge for taxation is based on the profit for the tax year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

**Notes** *(continued)*

30 June 2003

2	ADMINISTRATIVE EXPENSES	2003	2002
		£	£
	Directors' emoluments (see note 4)	271,474	263,165
	Management expenses	366,270	512,581
	Auditors' remuneration		
	—audit – company	10,000	9,500
	—audit – subsidiaries	11,887	9,650
	—non audit	5,250	8,500
	Depreciation	4,384	12,717
		<u>669,265</u>	<u>816,113</u>

3	INTEREST PAYABLE	2003	2002
		£	£
	Bank loans and overdrafts	236,672	720,039
	Loan stock repayable within five years	128,365	165,250
		<u>365,037</u>	<u>885,289</u>

4	REMUNERATION OF DIRECTORS	2003	2002
		£	£
	Directors' emoluments	230,474	225,165
	Company contributions to money purchase pension schemes	40,965	38,000
		<u>40,965</u>	<u>38,000</u>

The aggregate of emoluments and amounts receivable under long term incentive schemes of the highest paid director was £112,491 (2002 – £106,800), and Company pension contributions of £20,465 (2002 – £20,000) were made to a money purchase scheme on his behalf.

		Number of directors	
		2003	2002
	Retirement benefits are accruing to the following number of directors under:		
	Money purchase schemes	<u>2</u>	<u>2</u>
	The number of directors who exercised share options was	<u>—</u>	<u>—</u>
	The number of directors in respect of whose services shares were received or receivable under long-term incentive schemes was	<u>2</u>	<u>2</u>

5	EMPLOYEES		
	The average number of persons, including directors, employed by the Group during the year was:		
		2003	2002
		Number	Number
	Management	4	4
	Administration	2	2
	Other	15	19
		<u>21</u>	<u>25</u>

	The aggregate payroll costs of these persons were as follows:		
		2003	2002
		£	£
	Wages and salaries	406,605	384,809
	Social security costs	29,724	37,399
	Other pension costs	40,965	40,320
		<u>477,294</u>	<u>462,528</u>



## Notes *(continued)*

30 June 2003

6 TAXATION	2003	2002
	£	£
Analysis of change in period:		
UK corporation tax		
Current tax on income for the period	—	1,245,000
Overprovision in respect of previous year	(5,097)	—
Less: charged to prior years in respect of revaluation realised	—	(860,849)
Tax on profit on ordinary activities	<u>(5,097)</u>	<u>384,151</u>
Current tax reconciliation		
	2003	2002
	£	£
Profit on ordinary activities before tax	<u>502,870</u>	<u>3,621,729</u>
Current tax at 30%	150,861	1,086,518
Effects of:		
Expenses not deductible for tax purposes	5,574	12,361
Capital allowances for period in excess of depreciation	(55,037)	(819,715)
Capital gains tax indexation	—	(1,298,085)
Utilisation of tax losses	(101,398)	—
Prior year revaluations	—	2,258,823
	(150,861)	153,384
Tax over/(under) provision	(5,097)	5,098
Tax charged to prior years in respect of revaluation realised	—	(860,849)
Total current tax charge (see above)	<u>(5,097)</u>	<u>384,151</u>
7 DIVIDENDS	2003	2002
	£	£
Interim dividend for year 1.0p (2002 – 0.5p) per share	115,103	57,564
Final dividend for year 1.1p (2002 – 1.0p) per share	126,613	115,103
	<u>241,716</u>	<u>172,667</u>

## Notes (continued)

30 June 2003

## 8 INVESTMENT PROPERTIES

	Group £	Freehold Company £
Investment properties:		
Valuation at 1 July 2002	10,300,000	3,800,000
Revaluation in year	581,966	581,966
Acquired in year	2,565,299	18,034
Valuation at 30 June 2003	<u>13,447,265</u>	<u>4,400,000</u>
Properties held for development:		
Valuation at 1 July 2002	4,104,759	—
Revaluation in year	(25,390)	—
Sold in year	(160,000)	—
Purchased in year	627,604	178,156
Additions in year	613,606	—
Revaluation surplus arising in year	—	—
Valuation at 30 June 2003	<u>5,160,579</u>	<u>178,156</u>
Net book amount at 30 June 2003	<u>18,607,844</u>	<u>4,578,156</u>
Net book amount at 1 July 2002	<u>14,404,759</u>	<u>3,800,000</u>

Investment properties and properties held for development have been stated at directors' valuation at the balance sheet date based on independent valuations at open market value made by Montagu Evans at 30 June 2003.

The historical cost of properties included at valuation is as follows:

	Group		Company	
	2003 £	2002 £	2003 £	2002 £
Investment properties	<u>17,274,853</u>	<u>13,628,344</u>	<u>2,916,183</u>	<u>2,719,993</u>

The cumulative amount of interest capitalised in respect of the Group's investment properties is £989,121 (2002 – £989,121). The cumulative amount of such interest capitalised for the Company is £462,717 (2002 – £462,717).

## 9 OTHER ASSETS

	Motor vehicles £	Office equipment £	Total £
GROUP			
Cost at 1 July 2002	47,860	192,556	240,416
Sold in year	(35,110)	—	(35,110)
Additions in year	—	2,520	2,520
Cost at 30 June 2003	<u>12,750</u>	<u>195,076</u>	<u>207,826</u>
Depreciation at 1 July 2002	39,359	190,618	229,977
Charged in year	4,250	134	4,384
Sold in year	(35,110)	—	(35,110)
Depreciation at 30 June 2003	<u>8,499</u>	<u>190,752</u>	<u>199,251</u>
Net book amount at 30 June 2003	<u>4,251</u>	<u>4,324</u>	<u>8,575</u>
Net book amount at 1 July 2002	<u>8,501</u>	<u>1,938</u>	<u>10,439</u>
COMPANY			
Cost at 1 July 2002	47,860	43,836	91,696
Sold in year	(35,110)	—	(35,110)
Cost at 30 June 2003	<u>12,750</u>	<u>43,836</u>	<u>56,586</u>
Depreciation at 1 July 2002	39,359	42,898	82,257
Sold in year	(35,110)	—	(35,110)
Charged in year	4,250	134	4,384
Depreciation at 30 June 2003	<u>8,499</u>	<u>43,032</u>	<u>51,531</u>
Net book amount at 30 June 2003	<u>4,251</u>	<u>804</u>	<u>5,055</u>
Net book amount at 1 July 2002	<u>8,501</u>	<u>938</u>	<u>9,439</u>

## Notes *(continued)*

30 June 2003

10 INVESTMENTS	Shares in subsidiary undertakings	Listed investments	Other unlisted investments	Total
	£	£	£	£
GROUP				
Cost at 1 July 2002	—	—	20	20
At 30 June 2003	—	—	20	20
COMPANY				
Cost at 1 July 2002	4,932,978	—	—	4,932,978
At 30 June 2003	4,932,978	—	—	4,932,978
Revaluation surplus at 1 July 2002	10,364,906	—	—	10,364,906
Revaluation in year	(60,809)	—	—	(60,809)
Dividend paid during year	(2,000,000)	—	—	(2,000,000)
At 30 June 2003	8,304,097	—	—	8,304,097
Net book amount at 30 June 2003	13,237,095	—	—	13,237,095
Net book amount at 1 July 2002	15,297,884	—	—	15,297,884

The Company's investment in unlisted investments is as follows:

	% held	Activity
Bedrocks Limited	19.9%	Leisure activity operator

The Company is registered in Scotland.

The Company's investments in the ordinary share capital of its principal subsidiary undertakings are included at net asset value of the undertakings which are as follows:

Subsidiary Undertaking	% held	Activity
Caledonian Scottish Developments Ltd	100%	Property Development
South Castle Properties Ltd	100%	Property Investment
Caledonian Stoneywood Ltd	100%	Investment Holding Company
Caledonian City Developments Ltd	100%	Property Development
West Castle Properties Ltd	100%	Property Investment
Melville Management Ltd	100%	Property Investment

All the principal subsidiary undertakings are registered in Scotland except Caledonian City Developments Limited and Caledonian Stoneywood Ltd, which are registered in England and Wales.

11 DEBTORS	Group		Company	
	2003	2002	2003	2002
	£	£	£	£
Amounts falling due within one year	—	—	10,828,366	6,813,928
Amounts owed by subsidiary undertakings	—	—	4,159	7,572
Other debtors	4,158	2,074,126	8,824	—
Prepayments and accrued income	302,490	458,272	—	—
	306,648	2,532,398	10,841,349	6,821,500

**Notes** *(continued)*

30 June 2003

## 12 CASH AT BANK AND IN HAND

Group bank balances totalling £75,698 (2002 – £376,269) were held by the Group's bankers as collateral against loans provided to subsidiary undertakings.

## 13 CREDITORS: Amounts falling due within one year:

	Group		Company	
	2003	2002	2003	2002
	£	£	£	£
Bank loans and overdrafts	1,177,483	2,186,118	149,729	161,289
Amounts owed to subsidiary undertakings	—	—	12,454,533	11,809,626
Final dividend	126,613	115,103	126,613	115,103
Other creditors and accruals	911,455	1,529,151	125,573	238,277
	<u>2,215,551</u>	<u>3,830,372</u>	<u>12,856,448</u>	<u>12,324,295</u>

Bank loans and overdrafts are secured on certain of the Group's properties.

## CREDITORS: Amounts falling due after more than one year:

	Group		Company	
	2003	2002	2003	2002
	£	£	£	£
Bank loans	2,302,500	1,352,500	1,302,500	1,352,500
Floating rate unsecured loan stock	—	—	—	—
7.5% convertible unsecured loan stock	—	1,711,558	—	1,711,558
	<u>2,302,500</u>	<u>3,064,058</u>	<u>1,302,500</u>	<u>3,064,058</u>

## Analysis of debt

Debt can be analysed as falling due:

	Group		Company	
	2003	2002	2003	2002
	£	£	£	£
In one year or less, or on demand	1,177,483	2,186,118	149,729	161,289
Between one and two years	1,050,000	50,000	50,000	50,000
Between two and five years	1,252,500	3,014,058	1,252,500	3,014,058
In five years or more	—	—	—	—
	<u>3,479,983</u>	<u>5,250,176</u>	<u>1,452,229</u>	<u>3,225,347</u>

Bank loans of £1,055,000 are repayable in instalments. Of this £50,000 is due within one year and is included in current liabilities. The loans are secured by standard securities and floating charges over the assets of certain subsidiaries and by an unlimited guarantee from Caledonian Trust. Interest charged on these loans is based on margins ranging from 1½% to 3% over the prevailing London Interbank Offer Rate with the exception of a mortgage loan of £300,000 at a fixed rate of 12.302%.

## Notes (continued)

30 June 2003

14 SHARE CAPITAL	No.	2003 £	No.	2002 £
Authorised:				
Ordinary shares of 20p each	<u>20,000,000</u>	<u>4,000,000</u>	<u>20,000,000</u>	<u>4,000,000</u>
Allotted, called up and fully paid:				
Ordinary shares of 20p each	<u>11,510,267</u>	<u>2,302,053</u>	<u>11,510,267</u>	<u>2,302,053</u>

15 RESERVES	Share premium account £	Revaluation reserve £	Capital redemption reserve £	Profit and loss account £	Total £
GROUP					
Balance at 1 July 2002	2,530,753	6,885	155,846	13,819,884	16,513,368
Net revaluation in year	—	556,575	—	—	556,575
Profit for the financial year	—	—	—	507,967	507,967
Dividend for year	—	—	—	(241,716)	(241,716)
Balance at 30 June 2003	<u>2,530,753</u>	<u>563,460</u>	<u>155,846</u>	<u>14,086,135</u>	<u>17,336,194</u>

	Share premium account £	Revaluation reserves Property £	Investments £	Capital redemption reserve £	Profit and loss account £	Total £
COMPANY						
Balance at 1 July 2002	2,530,753	617,290	5,445,647	155,846	7,843,832	16,593,368
Net revaluation in year	—	581,966	(60,809)	—	—	521,157
Dividend paid by subsidiary	—	—	(2,000,000)	—	2,000,000	—
Profit for the financial year	—	—	—	—	463,385	463,385
Dividend for year	—	—	—	—	(241,716)	(241,716)
Balance at 30 June 2003	<u>2,530,753</u>	<u>1,199,256</u>	<u>3,384,838</u>	<u>155,846</u>	<u>10,065,501</u>	<u>17,336,194</u>

Of the balance on Profit and Loss Account £319,812 is not distributable.

16 RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS	2003 £	2002 £
Retained profit for the financial year	266,251	3,064,911
Revaluation surplus	556,575	450,000
Taxation in respect of prior year revaluation realised	—	(860,849)
Ordinary shares bought in	—	(497,865)
Net addition to shareholders' funds	822,826	2,156,197
Opening shareholders' funds	18,815,421	16,659,224
Closing shareholders' funds	<u>19,638,247</u>	<u>18,815,421</u>

### 17 TRANSACTIONS WITH DIRECTORS

B. J. Rankin received £13,350 in respect of consultancy fees in the year in addition to his emoluments as a director.

**Notes** *(continued)*

30 June 2003

**18 EARNINGS PER ORDINARY SHARE**

The calculation of earnings per ordinary share is based on the reported profit of £507,967 (2002: £3,237,578) and on the weighted average number of ordinary shares in issue in the year, as detailed below. The calculation of diluted earnings per ordinary share is calculated adjusting the profit for the period in respect of interest on loan stock deemed to have been converted. The weighted average number of shares has been adjusted for deemed conversion of loan stock and deemed exercise of share options outstanding.

	2003	2002
Weighted average of ordinary shares in issue during year – undiluted	11,510,267	11,747,541
Weighted average of ordinary shares in issue during year – fully diluted	11,980,267	13,586,787

**19 FINANCIAL INSTRUMENTS**

The group's principal financial instruments comprise bank loans, cash and short term deposits. The main purpose of these financial instruments is to raise finance for the group's operations. The group has in addition trade debtors and trade creditors, which arise directly from its operation and are not considered in this note.

As the group operates wholly within the United Kingdom, there is currently no exposure to currency risk.

The main risks arising from the group's financial instruments are interest rate risks and liquidity risks. The board reviews and agrees policies for managing each of these risks, which are summarised below.

**INTEREST RATE RISK**

The group borrowings are at floating rates of interest based on LIBOR or Base Rate with the exception of one bank loan which is at a fixed rate.

The interest rate profile of the group's borrowings as at the year end was as follows:

	2003 £	2002 £
Fixed Rate	300,000	2,036,558
Floating Rate	3,179,983	3,213,618
	<u>3,479,983</u>	<u>5,250,176</u>

The weighted average interest rate of the fixed rate borrowings was 10.37% pa fixed for a weighted average of 2.27 years.

The weighted average interest rate of the floating rate borrowings was 5.76% pa fixed for a weighted average of 0.78 years.

The interest rate profile on the Group's financial assets was as follows:

	2003 £	2002 £
Non-interest bearing	—	—
Floating Rate	5,233,142	8,762,235
	<u>5,233,142</u>	<u>8,762,235</u>

## Notes (continued)

30 June 2003

### 19 FINANCIAL INSTRUMENTS (continued)

#### LIQUIDITY RISK

The Group's policy is to maintain a balance between continuity of funding and flexibility through loans secured on its property assets from banks and unsecured loan stocks held by third parties sufficient to enable it to meet its commitments and to make further investments.

The maturity profile of the Group's financial liabilities was as follows:

	2003 £	2002 £
In one year or less, or on demand	1,177,483	2,186,118
Between one and two years	1,050,000	50,000
Between two and five years	1,252,500	3,014,058
In five years or more	—	—
	<u>3,479,983</u>	<u>5,250,176</u>

A comparison of book values and fair values of the Group's financial assets and liabilities at 30 June 2003 is as follows:

	Book Value £	Fair value £
Fixed rate borrowings	300,000	371,450
Floating rate borrowings	3,179,983	3,179,983
Cash and short-term deposits	<u>5,233,142</u>	<u>5,233,142</u>

The fair value of the fixed rate borrowings has been arrived at by calculating the cash flows which would arise if the commitments at 30 June 2003 had been entered into at that date. The difference between such cash flows and the actual committed cash flows was then discounted at the prevailing market interest rate.

## Notice of Meeting

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NOTICE IS HEREBY GIVEN that the ANNUAL GENERAL MEETING of CALEDONIAN TRUST PLC will be held at 61 North Castle Street, Edinburgh EH2 3LJ on Friday 23 January 2004 at 12.30 pm for the following purposes:

1. To receive the Report of the Directors and the Financial Statements for the year ended 30 June 2003 and the Report of the Auditors thereon.
2. To re-appoint KPMG Audit Plc, Chartered Accountants and Registered Auditors, as Auditors and to authorise the Directors to fix their remuneration.
3. To declare a dividend.

As special business to consider and, if thought fit, pass the following Resolutions which will be proposed as Special Resolutions:

4. That the Directors be and are hereby empowered pursuant to Section 95 of the Companies Act 1985 to allot equity securities (within the meaning of Section 94 of that Act) pursuant to the authority conferred by the Ordinary Resolution of the Company passed on 19 January 2001 as if Section 89 of the Companies Act 1985 did not apply to any such allotment provided that this power shall be limited:
  - (a) to the allotment otherwise than pursuant to sub-paragraph (b) below of equity securities which are, or are to be, wholly paid up in cash having an aggregate nominal amount equal to 5% of the issued Ordinary Share capital of the Company as shown in the audited consolidated accounts of the Company and its subsidiaries for the year ended 30 June 2003; and
  - (b) to the allotment of equity securities in connection with an offer to Ordinary Shareholders in proportion (as nearly as may be) to the respective numbers of Ordinary Shares held by them, subject to the Directors having a right to aggregate and sell for the benefit of the Company all fractions of a share which may arise in apportioning equity securities among the Ordinary Shareholders of the Company and subject to such exclusions or other arrangements as the Directors may deem necessary or expedient in relation to legal or practical problems under the law of, or the requirements of, any regulatory body or any stock exchange in any overseas territory;

and shall expire on the date of the next Annual General Meeting of the Company after the passing of this Resolution provided 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 Directors may allot equity securities in pursuance of such offer or agreement as if the power hereby conferred had not expired.

5. That authority be and is hereby generally and unconditionally given pursuant to Section 166 of the Companies Act 1985, for the Company to make one or more market purchases as defined in Section 163(3) of the Companies Act 1985 of any of its own Ordinary Shares of 20p each in such manner and on such terms as the Directors may from time to time determine provided that:



## Notice of Meeting (continued)

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- (a) the authority hereby given shall, unless previously varied, revoked or renewed expire on the date of the next Annual General Meeting of the Company after the passing of this Resolution, save that the Company shall be entitled by such authority to make at any time before the expiry thereof any contract to purchase its own Ordinary Shares which would or might become effective wholly or partly after the expiry of such authority;
- (b) the maximum number of Ordinary Shares hereby authorised to be acquired is 575,500 Ordinary Shares; and
- (c) the maximum price (exclusive of expenses) to be paid for each Ordinary Share of 20p each shall not be more than 5% above the average of the middle market quotation for an ordinary share as derived from the Alternative Investment Market (or such other official market as may become admitted) of the London Stock Exchange for the five business days immediately preceding the date of purchase and the minimum price is 20p.

St Ann's Wharf  
112 Quayside  
Newcastle upon Tyne  
NE99 1SB

By Order of the Board  
M J BAYNHAM  
Secretary

18 December 2003

### *Notes*

Copies of contracts of service between Directors and the Company will be available for inspection at the head office of the Company, 61 North Castle Street, Edinburgh EH2 3LJ during business hours on any business day from the date of this notice until 22 January 2004 and also for fifteen minutes prior to and throughout the meeting.

The register of Directors' shareholdings and transactions will be available for reference at the commencement of, and during the continuance of, the Annual General Meeting.

A member entitled to attend and vote at this meeting is entitled to appoint one or more proxies to attend and vote in his place. A proxy need not be a member of the Company.

A form of proxy is enclosed for the use of Ordinary Shareholders. If you do not intend being present at the meeting, please complete the form of proxy, sign it and return it so as to reach the Company at least forty-eight hours before the time of the meeting.

