The **Scottish Oriental**
Smaller Companies Trust PLC

# 2011

The **Scottish Oriental** Smaller Companies Trust PLC

Annual
Report and Accounts **2011**

## Contents



# Annual Report and Accounts 2011

This document is important and requires your immediate attention. If you are in any doubt as to what action you should take, you are recommended to seek your own financial advice from your stockbroker, solicitor, accountant or other independent professional adviser authorised under The Financial Services and Markets Act 2000 immediately. If you have sold or otherwise transferred all of your shares in The Scottish Oriental Smaller Companies Trust plc, please forward this document, together with the accompanying form of proxy, as soon as possible to the purchaser or transferee or to the stockbroker, bank or other agent through whom the sale or transfer was effected for transmission to the purchaser or transferee.

# Financial Highlights

## Performance *for the year ended 31st August 2011*

| | | | |
|---|---|---|---|
| Net Asset Value | 11.4% | MSCI AC Asia ex Japan Index (£)* | 3.7% |
| Share Price | 24.1% | MSCI AC Asia ex Japan Small Cap Index (£)* | -0.5% |
| * Total return (capital return with dividends reinvested) | | FTSE All-Share Index (£)* | 7.3% |

## Summary Data *at 31st August 2011*

| | | | |
|---|---|---|---|
| Shares in issue | 30,213,650 | Shareholders' Funds | £186.89m |
| | | Market Capitalisation | £181.28m |
| Net Asset Value per share | 618.56p | Share Price Discount to Net Asset Value | 3.0% |
| Share Price | 600.00p | | |

# Benchmark and Comparative Indices

From inception in March 1995 until October 1999, the Trust adopted the Morgan Stanley Capital International AC Asia ex Japan Index ("MSCI") as its benchmark. No suitable regional smaller companies index was available at that time.

In October 1999 the Directors agreed to the replacement of the MSCI with the SG Asian (ex Japan) Smaller Companies Index, following its reconstitution to cover previously excluded countries. Unfortunately, this Index ceased to be available from the end of 2002.

In 2003 the Directors agreed to revert to the MSCI as the Trust's benchmark. This Index, being dominated by larger companies, is far from ideal as a performance measurement tool. It has, however, the dual merit of being the most widely recognised regional index and of pre-dating the inception of the Trust.

For comparative purposes we are also displaying the MSCI AC Asia ex Japan Small Cap Index, which covers the relevant markets with the exception of Pakistan and Sri Lanka. This Index is made up of companies with a market capitalisation of between US$200m and US$800m. The range does not exactly match that of the Trust, which has no lower limit and which mainly invests in companies with a market capitalisation of under US$1,000m. Nevertheless, it gives a useful indication of the performance of smaller companies in Asia over recent years.

As most investors in the Trust are based in the United Kingdom, the Directors consider that it is also relevant to compare the Trust's performance to that of the FTSE All-Share Index.

## Investment Policy and Objective

- The Scottish Oriental Smaller Companies Trust PLC ("Scottish Oriental", "the Company" or "the Trust") aims to achieve long-term capital growth by investing in mainly smaller Asian quoted companies.
- The Trust invests mainly in the shares of smaller Asian quoted companies, that is companies with market capitalisations of below US$1,000m, or the equivalent thereof, at the time of first investment.
- The Trust may also invest in companies with market capitalisations of between US$1,000m and US$2,000m at the time of first investment, although not more than 20 per cent of the Trust's net assets at the time of investment will be invested in such companies.
- To enable the Trust to participate in new issues, it may invest in companies which are not quoted on any stock exchange, but only where the Investment Manager expects that the relevant securities will shortly become quoted.
- For investment purposes, the investment Region includes China, Hong Kong, India, Indonesia, Malaysia, Pakistan, Philippines, Singapore, South Korea, Sri Lanka, Taiwan, Thailand and Vietnam. Countries in other parts of Asia may be considered with approval of the Board.
- With the objective of enhancing capital returns to shareholders, the Directors of the Trust will consider the use of long term borrowings up to a limit of 50 per cent of the net assets of the Trust at the time of borrowing.
- The Trust invests no more than 15 per cent of its gross assets in other listed investment companies (including listed investment trusts).
- The Trust invests no more than 15 per cent of its total assets in the securities of any one company or group of companies at the time of investment.
- The Trust reserves the right to invest in equity-related securities (such as convertible bonds and warrants) of companies meeting its investment criteria. In the event that the Investment Manager anticipates adverse equity market conditions, the Trust may invest in debt instruments in any country or currency.
- The majority of the Trust's assets are denominated in Asian currencies or US dollars. The Trust reserves the right to undertake foreign exchange hedging of its portfolio.

A portfolio review by the Investment Manager is given on pages 10 to 14 and the investments held at the year end are listed on pages 15 and 16.

## Investment Statement

- We aim to maximise the rate of return with due regard to risk. Risk is principally contained by focusing on soundly managed and financially strong companies, and by ensuring that the portfolio is reasonably well diversified geographically and by sector at all times. Quantitative analysis demonstrating the diversification of the Trust's portfolio of investments is contained in the country allocation and sector allocation analysis within the Portfolio Review.
- While cultural, political, economic and sectoral influences play an important part in the decision-making process, the availability of attractively-priced, good quality companies with solid long-term growth prospects is the major determinant of investment policy.
- Our country weightings bear no relationship to regional stock market indices. We do not consider ourselves obliged to hold investments in any individual market, sector or company.
- Existing holdings are carefully scrutinised to ensure that our corporate performance expectations are likely to be met, and that market valuations are not excessive. Where otherwise, disposals are made.
- Strong emphasis is placed on frequent visits to countries of the Region and on meeting the management of those companies in which the Trust is invested, or might invest.

# Chairman's Statement

Scottish Oriental had another good year. The net asset value increased by 11.4 per cent over the 12 months and the share price by 24.1 per cent. The MSCI AC Asia ex Japan Index rose by 3.7 per cent.

Earnings per share have increased again, being 11.39p compared to 10.58p last year. This rise was a result of continuing strong dividend growth from our investments. We are proposing a dividend of 9.0p net, an increase of 5.9 per cent. The undistributed balance of £724,000 will be added to the revenue reserve, as set out on page 40. It remains our intention at least to maintain this level of dividend, using our reserves if necessary.

A performance fee was earned for the second year in succession. The details of the fee, which is based on the Company's share price total return over a three year period, are set out on page 21. When this fee was established in September 2005, the rate of the base fee was reduced; it is 0.75 per cent per annum at present. The base fee is charged to income whereas the performance fee is charged to capital. Scottish Oriental's total expense ratio for the year was 1.01 per cent (2010: 1.00 per cent), but if the performance fee were to be included it would rise to 2.29 per cent (2010: 1.65 per cent). Up to the end of the last financial year, no deduction was made from the net asset value for the performance fee until it was earned at the end of the Trust's year. We have changed our policy on this and now an accrual is deducted from the net asset value that is released daily.

The transfer of our secretarial arrangements to Personal Assets Trust Administration Company Limited, about which I wrote last year, became effective on 1st March 2011. The transfer was carried out smoothly which is a tribute to both First State and our new secretarial team. We would like to re-iterate our thanks to those at First State and their predecessors for the secretarial service that they provided from the foundation of the Company.

We announced on 15th August 2011 that Scottish Oriental had borrowed US$32.5 million (£19.8 million) for 3 years at an interest cost of 2.19 per cent per annum. Our managers have not rushed to invest this money in the present turbulent conditions, but they are looking for suitable opportunities in the belief that they will be able to achieve a yield that is greater than the cost of borrowing. The present yield on our existing equity portfolio is 3.6 per cent.

We remain optimistic about the prospects for investment in Asia and particularly so as smaller and medium sized companies tend to be neglected at present. The predominant view in most equity markets is pessimistic despite the underlying strength in a number of economies and companies; this gives encouragement to our managers in their search for good companies at reasonable valuations.

**James Ferguson**
Chairman

31st October 2011

# Directors

**Dr Janet Morgan**, **CBE** aged 65, joined the Board in 1995. She is a non-executive Director of Murray International Trust plc and Close Enterprise VCT plc. She is also Chairman of the Nuclear Liabilities Fund, the Nuclear Trust and the Nuclear Liabilities Financing Assurance Board. She retired as a non-executive Director of Stagecoach plc in June 2010.

**James Ferguson**, aged 63, joined the Board in 2004. He is Chairman of Value and Income Trust plc, The Monks Investment Trust plc, Northern 3 VCT plc and Edinburgh US Tracker Trust plc and is a Director of The Independent Investment Trust plc and Audax Properties plc. He retired as Chairman of Stewart Ivory in 2000. He is a former deputy Chairman of the Association of Investment Companies.

**Alexandra Mackesy**, aged 49, joined the Board in 2004. Between 1988 and 2000, she worked as an investment analyst specialising in Asian equities, based in Hong Kong, becoming Director of Hong Kong and China equity research at Credit Suisse First Boston in 1998. Since 2000, she has worked as a consultant to Credit Suisse's Asian equities department. She is a non-executive Director of Henderson TR Pacific Investment Trust Plc and RENN Universal Growth Investment Trust Plc.

**Anne West**, aged 61, joined the Board in July 2010. She is currently a Fund Director in the Private Client Department of Cazenove Capital Management. She joined Cazenove in 1989 and assumed responsibility for Asian and Japanese portfolios, later becoming Head of the Emerging Markets team and then the Global Equity team. She was Chief Investment Officer from 2001 to 2008. Previously she held positions at Standard Chartered Bank and Hambro Pacific, based in Hong Kong.

# Portfolio Manager's Report

## REVIEW

The performance of Asian equity markets was again volatile for the year ending 31st August 2011. Significant gains were achieved in the last months of 2010, supported by expectations of further monetary stimulus, particularly in the US, and by high levels of foreign funds allocated to the Region. Economic growth in Asia remained robust. Combined with rising commodity prices, this resulted in higher than expected inflation. In January and February 2011 there was a pause in the Region's outperformance as the prospect of tighter monetary policy combined with relatively expensive valuations prompted a reversal in the flow of funds towards more developed stockmarkets. Thereafter, the performance of Asian equities in general was mixed. Those countries which experienced higher inflation and corresponding tightening of monetary policies generated lower returns.

India was the worst performing market during the period owing to concerns over persistently high inflation as well as evidence that political support for economic reforms has stalled. Chinese equities were also weak as the Government's attempts to slow elements of the economy, particularly property development, resulted in a decline in funds available to the private sector. The situation was exacerbated by accounting scandals affecting a number of US listed Chinese companies. In contrast, Indonesian and Thai equities achieved significant gains in the year, supported by strong domestic consumption.

Scottish Oriental's performance over the year was gratifying both in absolute terms and also relative to its benchmark. This was achieved in spite of the underperformance of smaller companies, as seen by the decline in the MSCI Asia ex Japan Small Cap Index over the period under review. The Trust benefited from its high exposure to Indonesia and Thailand, as well as strong returns from some of its larger holdings, such as Security Bank and SM Development in the Philippines and JVM Co. and Cosmax in South Korea.

### Stockmarket Performance *for the year ending 31st August 2011*

| Country | Sterling<br>% | Local Currency<br>% | Country Allocation on 31st August 2011<br>% |
|---|---|---|---|
| China | (5.7) | 0.0 | 15.5 |
| Hong Kong | 6.6 | 13.1 | 8.9 |
| Taiwan | 9.9 | 5.4 | 12.6 |
| *Greater China* | | | *37.0* |
| Singapore | 4.8 | (1.3) | 14.4 |
| Thailand | 20.5 | 22.3 | 8.4 |
| Malaysia | 4.7 | 5.4 | 8.4 |
| Indonesia | 19.5 | 19.5 | 5.4 |
| Philippines | 11.9 | 10.5 | 4.1 |
| Vietnam | (9.6) | 2.4 | 1.1 |
| *South East Asia* | | | *41.8* |
| India | (12.1) | (8.8) | 1.5 |
| Sri Lanka | 8.8 | 5.3 | 1.5 |
| *Indian Subcontinent* | | | *3.0* |
| South Korea | 14.0 | 7.4 | 13.2 |
| MSCI* | 3.7 | 4.0 | — |
| Net current assets | — | — | 15.7 |
| Loan | — | — | (10.7) |
| Total | | | 100.0 |

* Morgan Stanley Capital International AC Asia ex Japan Index

# Portfolio Manager's Report – continued

*Greater China*

Inflation in **China** remained high despite further tightening of monetary policy and more stringent limits on bank lending. The main cause was the rise in commodity prices, particularly food, while demand remained supported by the rise in wages. Higher costs have had a negative impact on corporate earnings, most notably for the manufacturing sector, where strong competition and weak export demand have limited companies' ability to raise prices.

**Hong Kong** continued to experience strong domestic economic growth as the currency peg with the US dollar has resulted in sustained low interest rates. Retail sales continued to grow at a dramatic rate supported by higher disposable incomes as well as strong demand from mainland Chinese tourists. The Government imposed further restrictions on lending for high-end residential properties in an attempt to limit price rises.

In **Taiwan**, there was a wide divergence in the performance of individual companies. There were disappointing returns from a number of technology related companies owing to weak demand. In contrast, there was a re-rating in the valuations of several consumer discretionary companies which were viewed as the beneficiaries of a stronger domestic economy, resulting from improved relations with China. Scottish Oriental benefited from its holding in Taiwan Familymart, the second largest convenience store operator.

*South East Asia*

**Singapore's** economy grew at a rapid rate at the end of 2010 and early part of 2011 as the Government continued to support its manufacturing base with the importation of unskilled labour. It also allowed its property market to continue appreciating. However, both these policies backfired during the May General Election, resulting in a significant decline in the ruling party's share of the popular vote. It became clear that the Government had underestimated the level of dissatisfaction felt by its citizens, many of whom have suffered a decline in living standards in recent years.

In **Malaysia**, the economic environment continued to improve with a stable labour market and a recovery in consumer sentiment. However, the rise in raw material costs resulted in higher inflation and thus an increase in interest rates by the Central Bank. The Prime Minister, Najib Razak, recently announced changes to controversial laws that will increase civil liberties in the country. While this is a positive development, it also reflects the Government's slow progress in reforming the economy and its attempts to improve its popularity prior to next year's General Election.

Politics remained a dominant theme in **Thailand** culminating in the pro-Thaksin Pheu Thai Party winning the Parliamentary General Election held in May. The country now has its first female Prime Minister, Yingluck Shinawatra, who has publicly committed herself to a policy of national reconciliation. Economic growth remained robust and domestic demand, particularly in the rural areas, continued to grow, supported by high prices for agricultural products such as rice and rubber.

**Indonesia's** economy and equity market performed well, supported by strong demand for the country's natural resources as well as low interest rates and a stable political environment. The Central Bank has avoided a rise in interest rates this year, relying instead on a strong currency to curb upward pressure on inflation.

The much needed investment in the **Philippines'** infrastructure via more private-public partnerships is progressing, albeit at a slow pace. In the meantime, economic growth has been strong, supported by low interest rates and strong Overseas Filipino Worker remittances which reached a record US$19 billion in 2010.

# Portfolio Manager's Report – continued

**Vietnam's** economy has suffered from the Government's previous pro-growth policy which led to a devaluation of the currency and a sharply higher trade deficit. Higher food prices have resulted in inflation rising to more than 20 per cent in 2011 and the application of severely tight monetary policy, which has already had a dampening effect on consumption.

## *Indian Subcontinent*

**India** continues to suffer from persistently high inflation, despite further monetary tightening by the Central Bank. Economic growth has slowed and the outlook for corporate profits has deteriorated, resulting in a decline in earnings forecasts and a de-rating of equity valuations. In addition, much heralded economic reforms seem to have stalled.

**Sri Lanka's** economic growth has accelerated since the end of the civil war in May 2009, fuelled by strong domestic demand and a rise in fixed asset investment. At the same time, the currency has appreciated, supported by strong capital inflows. Although the outlook for corporate earnings has improved, this is more than adequately reflected in valuations which are now expensive.

## *South Korea*

**South Korea's** economic growth has been strong, supported by robust demand for its exports and an improvement in domestic consumption. Although the rate of inflation has increased, the corresponding rise in interest rates has been modest, mainly because a significant number of Korean households and smaller companies remain highly indebted.

## Performance of individual equity holdings *for the year ending 31st August 2011*

| Company | Country | Contribution Performance (£) % | % of Shareholders' Funds (as of 31 Aug 2011) |
|---|---|---|---|
| **Best** | | | |
| BFI Finance | Indonesia | 1.9 | — |
| JVM Co. | South Korea | 1.7 | 2.6 |
| Cosmax | South Korea | 1.4 | 1.6 |
| Security Bank | Philippines | 0.9 | 1.9 |
| SM Development | Philippines | 0.9 | 1.6 |
| **Worst** | | | |
| Supermax | Malaysia | (0.8) | 1.2 |
| Boer Power | China | (0.7) | 0.6 |
| Amtek Engineering | Singapore | (0.7) | 1.3 |
| Samson Holding | China | (0.6) | 1.0 |
| Greens Holdings | China | (0.4) | 0.5 |

For the five best performing stocks, the common theme is valuation re-rating as recent earnings have surpassed expectations. **BFI Finance** benefited from the acquisition of a significant stake by a local investor as well as favourable financing terms for its recent bond issues. Scottish Oriental has since sold its position in this company. For both **JVM** and **Cosmax**, the recovery in corporate earnings has been significant and has resulted in the resumption of analyst coverage with positive recommendations. **Security Bank** and **SM Development** have benefited from the resilience of the Philippine economy with robust demand for both loans and affordable housing.

# Portfolio Manager's Report – continued

**Supermax's** earnings were lower than expected as the company was unable to raise prices to reflect fully the higher rubber price. Share prices for both **Boer Power** and **Samson Holding** fell sharply, following the announcement of profit warnings which reflected the highly competitive nature of their respective industries. **Amtek Engineering** fell in line with other Singapore listed technology companies, despite achieving earnings that were in line with expectations. **Greens Holdings** also continued to underperform, owing to concerns over the outlook for smaller companies in China. Despite their recent underperformance, Scottish Oriental continues to hold these companies, given their positive long term prospects and attractive valuations.

## OUTLOOK

The short term outlook for Asian equities is expected to be overshadowed by current economic events in Europe and the US. Forecasts for global economic growth are being revised down as many western nations are forced to apply more prudent fiscal policies. In the meantime, interest rates are expected to remain at current low levels despite the recent rise in inflation. Asia's economies are not immune to this slowdown, given their historic reliance on exports. However, the impact is likely to be more modest because real interest rates are still low and structural change continues to support growth in domestic consumption.

Inflation remains the key medium term risk to Asia from both an economic and a political perspective. The rise in commodity prices has resulted in not only more expensive manufactured goods but also increased food prices, as higher fuel and fertiliser prices raise the cost of production. The situation has been exacerbated by tighter labour markets, particularly in China, which have pushed up wages, resulting in stable demand despite the rise in food prices. In addition, rapid urban development has reduced the amount of land used for agriculture and declining availability of water has reduced yields. A sustained rise in the cost of living usually results in more vocal resistance to the incumbent political regime. Most Governments in Asia would rather use costly, inefficient subsidies than face the risk of social unrest. There is hope that a slowdown in global economic growth will result in an easing in commodity prices and moderation in the rate of inflation. If not, price rises are likely to remain above expectations until supply catches up with demand.

Although valuations for Asian smaller companies appear attractive, the outlook for corporate earnings remains uncertain. A number of companies, most notably exporters, continue to struggle to sustain margins owing to strong competition and limited pricing power. Scottish Oriental's investment philosophy is well suited for the current uncertainty, given its focus on well managed, financially sound companies.

In addition, the Trust will be able to utilise the US$32.5m additional cash from the loan with Scotiabank Europe. This is a 3 year loan at a fixed interest rate of 2.19 per cent which is due for repayment on 12 August 2014. This borrowing will enable the Trust to invest further in the mispriced assets which invariably arise in periods of high volatility.

**Susie Rippingall**
**Scott McNab**
**Angus Tulloch**
First State Investment Management (UK) Limited, Investment Manager

31st October 2011

# Portfolio Review

Scottish Oriental's portfolio of investments is well diversified not only by country but also by sector. The largest country exposure is China with a 15.5 per cent position. Consumer Discretionary accounted for 31.4 per cent of the portfolio, the largest sector weighting. As at 31st August 2011 Scottish Oriental was invested in 88 different companies with the largest holding, JVM Co, accounting for 2.6 per cent of the Portfolio. The aggregate of the Trust's ten largest holdings was 18.0 per cent.

## Country Allocation *at 31st August 2011 (based on geographical area of activity)*

| Country/Region | Scottish Oriental % | MSCI* % | MSCI Small Cap† % |
|---|---|---|---|
| China | 15.5 | 24.1 | 17.3 |
| Hong Kong | 8.9 | 11.6 | 10.7 |
| Taiwan | 12.6 | 15.4 | 20.8 |
| *Greater China* | *37.0* | *51.1* | *48.8* |
| Singapore | 14.4 | 7.1 | 8.3 |
| Thailand | 8.4 | 2.7 | 3.8 |
| Malaysia | 8.4 | 4.5 | 4.6 |
| Indonesia | 5.4 | 3.9 | 4.2 |
| Philippines | 4.1 | 0.9 | 1.4 |
| Vietnam | 1.1 | — | — |
| *South East Asia* | *41.8* | *19.1* | *22.3* |
| India | 1.5 | 9.7 | 10.1 |
| Sri Lanka | 1.5 | — | — |
| *Indian Subcontinent* | *3.0* | *9.7* | *10.1* |
| South Korea | 13.2 | 20.1 | 18.8 |
| *Net current assets* | *15.7* | — | — |
| *Loan* | *(10.7)* | — | — |
| *Net assets* | *100.0* | *100.0* | *100.0* |

* Morgan Stanley Capital International AC Asia ex Japan Index

† Morgan Stanley Capital International AC Asia ex Japan Small Cap Index

### *Greater China*

Scottish Oriental continues to have an underweight position in **China**-related companies. The Government is applying administrative pressures to tackle over-investment in both commercial and residential property. These measures include restrictions on bank lending which has resulted in a lack of credit available to small and medium sized companies. In addition, the imposition of price controls for certain key products, such as fuel, results in further distortions to the long term demand and supply imbalance. Valuations, particularly for the export related companies, are no longer expensive but the outlook for corporate earnings remains uncertain.

**Hong Kong's** domestic economy remains supported by low interest rates. However, inflation has gained momentum and may undermine consumer spending if wages fail to keep up with the higher cost of living. The Government appears determined to curtail the high cost of residential

# Portfolio Review – continued

property by raising supply, particularly for the more affordable units. Scottish Oriental is mainly invested in consumer related companies, such as Aeon Stores and Dickson Concepts.

There was a change in the Trust's holdings in **Taiwan**, with the replacement of a number of technology related companies with those companies that are well positioned to benefit from the improved relations with China. New positions include Johnson Health Tech and Lumax International, which have operations in both China and Taiwan.

## *ASEAN Countries*

Scottish Oriental continues to have a large position in **Singapore**. The holdings are diversified in terms of geographical reach with some, such as CSE Global and Petra Foods, having multinational exposure while others, such as Hong Leong Finance and Raffles Medical, focus on the domestic economy.

The Trust remains overweight in **Thailand**. Strong domestic consumption should continue, supported by the new Government's economic policies which include financial incentives for buyers of new cars and low end residential property. Valuations remain attractive with a number of the Trust's holdings, such as Aeon Thana Sinsap and Tisco Financial, providing dividend yields of more than 5%.

There were a number of changes to the Trust's holdings in **Malaysia**. Both Hong Leong Financial Group and Jobstreet Corp were sold following a re-rating of their valuations and replaced by a new position in Aeon Credit Services, which provides consumer finance to middle income consumers.

The Trust's exposure to **Indonesia** has been reduced following the sale of two finance related companies – BFI Finance and OCBC NISP – owing to expensive valuations and longer term concerns over the outlook for interest rates and the strength of the banking system. The Central Bank has kept interest rates unchanged despite the rise in inflation which has fuelled strong demand for loans and rising asset values.

Scottish Oriental's holdings in the **Philippines** remain focused on the domestic economy. SM Development, part of the well respected SM Group, is a middle income residential property developer that is enjoying strong demand for the sale of its apartments.

The Trust retains a small position in **Vietnam**. Although the short term outlook for the economy remains uncertain owing to high inflation and the unstable currency, equity valuations are now attractive. Exposure is via the Vietnam Enterprise Investments Fund.

## *Indian Sub-Continent*

Scottish Oriental continues to have a small weighting in **India** as valuations for well managed companies remain high. Economic growth is expected to slow, owing to higher interest rates, and this has yet to be fully reflected in forecasts for corporate earnings. The Trust continues to hold small positions in Castrol (India) and Marico and will look to add to its exposure, following the identification of suitable companies trading on attractive valuations.

Although the outlook for corporate earnings in **Sri Lanka** has improved, this is more than adequately reflected in corporate valuations, which are now expensive, particularly for those companies exposed to the domestic economy. Scottish Oriental sold its remaining position in Aitken Spence and replaced it with a new holding in Expolanka which provides logistics support for the garment industry in South and South East Asia.

## *South Korea*

The Trust added to its holdings in **South Korea** over the period with the purchase of Hana Tour Service and LG Life Sciences. Hana Tour is South Korea's leading travel company, selling through an extensive network of agents countrywide. LG Life Sciences is one of Korea's leading pharmaceutical companies with a strong focus on research and development.

# Portfolio Review – continued

## Sector Allocation *at 31st August 2011*

| Sector | % |
|---|---|
| Consumer Discretionary | 31.4 |
| Consumer Staples | 5.7 |
| | 37.1 |
| Energy | 2.8 |
| Financials | 20.9 |
| Information Technology | 11.0 |
| Industrial | 11.0 |
| Healthcare | 9.5 |
| Materials | 0.7 |
| Telecommunication Services | 0.8 |
| Utilities | 1.2 |
| | 95.0 |
| *Net current assets* | *15.7* |
| *Loan* | *(10.7)* |
| *Net assets* | *100.0* |

Scottish Oriental's exposure to the **Consumer Discretionary** sector increased significantly over the period, owing to a combination of strong outperformance from existing holdings as well as the acquisition of new companies. The Trust's holdings in the **Consumer Staples** sector were largely unchanged. There remains a wide selection of companies in these sectors which fulfil the Manager's investment requirements in terms of management quality, strong business franchise and robust financial position. In addition, these consumer-related companies will continue to benefit from the strength of the domestic economies in the Region.

The Trust reduced its position in **Financials** as a number of finance companies were sold following a re-rating of their valuations. Included in this sector are property companies as well as banks and consumer finance companies. The outlook for property markets remains positive over the longer term and valuations are relatively attractive.

Overall exposure to the **Information Technology** and **Industrial** sectors were largely unchanged although there was some change in the underlying holdings, with the sales of Powertech Technology in Taiwan and Dynasty Ceramics in Thailand.

The Trust's exposure to **Healthcare** increased with strong performance of the existing holdings, such as Raffles Medical in Singapore, as well as the acquisition of new holdings, such as Pacific Hospital Supply in Taiwan.

Scottish Oriental continues to have a limited exposure to stocks in the cyclical **Energy** and **Materials** sectors as these tend to be price-takers rather than price-setters and may be vulnerable to a slowdown in the global economy. It also has a very low weighting in the **Telecommunications** and **Utilities** sectors owing to the limited number of small but reasonably valued companies.

# Portfolio Review – continued

## Ten Largest Equity Holdings *at 31st August 2011*

| Company | Market | Value | % of Shareholders' Funds |
|---|---|---|---|
| **JVM Co.** | **South Korea** | **£4,865,008** | **2.6%** |

JVM designs and produces automatic tablet dispensing and packaging machines (ATDPS) and semi-automatic tablet dispensers. The ATDPS digitises the entire medicine preparation process from sorting, distribution, information printing and inventory management to billing. It is used in hospitals, large pharmacies and nursing homes and one unit typically handles the work of three or four pharmacists. The outlook for earnings is positive, supported by the recent launch of the company's new range of products.

| | | | |
|---|---|---|---|
| **Security Bank** | **Philippines** | **£3,515,190** | **1.9%** |

Established in 1959, Security Bank is an independent corporate bank with a strong position in the mass affluent Chinese community. In recent years, its assets have been growing at a faster rate than its peers, owing to the successful cross-marketing of a range of innovative products, including corporate, consumer and investment banking services.

| | | | |
|---|---|---|---|
| **Tisco Financial** | **Thailand** | **£3,442,718** | **1.8%** |

Tisco Financial is a diversified financial services company with investment banking, stockbroking, asset management and consumer finance divisions. In 2005, the company completed a restructuring which effectively changed Tisco into a bank and gave it access to low cost deposits. The consumer finance division is currently the largest contributor to earnings with a specific emphasis on hire purchase. Tisco has a very conservative provisioning policy for non-performing loans. Management is highly regarded and has a strong focus on the long term career development of its employees.

| | | | |
|---|---|---|---|
| **Media Prima** | **Malaysia** | **£3,360,030** | **1.8%** |

Media Prima is the leading media company in Malaysia with exposure to TV, radio and outside advertising as well as newspapers via its ownership of New Straits Times Press. The company has four free to air TV channels of which TV 3, Malaysia's leading network, is the largest contributor to the group's earnings. The combined viewership market share for the company's four TV channels is about 50%.

| | | | |
|---|---|---|---|
| **Amorepacific Group** | **South Korea** | **£3,269,685** | **1.7%** |

Amorepacific Group is a holding company whose major asset is a 35% stake in Amorepacific Corp, Korea's leading domestic cosmetics company. Amorepacific Corp has two key brands, Hera and Sulwhasoo, which are sold domestically and overseas, mainly in China and France. The group's other businesses include cosmetics bottling, green tea manufacturing and advertising services. It has a strong balance sheet and management continue to look for suitable acquisitions.

| | | | |
|---|---|---|---|
| **Texwinca** | **China** | **£3,145,819** | **1.7%** |

Texwinca's core businesses are the production of knitted fabric and garment retailing. The company is one of the largest manufacturers of knitted jersey in the world, operating from a single production base in Dongguan, China. Management's stringent cost controls combined with economies of scale support this division's superior margins. Texwinca's retail operations are under several brands including Baleno, S&K and the I.P. Zone. The focus is on China where it operates over 3,800 stores. Earnings growth is expected to come from steady expansion in textile production capacity combined with improved margins from the retailing business.

# Portfolio Review – continued

| Company | Market | Value | % of Shareholders' Funds |
|---|---|---|---|
| **Aeon Company** | **Malaysia** | **£3,080,859** | **1.7%** |

Aeon Company owns and operates Jusco general merchandise stores as well as standalone Maxvalu supermarkets in Malaysia. The company has been operating there for over 20 years and has developed a strong network of suppliers and distributors. Aeon's stores target the middle-income consumer and are located in high-density residential estates in the suburbs of major towns. Despite strong competition from hypermarkets, the company has been able to identify new store locations albeit at a conservative pace. Management are impressive with a strong focus on customer service.

| | | | |
|---|---|---|---|
| **SM Development** | **Philippines** | **£3,074,937** | **1.6%** |

SM Development, part of the SM Group, is involved in the investment and development of both residential and commercial properties in the Philippines. The company has benefited from having access to land near or beside SM Prime's shopping malls. Demand for residential property remains strong, owing to insufficient supply and robust remittances from overseas workers. SM Development also has a substantial investment portfolio which is retained to provide stable cash flows.

| | | | |
|---|---|---|---|
| **Ezion Holdings** | **Singapore** | **£3,013,972** | **1.6%** |

Ezion was created in March 2007 via a backdoor listing into Nylect Technology Limited. The Chief Executive and major shareholder is TK Chew, who was previously Chief Executive of KS Energy. Mr Chew established an impressive track record in his previous position. The company was established to own and lease out liftboats which are used for the maintenance and operational support of offshore platforms. Ezion also has a fleet of more than 20 ships, which include ballastable vessels, barges and tugs, of which half are under long term contracts and the rest on charter. The company has already commissioned four liftboats with a fifth due for completion by early next year.

| | | | |
|---|---|---|---|
| **TK Corp** | **South Korea** | **£2,984,286** | **1.6%** |

Established in 1965, TK Corp manufactures industrial fittings, with a specific focus on electronic and piping system for ships, petrochemical and power plants. The company has successfully expanded its capacity in recent years and increased its global market share at the expense of its European competitors. The majority of its revenues are from overseas and the company has recently set up offices in Houston, Beijing, India and Europe to handle these. TK Corp's wide product range of more than 45,000 items is a key barrier to entry. In addition, the company's strong financial position allows it to hold substantial inventory which ensures timely delivery for customers.

**Susie Rippingall**
**Scott McNab**
**Angus Tulloch**
First State Investment Management (UK) Limited, Investment Manager

31st October 2011

# List of Quoted Equity Investments at 31st August 2011

| | % of Shareholders' Funds |
|---|---|
| CHINA (15.5%) | |
| **Consumer Discretionary (11.6%)** | |
| Asia Satellite | 1.3 |
| Beijing Jingkelong | 0.9 |
| Glorious Sun Enterprises | 0.9 |
| Minth | 0.7 |
| Pacific Textiles | 1.1 |
| Pou Sheng International | 1.1 |
| Samson Holding | 1.0 |
| Shirble Department Store | 1.0 |
| Sun Hing Vision | 1.0 |
| Texwinca | 1.7 |
| YGM Trading | 0.9 |
| **Industrial (2.2%)** | |
| Boer Power | 0.6 |
| Greens Holdings | 0.5 |
| Lung Kee Holdings | 1.1 |
| **Information Technology (0.5%)** | |
| Sinocom Software | 0.5 |
| **Utilities (1.2%)** | |
| Towngas China | 1.2 |
| HONG KONG (8.9%) | |
| **Consumer Discretionary (3.4%)** | |
| Aeon Stores | 0.9 |
| Dickson Concepts | 1.2 |
| Next Media | 0.9 |
| Tai Ping Carpets | 0.4 |
| **Consumer Staples (1.2%)** | |
| Four Seas Mercantile | 0.4 |
| Vitasoy International | 0.8 |

| | % of Shareholders' Funds |
|---|---|
| HONG KONG (8.9%) (continued) | |
| **Financial (4.3%)** | |
| Aeon Credit Service | 0.7 |
| Dah Sing Financial | 0.6 |
| Keck Seng Investment | 0.6 |
| Public Financial | 1.1 |
| Tai Cheung Holdings | 1.3 |
| INDIA (1.5%) | |
| **Consumer Staples (0.8%)** | |
| Marico | 0.8 |
| **Materials (0.7%)** | |
| Castrol (India) | 0.7 |
| INDONESIA (5.4%) | |
| **Consumer Discretionary (3.3%)** | |
| Ace Hardware | 1.2 |
| Pembangunan Jaya Ancol | 1.1 |
| Sumber Alfaria Trijaya | 1.0 |
| **Energy (1.2%)** | |
| Salamander Energy | 1.2 |
| **Financial (0.9%)** | |
| Jaya Real Property | 0.9 |
| MALAYSIA (8.4%) | |
| **Consumer Discretionary (3.5%)** | |
| Aeon Company | 1.7 |
| Media Prima | 1.8 |
| **Financial (2.3%)** | |
| Aeon Credit Service | 1.4 |
| Quill Capita Trust | 0.9 |

| | % of Shareholders' Funds |
|---|---|
| MALAYSIA (8.4%) (continued) | |
| **Healthcare (1.2%)** | |
| Supermax | 1.2 |
| **Industrial (1.4%)** | |
| IJM Corporation | 1.4 |
| PHILIPPINES (4.1%) | |
| **Consumer Discretionary (0.6%)** | |
| Pancake House | 0.6 |
| **Financial (3.5%)** | |
| SM Development | 1.6 |
| Security Bank | 1.9 |
| SINGAPORE (14.4%) | |
| **Consumer Discretionary (0.7%)** | |
| Tan Chong International | 0.7 |
| **Consumer Staples (2.0%)** | |
| Petra Foods | 1.2 |
| Supergroup | 0.8 |
| **Energy (1.6%)** | |
| Ezion Holdings | 1.6 |
| **Financial (3.3%)** | |
| Bukit Sembawang Estates | 1.1 |
| Hong Leong Finance | 1.1 |
| Sabana REIT | 1.1 |
| **Healthcare (1.2%)** | |
| Raffles Medical | 1.2 |
| **Industrial (1.3%)** | |
| Amtek Engineering | 1.3 |

# List of Quoted Equity Investments at 31st August 2011 – continued

| | % of Shareholders' Funds |
|---|---|
| **SINGAPORE (14.4%) (continued)** | |
| **Information Technology (4.3%)** | |
| CSE Global | 1.5 |
| euNetworks | 0.5 |
| Nera Telecommunications | 1.0 |
| Venture Corporation | 1.3 |
| **SOUTH KOREA (13.2%)** | |
| **Consumer Discretionary (1.0%)** | |
| Hana Tour Service | 1.0 |
| **Consumer Staples (1.7%)** | |
| Amorepacific Group | 1.7 |
| **Financial (1.7%)** | |
| DGB Financial | 1.0 |
| Nice E-Banking Services | 0.7 |
| **Healthcare (4.8%)** | |
| JVM Co. | 2.6 |
| LG Life Sciences | 1.0 |
| Yuhan Corp | 1.2 |
| **Industrial (3.2%)** | |
| Cosmax | 1.6 |
| TK Corp | 1.6 |
| **Information Technology (0.8%)** | |
| IDIS Holdings | 0.4 |
| Intelligent Digital Integrated Security | 0.4 |

| | % of Shareholders' Funds |
|---|---|
| **SRI LANKA (1.5%)** | |
| **Industrial (0.7%)** | |
| Expolanka Holdings | 0.7 |
| **Telecommunication Services (0.8%)** | |
| Dialog Axiata | 0.8 |
| **TAIWAN (12.6%)** | |
| **Consumer Discretionary (3.7%)** | |
| E-Life Mall | 1.3 |
| Taiwan Familymart | 1.2 |
| Johnson Health Tech. | 1.2 |
| **Healthcare (2.3%)** | |
| St Shine Optical | 1.3 |
| Pacific Hospital Supply | 1.0 |
| **Industrial (2.2%)** | |
| 104 Corp | 1.0 |
| Yungtay Engineering | 1.2 |
| **Information Technology (4.4%)** | |
| Chroma Ate | 0.9 |
| Lumax International | 1.3 |
| Taiflex Scientific | 1.2 |
| Wah Lee Industrial | 1.0 |

| | % of Shareholders' Funds |
|---|---|
| **THAILAND (8.4%)** | |
| **Consumer Discretionary (3.6%)** | |
| Amarin Printing | 0.7 |
| Erawan Group | 1.3 |
| Home Product Center | 1.6 |
| **Financial (3.8%)** | |
| Aeon Thana Sinsap | 1.3 |
| Lalin Property | 0.7 |
| Tisco Financial | 1.8 |
| **Information Technology (1.0%)** | |
| Hana Microelectronic | 1.0 |
| **VIETNAM (1.1%)** | |
| **Financial (1.1%)** | |
| Vietnam Enterprise Investments | 1.1 |

# Ten Year Record

## Capital

| Year ended 31st August | Market Capitalisation £m | Shareholders' Funds £m | NAV Diluted (p) | NAV Undiluted (p) | Price Ordinary (p) | Price Warrant (p) | Discount to NAV Diluted % | Discount to NAV Undiluted % |
|---|---|---|---|---|---|---|---|---|
| 2002 | 31.51 | 35.29 | 133.77 | 138.56 | 123.75 | 49.50 | (7.5) | (10.7) |
| 2003 | 39.73 | 44.55 | 163.94 | 174.91 | 156.00 | 67.50 | (4.8) | (10.8) |
| 2004 | 39.94 | 46.00 | 169.14 | 180.50 | 156.75 | 69.50 | (7.3) | (13.2) |
| 2005 | 54.23 | 61.57 | 219.95 | 241.56 | 212.75 | 112.50 | (3.3) | (11.9) |
| 2006 | 64.41 | 73.26 | 256.22 | 279.24 | 245.50 | 144.00 | (4.2) | (12.1) |
| 2007 | 94.87 | 104.14 | 344.67 | 344.67 | 314.00 | — | (8.9) | (8.9) |
| 2008 | 79.16 | 94.50 | 312.78 | 312.78 | 262.00 | — | (16.2) | (16.2) |
| 2009 | 98.95 | 113.86 | 376.85 | 376.85 | 327.50 | — | (13.1) | (13.1) |
| 2010 | 146.08 | 167.76 | 555.26 | 555.26 | 483.50 | — | (12.9) | (12.9) |
| 2011 | 181.28 | 186.89 | 618.56 | 618.56 | 600.00 | — | (3.0) | (3.0) |

## Revenue

| Year ended 31st August | Gross revenue £'000 | Available for ordinary shareholders £'000 | Earnings per share* p | Dividend per share (net) p | Total expense ratio % | Total expense ratio incl performance fee % | Actual gearing† | Potential gearing‡ |
|---|---|---|---|---|---|---|---|---|
| 2002 | 1,211 | 445 | 1.75 | 1.50 | 1.51 | 1.51 | 105 | 109 |
| 2003 | 1,314 | 496 | 1.95 | 1.50 | 1.28 | 1.28 | 100 | 109 |
| 2004 | 1,567 | 547 | 2.14 | 1.58 | 1.54 | 1.54 | 102 | 108 |
| 2005 | 2,262 | 960 | 3.77 | 2.60 | 1.48 | 1.48 | 93 | 105 |
| 2006 | 2,416 | 1,239 | 4.78 | 3.60 | 0.88 | 0.88 | 94 | 101 |
| 2007 | 3,379 | 1,812 | 6.35 | 4.60 | 0.83 | 0.83 | 94 | 101 |
| 2008 | 3,643 | 2,008 | 6.64 | 5.00 | 0.78 | 0.78 | 98 | 101 |
| 2009 | 3,744 | 2,307 | 7.63 | 6.00 | 1.04 | 1.04 | 94 | 101 |
| 2010 | 4,940 | 3,197 | 10.58 | 8.50 | 1.00 | 1.65 | 94 | 101 |
| 2011 | 5,726 | 3,443 | 11.39 | 9.00 | 1.01 | 2.29 | 95 | 111 |

*The calculation of earnings per share is based on the revenue from ordinary activities after taxation and the weighted average number of ordinary shares in issue

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

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

## Cumulative Performance (taking year ended 31st August 2001 as 100)

| Year ended 31st August | NAV per share | Price per share | Price per warrant | MSCI AC Asia ex Japan Index | FTSE All-Share Index | Earnings per share | Dividend per share |
|---|---|---|---|---|---|---|---|
| 2001 | 100 | 100 | 100 | 100 | 100 | 100 | 100 |
| 2002 | 125 | 135 | 165 | 99 | 79 | 68 | 83 |
| 2003 | 158 | 170 | 225 | 112 | 80 | 76 | 83 |
| 2004 | 163 | 170 | 232 | 110 | 85 | 84 | 87 |
| 2005 | 218 | 231 | 375 | 137 | 103 | 147 | 144 |
| 2006 | 252 | 267 | 480 | 158 | 116 | 187 | 199 |
| 2007 | 311 | 341 | — | 216 | 126 | 248 | 254 |
| 2008 | 282 | 285 | — | 192 | 111 | 259 | 276 |
| 2009 | 340 | 356 | — | 204 | 97 | 298 | 331 |
| 2010 | 501 | 526 | — | 247 | 104 | 413 | 470 |
| 2011 | 559 | 652 | — | 249 | 108 | 445 | 497 |

# Scottish Oriental's Investment Management Team

Scottish Oriental is managed by First State Investment Management (UK) Limited, previously known as Stewart Ivory & Company Limited (the "Investment Manager"). The Investment Manager is part of Colonial First State Global Asset Management, the consolidated asset management business of The Commonwealth Bank of Australia. The Investment Manager offers a range of products across categories including Asia Pacific and global emerging markets, global resources and global equities, property securities and infrastructure.

**Susie Rippingall**
**Portfolio Manager of Scottish Oriental**

Susie has been part of the Asian Equities team since 1995, when she joined Stewart Ivory & Company. Between 1991 and 1995 Susie worked at Lehman Brothers Global Asset Management and prior to that she worked in corporate finance with Credit Lyonnais Securities. She graduated with an Honours degree in Economics at Edinburgh University. Susie is based in Hong Kong.

**Scott McNab**
**Senior Analyst, Global Emerging Markets/Asia Pacific (ex Japan) Equities**

Scott joined the Asian Equities team of First State Investments in 2001. Between 1999 and 2001 he worked for Ernst & Young in Bermuda. Prior to this Scott was a graduate trainee in the audit department of KPMG. He graduated with an Honours degree in Computer Science from the University of Durham. Scott is a Chartered Accountant, a CFA charterholder and an Associate member of the UK Society of Investment Professionals.

**Angus Tulloch**
**Joint Managing Partner of Global Emerging Markets/Asia Pacific (ex Japan) Equities**

Angus graduated from Clare College, Cambridge in 1970 with an Honours degree in Economics and History. After working as an accountant with Whinney Murray (now Ernst & Young), the National Bus Company and Elba Growers, he joined Cazenove in 1980 where he specialised in Far East equity investment. Angus returned to Scotland in 1988, joining Stewart Ivory & Company Limited to establish an Asia Pacific (ex Japan) capability. Since then, this team has gained industry recognition as one of the leading managers in its sector.

The Scottish Oriental Smaller Companies Trust plc was awarded the best in the 'Asia excluding Japan' category at the 2011 Moneywise Investment Trust Awards and the best in the 'Asia Pacific' category at the 2011 Money Observer Investment Trust Awards.

The Investment Manager was named Best Large Equity Fund House of the Morningstar UK Fund Awards 2011, Best International Equity Group and Best Fund Management Group (Small) at the Professional Adviser Awards 2011 and Equity Asset Manager of the Year at the Financial News Awards for Excellence in Institutional Asset Management Europe 2011.

# Company Information

## Registered Office
10 St. Colme Street
Edinburgh EH3 6AA, Scotland

## Company Number
SC156108

## Investment Manager
First State Investment Management (UK) Limited
23 St Andrew Square
Edinburgh EH2 1BB, Scotland
(Authorised and regulated by the Financial Services Authority)
Tel: +44 (0)131 473 2200 Fax: +44 (0)131 473 2222

## Company Secretary
Steven K Davidson
Personal Assets Trust Administration
Company Limited
10 St. Colme Street
Edinburgh EH3 6AA, Scotland

## Registrar
Computershare Investor Services plc
The Pavilions, Bridgwater Road,
Bristol BS99 6ZZ

## Auditor
Chiene + Tait
Chartered Accountants and Statutory Auditor
61 Dublin Street
Edinburgh EH3 6NL, Scotland

# Information for Investors

## Warrants
The final conversion date for the warrants occurred on 31st January 2007.

## Financial Diary
The Company's financial year ends on 31st August. The preliminary results are announced in October and the Annual Report and Accounts are published in November. Any dividend payable on the ordinary shares will be paid in January or February.

## Capital Gains Tax
An individual tax payer is currently entitled to an annual total tax-free gain, presently £10,600, from the sale of any shares and other capital assets. Any gain beyond that amount may be liable to capital gains tax.

For initial investors the apportioned base cost of ordinary shares and warrants for capital gains tax purposes is 92.59p per ordinary share and 37.05p per warrant.

## Where to find Scottish Oriental's Share Price
Scottish Oriental's share price appears daily in the Investment Companies Sector of the Financial Times and other leading daily newspapers.

The share price can also be found on the London Stock Exchange website by using the Trust's epic code 'SST' within the price search facility.

## The Internet
Scottish Oriental's website provides up-to-date information on the share price, net asset value and discount. We hope you will visit the Trust's website at: www.scottishoriental.com.

Investor Centre from Computershare (Scottish Oriental's registrar) enables you to manage and update your shareholder information. For this purpose you can register free with Investor Centre at www-uk.computershare.com/investor.

## Further Information
If you require any further information please contact Personal Assets Trust Administration Company Limited at the above address, by telephone on +44 (0)131 538 6610 or by fax on +44 (0)131 538 6607. For registry queries contact Computershare by telephone on +44 (0)870 707 1307.

# Directors' Report

The Directors have pleasure in submitting their Annual Report and Accounts for the year to 31st August 2011.

## Business Review

### Principal Activity, Status and Review

The Company is an investment company within the meaning of the Companies Act 2006 (company number: SC156108). HM Revenue and Customs' approval of the Company as an investment trust for the purposes of the Corporation Tax Act 2010 has been given for the year ended 31st August 2010, and the Company has subsequently directed its affairs so as to enable it to continue to seek such approval.

In the Directors' view, the description of the Company's development over the year and the identification of its key performance indicators are contained in the Financial Highlights, Ten Year Record, Chairman's Statement and Portfolio Manager's Report. In the Finance Act 2009, dividends and other distributions received from foreign companies from 1st July 2009 are for the most part exempt from corporation tax. The principal risks facing the Company relate to its investment activities and include market price risk and foreign currency risk. Further details of these risks are disclosed in note 16 of the Accounts on pages 43 to 45. Information on the Company's internal controls is set out on pages 25 and 26.

In common with most investment trusts, the Company has no employees.

The Company has given discretionary voting powers to the Investment Manager. The Board supports the integration by the Investment Manager of environmental, social and governance issues in its investment decision-making. In the Investment Manager's view, this assists the sustainable performance of the Company.

The table below shows the revenue position and dividend payable by the Company, subject to shareholders' approval at the Annual General Meeting of the final dividend of 9.00 pence per share proposed to be paid on 10th February 2012, on the former basis of accounting, which was to reflect a dividend in the accounts in the year to which it related rather than, as at present, to reflect it in the year in which the Company actually pays it.

| | £000 | Pence per share |
|---|---|---|
| Revenue reserve as at 31st August 2010 | 3,732 | 12.35 |
| Net revenue earned in the year | 3,443 | 11.39 |
| Dividend payable | (2,719) | (9.00) |
| Revenue reserve as at 31st August 2011 | 4,456 | 14.74 |

*Pence per share figures are based on the number of shares in issue at 31st August 2011*

### Borrowings

During the year the Company took out a US$32.5 million three year fixed rate loan with Scotiabank Europe plc. Further details of the loan can be found in note 11 on page 42.

### Share Capital

The Company's capital structure consists of 30,213,650 ordinary shares of 25p each in issue at 31st August 2011. Each ordinary share entitles the holder to one vote on a show of hands and, on a poll, to one vote for every share held.

# Directors' Report – continued

## Management

First State Investment Management (UK) Limited has been appointed as Investment Manager and Company Secretary under an agreement dated 20th March 1995 (as amended by supplemental agreements dated 31st July 1998, 22nd November 2005, 27th September 2006, 24th March 2009, 15th January 2010 and replaced by a new Investment Management Agreement on 1st March 2011) ("the Agreement").

The terms of the Agreement provide for payment of a base fee of 0.75% per annum of the Company's net assets payable quarterly in arrears. In addition an annual performance fee may be payable to the Investment Manager. These fees are capped, in aggregate, at an amount not exceeding or equal to 5% of the lower of (1) the gross asset value of the Company and (2) its market capitalisation, in each case at the relevant 31st August year end.

The performance fee is based on the Company's share price total return ("SPTR"), taking the change in share price and dividend together, over a three year period. If the Company's SPTR exceeds the SPTR of the Company's benchmark index (the MSCI AC Asia ex Japan Index) over the three year period plus ten percentage points then a performance fee is payable to the Investment Manager. The objective of the performance fee is to give the Investment Manager ten per cent of the additional value generated for shareholders by such outperformance. A performance fee of £2,405,137 is due to be paid for the twelve months ending 31st August 2011 and this fee will be charged against the Company's capital.

The Investment Manager's appointment as investment manager is subject to termination on one year's notice. The Company is entitled to terminate the Investment Manager's appointment on less than the specified notice period subject to compensation being paid to the Investment Manager for the period of notice not given. The compensation in the case of the Investment Manager's termination as investment manager is based on 0.75% of the value of the Company's net assets up to the date of termination on a pro rata basis. In addition a termination performance fee amount may be due to the Investment Manager based on the Company's three year performance up to the date of termination and paid on a pro rata basis.

The Agreement sets out matters over which the Investment Manager has authority and the limits above which board approval is required. In addition the Board has a formal schedule of matters specifically reserved to it for decision. This includes determination and monitoring of the Company's investment objectives and policy and its future strategic direction, gearing policy, matters relating to the buy-back and issuance of the Company's shares, appointment and removal of third party service providers, review of key investment and financial data and the Company's corporate governance and risk control arrangements.

## Company Secretary

Company Secretarial, accounting and administrative services were provided by First State Investment Management (UK) Limited for a fee, initially based on £35,000 per annum until 31st March 1996 and subsequently increased in line with the UK Retail Price Index annually, until 28th February 2011. On 1st March 2011 Personal Assets Trust Administration Company Limited was appointed to provide these services for an annual fee of £97,500 plus VAT payable quarterly in advance. The appointment is terminable on three months' notice following the initial period to 28th February 2012.

# Directors' Report – continued

## Continuing Appointment of the Investment Manager

The Board regularly appraises the performance and effectiveness of the investment managerial arrangements of the Company. As part of this process, such arrangements are reviewed formally once a year. In relation to the Board's formal review, the performance and effectiveness of such arrangements are measured against certain criteria. These include the Company's growth and return; performance against the Company's peer group; the success of the Company's investment strategy; the effectiveness, quality and standard of investment resource dedicated by the Investment Manager to the Company and the level of the Investment Manager's fee in comparison to its peer group. The Board, having conducted its review, considers that the Investment Manager's continued appointment as investment manager to the Company is in the best interests of shareholders.

## Creditor Payment Policy

The Company's payment policy for the year to 31st August 2012 is to agree terms of payment before business is transacted, to ensure suppliers are aware of these terms and to settle bills in accordance with them. The Company has no trade creditors.

## Substantial Shareholders

At 31st October 2011 the Company was aware of the following significant shareholdings representing (directly or indirectly) 3% or more of the voting rights attaching to the issued share capital of the Company:

| | Number of Shares held | Percentage held |
|---|---|---|
| Clients of Brewin Dolphin Securities | 3,865,066 | 12.8% |
| Clients of Alliance Trust Savings | 1,667,051 | 5.5% |
| Clients of Investec Wealth & Investment | 1,317,544 | 4.4% |
| Clients of Hargreaves Lansdown | 1,296,614 | 4.3% |
| Clients of Legal & General Investment Management | 1,084,024 | 3.6% |
| Clients of Henderson Global Investors | 1,040,000 | 3.4% |
| Clients of Barclays Stockbrokers | 1,032,790 | 3.4% |
| Clients of Rathbones | 1,024,801 | 3.4% |
| Clients of Smith & Williamson | 988,422 | 3.3% |
| Clients of F&C Asset Management | 937,185 | 3.1% |
| Clients of Adam & Co | 911,528 | 3.0% |

## Going Concern

After making inquiries, and bearing in mind the nature of the Company's business and assets, which are considered to be readily realisable if required, the Directors believe that the Company has adequate resources to continue operating for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

# Directors' Statement on Corporate Governance

Arrangements appropriate to an investment trust in respect of corporate governance have been made by the Board. The Board has considered the principles and recommendations of the AIC's Code of Corporate Governance (the "AIC Code") by reference to the AIC Corporate Governance

# Directors' Report – continued

Guide for Investment Companies (the "AIC Guide"). The AIC Code, as explained by the AIC Guide, addresses all the principles set out in the UK Corporate Governance Code issued by the Financial Reporting Council, as well as setting out additional principles and recommendations on issues that are of specific relevance to investment trusts. The AIC Code issued in October 2010 can be obtained from the AIC's website at www.theaic.co.uk.

The Board considers that reporting against the principles and recommendations of the AIC Code, and by reference to the AIC Guide (which incorporates the UK Corporate Governance Code), will provide better information to shareholders than if it had adopted the UK Corporate Governance Code.

The Company has complied with the recommendations of the AIC Code and the relevant provisions of the UK Corporate Governance Code, except as set out below.

The Board comprises four non-executive Directors, one of whom, Dr Janet Morgan, has been a Director for a period of longer than nine years. The Board considers Dr Morgan to be free from any business or other relationship with the Investment Manager or its employees which could interfere with or compromise the exercise of her independent judgement. Dr Morgan is therefore considered to be independent notwithstanding the length of her appointment. The Board considers that it is in the interests of the Company to have loyal and committed non-executive Directors, particularly as it does not have any employees or executive Directors.

James Ferguson was a Director of the Investment Manager until 2000 but has not been a Director of or employed by the Investment Manager or any member of its group since then and is therefore considered by the Board to be independent because of the period of time since he was connected with the Investment Manager. Additionally, the Chairman is considered to be independent notwithstanding his son's employment with the Investment Manager.

Finally, as the Board is an entirely non-executive Board, the Directors are involved in discussions to determine their own remuneration taking various factors into consideration. James Ferguson, the Chairman, also chairs the Remuneration Committee and the Audit Committee, appointments which are periodically reviewed. The Board considers that it is appropriate for Mr Ferguson to be Chairman of both committees as he is considered to be independent and has no conflicts of interests.

### *Directors*

The following Directors served during the year and had the following interests in the share capital of the Company. All the Directors' interests, save as otherwise disclosed, are beneficial interests in the share capital of the Company.

| | **31st August 2011 Ordinary 25p shares** | 31st August 2010 Ordinary 25p shares |
|---|---|---|
| James Ferguson* | 292,290 | 292,290 |
| Alexandra Mackesy | 28,600 | 28,600 |
| Dr Janet Morgan | 3,600 | 3,600 |
| Anne West | — | — |

* 272,290 ordinary shares in the Company are family interests
Sir Hamish Macleod retired as a Director on 25th January 2011 with a holding of 10,000 Ordinary 25p shares (31st August 2010: 10,000 Ordinary 25p shares)

# Directors' Report – continued

There were no changes to the above holdings between 31st August 2011 and 31st October 2011. The Company has no service contracts with its Directors and has not entered into any other contract in which a Director has an interest.

## *Meetings*

The Board meets at least quarterly and has a formal schedule of matters specifically reserved to it for decision including investment policy and agreement of the terms of appointment of the Investment Manager. The number of meetings of the Board, Audit Committee, Remuneration Committee and Nominations Committee held during the year and the attendance of the individual directors at those meetings is shown in the table below. Board papers are distributed prior to all meetings in a form and quality appropriate to enable the Board to discharge its duties. Directors can in addition raise any matters at meetings and there is a procedure in place for Directors to take independent professional advice, if necessary, at the Company's expense. The Company purchases and maintains Directors' and Officers' liability insurance. The Directors confirm that the Company Secretary is responsible for ensuring that the Board's procedures are followed and for compliance with applicable rules and regulations including the UK Corporate Governance Code. Appointment or removal of the Company Secretary is a matter for the Board as a whole. All Directors have access at any time to the advice and services of the Company Secretary.

| Number of Meetings | Board Meetings | Audit Committee | Committee of the Board | Remuneration Committee | Nomination Committee |
|---|---|---|---|---|---|
| James Ferguson | 5 | 2 | 2 | 1 | 1 |
| Alexandra Mackesy | 5 | 2 | 1 | 1 | 1 |
| Sir Hamish Macleod* | 2 | 1 | — | — | — |
| Dr Janet Morgan | 5 | 2 | 1 | 1 | 1 |
| Anne West | 5 | 2 | 1 | 1 | 1 |

* Retired as a Director on 25th January 2011

## *Independence of Directors*

The Board considers its four non-executive Directors to be free from any business or other relationship with the Investment Manager or its employees which could interfere with or compromise the exercise of his or her independent judgement and, therefore, independent of the Investment Manager. The Board deems the Chairman to be independent having taken into consideration his son's employment with the Investment Manager and his previous directorship with the Investment Manager. Dr Janet Morgan has served on the Board for more than nine years. The Board considers that Dr Morgan is independent of the Investment Manager in mind, character and judgement and free from any business or other relationship with the Investment Manager which could interfere with or compromise the exercise of her independent judgment. In addition, as the Trust does not have an executive board or any employees, it is considered to be in shareholders' interests for non-executive Directors to serve on the Board for longer periods of time.

## *Performance Appraisals*

Performance appraisals of the Chairman and Directors were carried out during the accounting period through a discussion based process. The Chairman's appraisal was led by the Senior Independent Director, Dr Janet Morgan. The Board concluded that the Chairman and each Director contributed effectively and demonstrated commitment to their role. The Board also concluded that the performance of the Board as a whole and its committees was effective. The training and development needs of Directors are discussed prior to and during the annual appraisal.

# Directors' Report – continued

## *Terms of Appointment and Re-election of Directors*

James Ferguson and Alexandra Mackesy retire by rotation at the Annual General Meeting ("AGM") and, being eligible, offer themselves for re-election. Dr Janet Morgan, having served on the Board for more than nine years, offers herself for re-election at the AGM. The Board confirms that each of the Directors seeking re-election continues to make a significant contribution to Board deliberations. The Board therefore believes that it is in the interests of shareholders that the above Directors be re-elected. The Articles of Association provide that each Director is subject to election at the first AGM after his or her appointment and must retire by rotation every three years. His or her re-election is subject to shareholder approval, based upon the recommendations of the full Board. Biographical details of all Directors are set out on page 5 of this Annual Report to enable shareholders to take an informed decision on their election. From these details, it will be seen that the Board has a breadth of investment, commercial and professional experience with an international, and more specifically, Far East perspective. The Directors are experienced in their role as Directors and any new Director will, upon appointment, receive a briefing on the investment operations and administrative functions of the Company and his or her role/responsibility as a Director as appropriate.

The Board is of the view that longer notice periods are necessary to ensure long term stability of the management of the Trust, given that the Trust has no employees. As an investment trust, the Board also adheres to the AIC Code.

The terms and conditions of appointment of non-executive Directors are available for inspection at the Company's registered office during normal business hours.

## *Nominations Committee*

The Board as a whole fulfils the functions of a Nominations Committee.

The Nominations Committee terms of reference are available on the Trust's website and clearly define the Committee's responsibilities.

The Nominations Committee meets at least annually.

## *Internal Controls*

The Directors are ultimately responsible for the internal controls of the Company which aim to ensure that proper accounting records are maintained, the assets are safeguarded and the financial information used within the business and for publication is reliable. The Directors are required to review the effectiveness of the Company's system of internal control. The UK Corporate Governance Code states that the review should cover all material controls, including financial, operational and compliance controls and risk management systems. Operational and reporting systems are in place to identify, evaluate and monitor the operational risks potentially faced by the Company and to ensure that effective internal controls have been maintained throughout the period under review and up to the date of approval of this Annual Report. The Board confirms that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Company. A full review of all internal controls is undertaken annually and the Board confirms that it has reviewed the effectiveness of the system of internal control.

# Directors' Report – continued

These controls include:

- Reports at regular Board meetings of all security and revenue transactions effected on the Company's behalf. These transactions can only be entered into following appropriate authorisation procedures determined by the Board, the Investment Manager and the Company Secretary;
- Custody of the Company's assets has been delegated to JPMorgan Chase. The records maintained by JPMorgan Chase permit the Company's holdings to be readily identified. The Investment Manager and Company Secretary carry out regular reconciliations with the custodian's records of the Company's cash and holdings;
- The Investment Manager's compliance and risk department monitors compliance by individuals and the Investment Manager's operations with the rules of the Financial Services Authority and provides regular reports to the Board;
- A risk matrix is prepared which identifies the significant risks faced by the Company and the Investment Manager's and Company Secretary's controls in place to manage these risks effectively.

These systems are designed to manage rather than eliminate risk and can only provide reasonable and not absolute assurance against material misstatement or loss.

### *Audit Committee and Auditor*

An Audit Committee has been established consisting of all the Directors, with three constituting a quorum. James Ferguson was appointed Chairman of the Audit Committee Meetings held on 14th October 2010 and 22nd March 2011. The Board considers that it is appropriate for all Directors to be members of the Committee given the size and composition of the Board. The Audit Committee has clearly defined written terms of reference which are available on the Company's website. The main functions of the Audit Committee are as follows:

- to monitor the integrity of the financial statements of the Company and any formal announcements relating to the Company's financial performance, and to review significant financial reporting judgements contained in them;
- to consider the appointment of the external auditor, the audit fee, and any questions of the external auditor's resignation or dismissal;
- to review the half-year and annual financial statements before submission to the Board;
- to monitor and review the effectiveness of the Company's statements on corporate governance and internal control systems (including financial and operational and compliance controls and risk management) prior to endorsement by the Board; and
- to review and monitor the external auditor's independence and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements. The Audit Committee also reviews the objectivity of the auditors and the terms under which they are appointed to perform non-audit services. Fees for these services amounted to £4,000 for the year ended 31st August 2011. The Board consider that the provision of such services at this low level is cost effective and does not impair the independence of Chiene + Tait.

The Audit Committee meets the Auditor at least once a year to review these and other matters. A resolution to re-appoint Chiene + Tait, Chartered Accountants and Statutory Auditor, as Auditor of the Company will be proposed at the Annual General Meeting. The Board does not consider that an internal audit function is necessary as a result of the Company's straightforward structure.

# Directors' Report – continued

## *Disclosure of Information to Auditor*

The Directors confirm that as far as they are aware, as at the date of this Report, there is no relevant audit information of which the Company's auditor is unaware and that each Director has taken all the steps he or she might reasonably be expected to have taken as a Director in order to make himself or herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

## *Share Buy Backs*

The Company's buy back authority was last renewed at the AGM on 25th January 2011 in respect of 4,532,047 ordinary shares of 25p each. No shares were bought back during the period under review and no shares are held in treasury.

## *Annual General Meeting*

The notice convening the Annual General Meeting to be held on 6th February 2012 is given on pages 48 to 52. The resolutions to be proposed include a resolution to approve the Directors' Remuneration Report, which is set out on pages 29 and 30.

Resolutions 8 and 9 to be proposed at the Annual General Meeting as ordinary and special resolutions respectively will, if approved, authorise the Directors to allot a limited number of unissued ordinary shares and empower them to allot some of the same for cash without first offering such shares to existing ordinary shareholders pro rata to their existing holdings. The authority being sought under Resolution 8 is in respect of £636,646 in nominal value of relevant securities, comprising the whole unissued ordinary share capital of the Company on 31st October 2011; this figure represents approximately 8.4% of the issued ordinary share capital on that date. The power to disapply preemption rights being sought under Resolution 9 is in respect of £377,670 of equity securities comprising 5% of the ordinary shares of the Company in issue on 31st October 2011. The authority under Resolutions 8 and 9 will expire at the conclusion of the next Annual General Meeting of the Company after the passing of the resolutions or on the expiry of 15 months from the passing of the resolutions, whichever is the earlier. The Directors, who have no present intention of exercising their authority to allot any of the same, will only allot relevant securities under this authority to take advantage of opportunities in the market as they arise and only if they believe it is advantageous to the Company's shareholders to do so.

Resolution 10 to be proposed at the Annual General Meeting as a special resolution gives authority to the Company to purchase its own shares, subject to the provisions of the Companies Act 2006, as permitted by the Company's Articles of Association. This resolution specifies the maximum such number of shares which may be acquired (being 4,532,047 ordinary shares, just under 15% of the Company's issued share capital at 31st October 2011) and the maximum (105% of the 5 day average middle market price) and minimum (the nominal value) prices at which shares may be bought. The Directors will only exercise the authority granted pursuant to this resolution through the market for cash at prices below the prevailing net asset value of the ordinary shares (as last calculated) in circumstances where such purchases will enhance net asset value. The proposed authority, if granted, will expire at the earlier of the next Annual General Meeting or 15 months following the passing of Resolution 10. There are no options outstanding over the Company's share capital.

# Directors' Report – continued

## *Notice Period for General Meetings*

Resolution 11 is being proposed to enable general meetings to be held on 14 clear days' notice rather than 21 clear days' notice following the implementation of The Companies (Shareholders' Rights) Regulations 2009 which implemented the EU Shareholder Rights Directive (2007/36/EC) (the "Directive").

The provisions of the Companies Act 2006 relating to meetings have been amended as a result of the implementation of the Directive. The minimum notice period for listed company general meetings has been increased to 21 clear days, but companies have an ability to reduce this period back to 14 clear days (other than for annual general meetings), provided that the company offers facilities for shareholders to vote by electronic means and that there is an annual resolution of shareholders approving the reduction in the minimum period for notice of general meetings (other than annual general meetings) from 21 clear days to 14 clear days. The Board is therefore proposing Resolution 11 as a special resolution to ensure that the minimum required period for notice of general meetings of the Company (other than annual general meetings) is 14 clear days. The Directors believe it is in the best interests of the shareholders of the Company to preserve the shorter notice period, although it is intended that this flexibility will only be used for non-routine business and where merited in the interests of shareholders as a whole. The approval will be effective until the Company's next Annual General Meeting when it is intended that a similar resolution will be proposed.

## *Recommendation*

The Directors unanimously recommend that you vote in favour of the resolutions to be proposed at the Annual General Meeting as it is their view that the Resolutions are in the best interests of shareholders as a whole.

## *Relations with Shareholders*

The Board recognises the value of the views of shareholders. The Investment Manager has a policy of meeting major shareholders and reports to the Board following such meetings. Any shareholder wishing to communicate with a member of the Board may do so by writing to him or her at the Company's registered office as detailed on page 19. All who attend at the AGM have an opportunity to question the Board and the Investment Manager. Proxy voting figures for each resolution are available to shareholders after the AGM. Separate items of business are proposed as separate resolutions. The Annual Report is sent to shareholders at least 20 working days before the AGM.

## *Exercise of Voting Powers*

The Investment Manager decides whether and how to vote on behalf of the Company in accordance with the Investment Manager's judgement of what is best for the Company and its shareholders in each individual case.

On behalf of the Board

Steven K Davidson
*Company Secretary*
31st October 2011

# Directors' Remuneration Report

## Directors' Remuneration Report

The Board has prepared this report in accordance with the requirements of Section 421 of the Companies Act 2006. An ordinary resolution for the approval of this report will be put to the members at the forthcoming Annual General Meeting.

The law requires the Company's Auditor to audit certain of the disclosures provided. Where disclosures have been audited, they are indicated as such. The Auditor's opinion is included in their report on pages 46 and 47.

## Remuneration Committee

The Company has four non-executive Directors. The Board as a whole fulfils the function of a Remuneration Committee as it considers specific appointments to such a committee are not appropriate due to the size and composition of the Board. Appointments are periodically reviewed.

The Remuneration Committee terms of reference are available on the Trust's website and clearly define the Committee's responsibilities.

The Board carried out a review of the level of Directors' fees during the year. It was resolved to increase the level of the Chairman's fee from £22,500 to £23,500 per annum and Directors' fees from £16,000 to £17,000 each per annum, such increases to take effect from 1st July 2011.

## Policy on Directors' Fees

The Board's policy is that the remuneration of non-executive Directors should reflect the experience of the Board as a whole, be fair and comparable to that of other investment trusts that are similar in size and have similar objectives and structures. Furthermore the level of remuneration should be sufficient to attract and retain the high calibre of Directors needed to oversee the Company properly and to reflect the specific circumstances of the Company, the duties and responsibilities of the Directors and the value and amount of time committed to the Company's affairs. It is intended that this policy will continue for the year ended 31st August 2012 and subsequent years.

The fees for the non-executive Directors are set within maximum limits determined from time to time by the Company in general meeting. The Directors are not eligible for bonuses, pension benefits, share options, long-term incentive schemes or other benefits. The Directors' fees are not performance related.

## Directors' Service Contracts

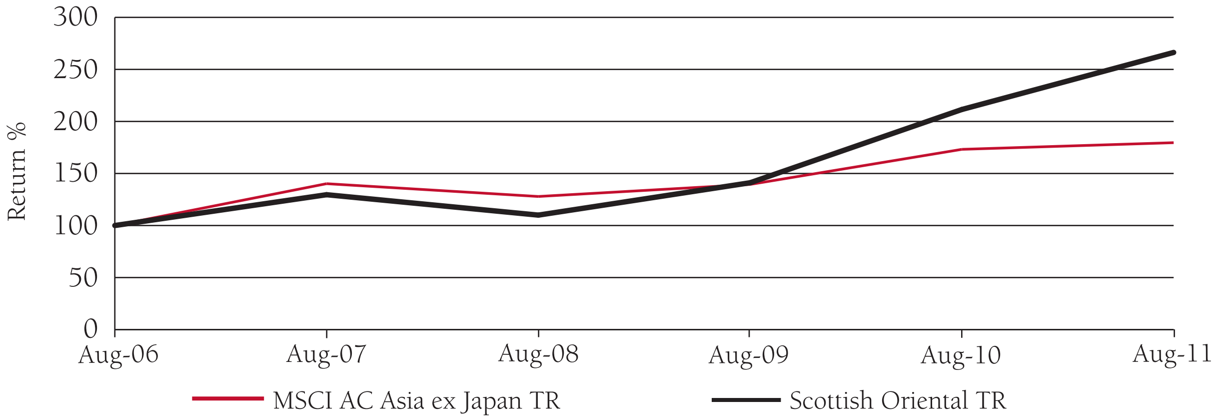
The Directors do not have a contract of service with the Company. All of the Directors have been provided with letters of appointment. The letters of appointment provide that Directors are appointed for a period of three years and are subject to election by shareholders at the first Annual General Meeting after their appointment. Thereafter they must retire at intervals of no more than three years. Their re-election is subject to shareholder approval. The letters of appointment are available for inspection on request. Any Director who has served on the Board for more than nine years will submit himself or herself for re-election annually. There is no notice period and no provision for compensation upon early termination of appointment. The Board believes that long term appointments are a benefit to the Company in terms of awareness and industry experience.

# Directors' Remuneration Report – continued

## Your Company's Performance

The graph below compares the total return (assuming all dividends are reinvested) to ordinary shareholders for the last five financial years compared to the total shareholder return on the MSCI AC Asia ex Japan Index. This index was chosen for comparison purposes, as it is the benchmark used for investment performance measurement purposes.

## Total Return – Scottish Oriental versus MSCI AC Asia ex Japan Index




## Directors' Emoluments for the Year (audited)

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

| | **Fees 2011 (£)** | Fees 2010 (£) |
|---|---|---|
| James Ferguson (Chairman) | 22,667 | 21,250 |
| Alexandra Mackesy | 16,167 | 15,167 |
| Sir Hamish Macleod* | 6,429 | 15,167 |
| Dr Janet Morgan | 16,167 | 15,167 |
| Anne West** | 16,167 | 1,841 |
| | 77,597 | 68,592 |

* Retired as a Director on 25th January 2011

** Appointed as a Director on 21st July 2010

## Sums Paid to Third Parties (audited)

No sums were paid to third parties.

## Approval

The Directors' Remuneration report on pages 29 to 30 was approved by the Board of Directors on 31st October 2011 and signed on its behalf by

**James Ferguson**, Chairman
31st October 2011

# Statement of Directors' Responsibilities

## Statement of Directors' Responsibilities

The Directors are responsible for preparing the Directors' Report, the Directors' Remuneration 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 the Directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the assets, liabilities, financial position and 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 accounting estimates that are reasonable and prudent; and
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements and the Remuneration Report comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors confirm that suitable accounting policies, applied consistently and supported by reasonable and prudent judgements and estimates, have been used in the preparation of the accounts and that applicable accounting standards have been followed.

The financial statements are published on the Company's website www.scottishoriental.com which is maintained by the Investment Manager. The maintenance and integrity of the corporate and financial information relating to the Company is the responsibility of the Investment Manager. The work carried out by the Auditor does not involve consideration of the maintenance and integrity of this website and, accordingly, the Auditor accepts no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website. Visitors to the website need to be aware that legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the Directors confirms that to the best of his or her knowledge:

- the financial statements, prepared in accordance with applicable United Kingdom accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company; and
- the Directors' Report includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that the Company faces.

By order of the Board

James Ferguson
*Chairman*
31st October 2011

# Income Statement

*For the year ended 31st August 2011*

| | | 2011 | | | 2010 | | |
|---|---|---|---|---|---|---|---|
| | Note | **Revenue £000** | **Capital £000** | **Total* £000** | Revenue £000 | Capital £000 | Total* £000 |
| Gains on investments | | **—** | **20,237** | **20,237** | — | 52,760 | 52,760 |
| Income from investments | 1 | **5,696** | **—** | **5,696** | 4,933 | — | 4,933 |
| Other income | 1 | **30** | **—** | **30** | 7 | — | 7 |
| Investment management fee | 2 | **(1,452)** | **(2,405)** | **(3,857)** | (1,131) | (937) | (2,068) |
| Currency gains | 13 | **—** | **470** | **470** | — | 825 | 825 |
| Other administrative expenses | 3 | **(461)** | **—** | **(461)** | (323) | — | (323) |
| **Net return before finance costs and taxation** | | **3,813** | **18,302** | **22,115** | 3,486 | 52,648 | 56,134 |
| Finance costs of borrowing | 4 | **(18)** | **(54)** | **(72)** | — | — | — |
| **Net return on ordinary activities before taxation** | | **3,795** | **18,248** | **22,043** | 3,486 | 52,648 | 56,134 |
| Tax on ordinary activities | 5 | **(352)** | **—** | **(352)** | (289) | (129) | (418) |
| **Net return attributable to equity shareholders** | | **3,443** | **18,248** | **21,691** | 3,197 | 52,519 | 55,716 |
| Net return per ordinary share | 7 | **11.39p** | **60.40p** | **71.79p** | 10.58p | 173.83p | 184.41p |

*The total column of this statement is the Profit & Loss Account of the Company.

A Statement of Total Recognised Gains and Losses has not been prepared as any gains or losses are recognised in the Income Statement.

**The Board is proposing a dividend of 9.00p per share for the year ended 31st August 2011 (2010: 8.50p per share) which, if approved, will be payable on 10th February 2012 to shareholders recorded on the Company's shareholder register on 16th December 2011.**

The accounting policies on pages 36 and 37 and the notes on pages 38 to 45 form part of these accounts.

All revenue and capital items derive from continuing operations.

# Balance Sheet

*as at 31st August 2011*

| | Note | 2011 £000 | 2011 £000 | 2010 £000 | 2010 £000 |
|---|---|---|---|---|---|
| FIXED ASSETS – EQUITY INVESTMENTS | 8 | | | | |
| China | | | **29,021** | | 17,277 |
| Hong Kong | | | **16,691** | | 17,715 |
| India | | | **2,764** | | 2,542 |
| Indonesia | | | **10,147** | | 11,532 |
| Malaysia | | | **15,724** | | 12,815 |
| Philippines | | | **7,701** | | 9,645 |
| Singapore | | | **26,843** | | 20,397 |
| South Korea | | | **24,727** | | 17,630 |
| Sri Lanka | | | **2,871** | | 3,609 |
| Taiwan | | | **23,434** | | 20,284 |
| Thailand | | | **15,691** | | 20,036 |
| Vietnam | | | **1,935** | | 2,226 |
| | | | **177,549** | | 155,708 |
| CURRENT ASSETS | | | | | |
| Debtors | 9 | **999** | | 1,314 | |
| Cash and deposits | | **31,328** | | 12,650 | |
| | | **32,327** | | 13,964 | |
| CURRENT LIABILITIES (due within one year) | | | | | |
| Creditors | 10 | **(3,028)** | | (1,907) | |
| | | **(3,028)** | | (1,907) | |
| **Net Current Assets** | | | **29,299** | | 12,057 |
| **Total Assets less Current Liabilities** | | | **206,848** | | 167,765 |
| CREDITORS (due after one year) | | | | | |
| Loan | 11 | | **(19,960)** | | — |
| **Equity Shareholders' Funds** | | | **186,888** | | 167,765 |
| *Represented by* | | | | | |
| CAPITAL AND RESERVES | | | | | |
| Ordinary share capital | 12 | | **7,554** | | 7,554 |
| Share premium account | 13 | | **21,337** | | 21,337 |
| Warrant reserve exercised | 13 | | **1,319** | | 1,319 |
| Capital reserve | 13 | | **149,503** | | 131,255 |
| Revenue reserve | 13 | | **7,175** | | 6,300 |
| | | | **186,888** | | 167,765 |
| **Net asset value per share** | 14 | | **618.56p** | | 555.26p |

These accounts were approved by the Board on 31st October 2011 and signed on its behalf by

**James Ferguson**, *Director* **Dr Janet Morgan**, *Director*

The accounting policies on pages 36 and 37 and the notes on pages 38 to 45 form part of these accounts.

# Cash Flow Statement

*for the year ended 31st August 2011*

| | 2011 £000 | 2011 £000 | 2010 £000 | 2010 £000 |
|---|---|---|---|---|
| OPERATING ACTIVITIES: | | | | |
| Dividends received from investments | | **5,594** | | 4,667 |
| Other income | | **64** | | 7 |
| | | **5,658** | | 4,674 |
| Investment management fee | **(1,305)** | | (1,063) | |
| Secretarial fee | **(84)** | | (51) | |
| Directors' fees | **(79)** | | (71) | |
| Other expenses paid | **(344)** | | (173) | |
| | | **(1,812)** | | (1,358) |
| **Net cash inflow from operating activities** | | **3,846** | | 3,316 |
| RETURNS ON INVESTMENTS AND SERVICING OF FINANCE | | | | |
| Loan drawn down | **19,813** | | — | |
| Arrangement fees | **(34)** | | — | |
| **Net cash inflow from investments and servicing of finance** | | **19,779** | | — |
| TAXATION | | | | |
| **Total tax paid** | | **(453)** | | (583) |
| CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT: | | | | |
| Purchases of investments | **(58,354)** | | (39,746) | |
| Sales of investments | **56,742** | | 42,558 | |
| Indian capital gains tax | **–** | | (129) | |
| Currency gains | **623** | | 825 | |
| Performance fee | **(937)** | | — | |
| **Net cash (outflow)/inflow from capital expenditure and financial investment** | | **(1,926)** | | 3,508 |
| EQUITY DIVIDEND PAID | | **(2,568)** | | (1,813) |
| **Increase in cash** | | **18,678** | | 4,428 |

The notes to the Cash Flow Statement are contained in note 15.

# Reconciliation of Movements in Shareholders' Funds

## *for the year ended 31st August 2011*

| | Share Capital £000 | Share Premium Account £000 | Warrant Reserve Exercised £000 | Capital Reserve £000 | Revenue Reserve £000 | Total £000 |
|---|---|---|---|---|---|---|
| Balance at 31st August 2010 | 7,554 | 21,337 | 1,319 | 131,255 | 6,300 | 167,765 |
| Realised gain on investments | — | — | — | **30,867** | — | **30,867** |
| Currency gain | — | — | — | **470** | — | **470** |
| Unrealised depreciation on investments in the year | — | — | — | **(10,630)** | — | **(10,630)** |
| Performance fee | — | — | — | **(2,405)** | — | **(2,405)** |
| Finance costs of borrowing | — | — | — | **(54)** | — | **(54)** |
| Income retained in the year | — | — | — | — | **3,443** | **3,443** |
| Dividend paid in the year | — | — | — | — | **(2,568)** | **(2,568)** |
| **Balance at 31st August 2011** | **7,554** | **21,337** | **1,319** | **149,503** | **7,175** | **186,888** |

## *for the year ended 31st August 2010*

| | Share Capital £000 | Share Premium Account £000 | Warrant Reserve Exercised £000 | Capital Reserve £000 | Revenue Reserve £000 | Total £000 |
|---|---|---|---|---|---|---|
| Balance at 31st August 2009 | 7,554 | 21,337 | 1,319 | 78,736 | 4,916 | 113,862 |
| Realised gain on investments | — | — | — | 20,058 | — | 20,058 |
| Currency gain | — | — | — | 825 | — | 825 |
| Unrealised appreciation on investments in the year | — | — | — | 32,702 | — | 32,702 |
| Performance fee | — | — | — | (937) | — | (937) |
| Indian capital gains tax | — | — | — | (129) | — | (129) |
| Income retained in the year | — | — | — | — | 3,197 | 3,197 |
| Dividend paid in the year | — | — | — | — | (1,813) | (1,813) |
| Balance at 31st August 2010 | 7,554 | 21,337 | 1,319 | 131,255 | 6,300 | 167,765 |

# Accounting Policies

## Basis of accounting

(a) These accounts have been prepared in accordance with applicable accounting standards and under the historical cost convention (modified to include the revaluation of fixed asset investments which are recorded at fair value), the Companies Act 2006 and the Statement of Recommended Practice "Financial Statements of Investment Trust Companies and Venture Capital Trusts" issued in January 2009 (the "SORP") except for certain illiquid stocks which have been valued at the last traded price, as has been the Company's practice. The Directors consider the last traded price for such stocks to be the best estimate of fair value. Financial assets and liabilities are recognised in the Company's Balance Sheet when it becomes party to the contractual provisions of the instrument.

In order better to reflect the activities of the Company and in accordance with guidance issued by the AIC, supplementary information which analyses the Profit and Loss Account between items of revenue and capital nature has been presented in the Income Statement.

The accounts have also been prepared on the assumption that approval as an investment trust will continue to be granted.

The financial statements, and the net asset value per share figures, have been prepared in accordance with UK Generally Accepted Accounting Practice ("UK GAAP").

The functional and reporting currency of the Company is pounds sterling as most investors in the Company are based in the United Kingdom.

## Income

(b) Dividends on securities are brought into account on the date on which the security is quoted "ex dividend" on the stock exchange in the country in which the security is listed. Interest on securities is accounted for on a time appointed basis. Foreign dividends include any withholding taxes payable to the tax authorities. Where a scrip dividend is taken in lieu of cash dividends, the net amount of the cash dividend declared is credited to the revenue account. Any excess in the value of shares received over the amount of cash dividend foregone is recognised as capital.

(c) Overseas income is recorded at rates of exchange ruling at the date of receipt.

(d) Bank interest receivable is dealt with on an accruals basis and taken to revenue.

## Expenses

(e) Expenses and interest payable are dealt with on an accruals basis and are charged through the revenue column of the Income Statement.

(f) The base investment management and company secretarial fees have been charged in full to the Income Account. The performance fee is chargeable in full to the Capital Account.

## Valuation of Investments

(g) Listed investments have been designated upon initial recognition as fair value through profit or loss. Investments are recognised and de-recognised at trade date where a purchase or sale is under a contract whose terms require delivery within the time frame established by the market concerned, and are initially measured at cost. Subsequent to initial recognition, investments are valued at fair value which for listed investments is deemed to be bid market or last traded prices. Gains and losses arising from changes in fair value are included as a capital item in the Income Statement and are ultimately recognised in the Capital Reserve. In accordance with the guidance given in the Association of Investment Companies SORP issued in January 2009 the Capital Reserve is not separated into realised and unrealised.

(h) Equities include ordinary shares and warrants.

(i) Gains and losses arising on realisation of investments are shown in the Capital Reserve.

# Accounting Policies – continued

## Foreign currency

(j) Exchange rate differences on capital items are included in the Capital Reserve, and on income items in the Revenue Reserve.

(k) All assets and liabilities denominated in foreign currencies have been translated at year end exchange rates.

## Cash and liquid resources

(l) Cash and liquid resources include cash at hand, deposits held on call with banks and other short term highly liquid investments with maturities of three months or less.

## Long term borrowings and finance costs

(m) Long term borrowings are carried in the Balance Sheet at fair value. Finance costs of such borrowings are charged to capital in the period in which they are incurred. Interest costs incurred on long-term borrowings are charged to income on a time apportioned basis over the life of the liability. Breakage costs are charged to capital.

## Dividends

(n) Interim dividends are recognised in the period in which they are paid and final dividends are recognised in the period in which they are approved by the Company's shareholders.

## Taxation

(o) In accordance with Financial Reporting Standard 19, deferred taxation is provided using the liability method on all timing differences, calculated at the rate at which it is anticipated the timing differences will reverse. Deferred tax assets are recognised only when, on the basis of available evidence, it is more likely than not that there will be taxable profits in the future against which the deferred tax asset can be offset.

Owing to the Company's status as an investment trust, and the intention to continue to meet the conditions required to obtain approval in the foreseeable future, the Company has not provided deferred tax on any capital gains and losses arising on the revaluation of investments.

# Notes on the Accounts

## 1. Income

Income from investments relates to dividends. Other income relates to bank deposit interest and £27,000 (2010: £7,000) in relation to Taiwan tax reclaims from overseas listed companies.

| 2. Investment Management Fee | 2011 £000 | 2010 £000 |
|---|---|---|
| Performance fee | **2,405** | 937 |
| Investment management fee | **1,452** | 1,131 |
| | **3,857** | 2,068 |

The basis of calculation of the investment management fee and performance fee is given on page 21.

| 3. Other Administrative Expenses | 2011 £000 | 2010 £000 |
|---|---|---|
| Auditor's remuneration for: | | |
| – audit | **12** | 12 |
| – tax services | **4** | — |
| Directors' fees | **78** | 69 |
| Company secretarial fees | **75** | 51 |
| Bank, custodial and other expenses | **292** | 191 |
| | **461** | 323 |

Since 1st July 2011 Directors' fees have been as follows:

| | |
|---|---|
| Chairman of the Board | £23,500 per annum |
| Each other Director | £17,000 per annum |

Prior to 1st July 2011 Directors' fees were as follows:

| | |
|---|---|
| Chairman of the Board | £22,500 per annum |
| Each other Director | £16,000 per annum |

| 4. Finance Costs of Borrowing | 2011 Revenue £000 | 2011 Capital £000 | 2011 Total £000 | 2010 £000 |
|---|---|---|---|---|
| Costs in relation to bank borrowing | **18** | **54** | **72** | — |

# Notes on the Accounts – continued

## 5. Taxation

### (a) Analysis of charge in period

| | 2011 Revenue £000 | 2011 Capital £000 | 2011 Total £000 | 2010 Revenue £000 | 2010 Capital £000 | 2010 Total £000 |
|---|---|---|---|---|---|---|
| Current tax: | | | | | | |
| Prior year adjustment | — | — | — | (30) | — | (30) |
| Overseas tax | **352** | — | **352** | 319 | 129 | 448 |
| | **352** | — | **352** | 289 | 129 | 418 |

### (b) Factors affecting the tax charge for the period

The tax assessed for the period is different from that calculated when corporation tax is applied to the total return. The differences are explained below:

| | 2011 £000 | 2010 £000 |
|---|---|---|
| Net gains on investments during the period | **20,237** | 52,760 |
| Other gains | **470** | 825 |
| Performance fee | **(2,405)** | (937) |
| Finance costs of borrowing | **(54)** | — |
| Net investment income before tax | **3,795** | 3,486 |
| **Total return for the period before taxation** | **22,043** | 56,134 |
| Total return for the period before taxation multiplied by the effective rate of corporation tax of 27.16% (2010: 28%) | **5,987** | 15,718 |
| Effect of: | | |
| Capital returns not subject to corporation tax | **(5,624)** | (15,004) |
| Prior year adjustment | — | (30) |
| Non-taxable income | **(1,547)** | (1,383) |
| Overseas tax | **352** | 448 |
| Movement on excess expenses | **1,184** | 669 |
| **Current tax charge for the period** | **352** | 418 |

Under changes enacted in the Finance Act 2009, dividends and other distributions received from foreign companies from 1st July 2009 are largely exempt from corporation tax.

### (c) Provision for deferred tax

The Company has a deferred tax asset of £1,755,000 at 31st August 2011 in respect of unrelieved tax losses carried forward. This asset has not been recognised in the accounts as it is unlikely under current legislation that it will be capable of being offset against future taxable profits.

# Notes on the Accounts – continued

## 6. Dividends

| | 2011 £000 | 2010 £000 |
|---|---|---|
| Dividends paid in the period: | | |
| Dividend of 8.50p per share (2010 - 6.00p) paid 28th January 2011 | **2,568** | 1,813 |

We note below the proposed dividend in respect of the financial year, which is the basis upon which the requirements of section 1158 of the Corporation Tax Act 2010 are considered. The proposed dividend is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements.

| | 2011 £000 | 2010 £000 |
|---|---|---|
| Income available for distribution | **3,443** | 3,197 |
| Proposed dividend for the year ended 31st August 2011 – 9.00p (2010 – 8.50p) payable 10th February 2012 | **(2,719)** | (2,568) |
| Retained income for section 1158 Corporation Tax Act 2010 purposes | **724** | 629 |

## 7. Return per Ordinary Share

| | 2011 Revenue p | 2011 Capital p | 2011 Total p | 2010 Revenue p | 2010 Capital p | 2010 Total p |
|---|---|---|---|---|---|---|
| Net return per ordinary share | **11.39** | **60.40** | **71.79** | 10.58 | 173.83 | 184.41 |

| | 2011 | 2010 |
|---|---|---|
| Revenue return | **£3,443,000** | £3,197,000 |
| Capital return | **£18,248,000** | £52,519,000 |
| Weighted average ordinary shares in issue | **30,213,650** | 30,213,650 |

There are no dilutive or potentially dilutive shares in issue.

# Notes on the Accounts – continued

## 8. Equity Investments

| | £000 |
|---|---|
| Cost at 31st August 2010 | 109,122 |
| Unrealised appreciation | 46,586 |
| Valuation at 31st August 2010 | 155,708 |
| Purchases at cost* | 57,896 |
| Sales – proceeds* | (56,292) |
| Sales – realised gains on sales | 30,867 |
| Unrealised depreciation on investments in the year | (10,630) |
| **Valuation at 31st August 2011** | 177,549 |
| Cost at 31st August 2011 | 141,593 |
| **Closing unrealised appreciation** | 35,956 |

All investments are listed on recognised stock exchanges.
*These figures include the following charges.

| | Transaction Costs | | |
|---|---|---|---|
| | Purchases £000 | Sales £000 | Total £000 |
| Stamp duty | 31 | 104 | 135 |
| Brokerage | 138 | 159 | 297 |
| Other fees | 10 | 12 | 22 |
| | 179 | 275 | 454 |

## 9. Debtors

| | **2011 £000** | 2010 £000 |
|---|---|---|
| Sales awaiting settlement | **—** | 450 |
| Accrued income | **763** | 679 |
| Overseas tax recoverable | **236** | 183 |
| VAT recoverable | **—** | 2 |
| | **999** | 1,314 |

## 10. Creditors (amounts falling due within one year)

| | **2011 £000** | 2010 £000 |
|---|---|---|
| Purchases awaiting settlement | **143** | 626 |
| Performance fee | **2,405** | 937 |
| Finance costs of borrowing | **21** | — |
| Interest due on loan | **18** | — |
| Other creditors | **441** | 344 |
| | **3,028** | 1,907 |

# Notes on the Accounts – continued

| 11. Creditors (amounts falling due after one year) | 2011 £000 | 2010 £000 |
|---|---|---|
| US$32,500,000 fixed rate loan 2.191% 12/08/14 | **19,960** | — |

The main covenants relating to the loan are that total net assets shall not fall below £80 million and the ratio of adjusted total net assets to debt shall exceed 3.333 to 1. There were no breaches of loan covenants during the year.

## 12. Share Capital

The authorised capital is £8,190,058 (2010: same) represented by 32,760,234 ordinary shares of 25p each (2010: same). The allotted capital is £7,553,412 (2010: same) represented by 30,213,650 ordinary shares of 25p each (2010: same).

The Board monitors and reviews the broad structure of the Company's capital on an ongoing basis. This will include:

– the level of equity shares in issue; and

– the extent to which revenue in excess of that which is required to be distributed should be retained.

Other than the loan covenants described in note 11 the Company does not have any externally imposed capital requirements. The capital of the Company is the ordinary share capital as detailed above. It is managed in accordance with its investment policy in pursuit of its investment objective, both of which are detailed on page 3.

| 13. Reserves | Share Premium Account £000 | Warrant Reserve Exercised £000 | Capital Reserve £000 | Revenue Reserve £000 |
|---|---|---|---|---|
| Balance at 31st August 2010 | 21,337 | 1,319 | 131,255 | 6,300 |
| Realised gain on investments | — | — | 30,867 | — |
| Currency gain | — | — | 470 | — |
| Unrealised depreciation on investments in the year | — | — | (10,630) | — |
| Performance fee | — | — | (2,405) | — |
| Finance costs of borrowing | — | — | (54) | — |
| Income retained in the year | — | — | — | 3,443 |
| Dividend paid in year | — | — | — | (2,568) |
| **Balance at 31st August 2011** | **21,337** | **1,319** | **149,503** | **7,175** |

The capital reserve includes investment holding gains amounting to £35,956,000 (2010: £46,586,000), as disclosed in note 8. The revenue reserve is distributable by way of dividend.

## 14. Net Asset Value per Ordinary Share

Net assets per share are based on total net assets of £186,888,000 (2010: £167,765,000) divided by 30,213,650 (2010: same) ordinary shares of 25p each in issue.

# Notes on the Accounts – continued

## 15. Cash Flow Statement

### (a) Reconciliation of total income to net cash inflow from operating activities

| | 2011 £000 | 2010 £000 |
|---|---|---|
| Income | **5,726** | 4,940 |
| Administration expenses | **(1,913)** | (1,454) |
| Decrease/(increase) in debtors | **2** | (1) |
| Decrease in dividends accounted for but not yet received | **(84)** | (266) |
| Increase in creditors | **115** | 97 |
| **Net cash inflow from operating activities** | **3,846** | 3,316 |

### (b) Analysis of changes in cash and net debt during the year

| | At the Start of the Year £000 | Cash Flows £000 | Non-cash Changes £000 | At the End of the Year £000 |
|---|---|---|---|---|
| Cash | 12,650 | 18,678 | – | 31,328 |
| Loan due between one and five years | – | (19,813) | (147) | (19,960) |
| | 12,650 | (1,135) | (147) | 11,368 |

## 16. Risk Management, Financial Assets and Liabilities

The Company invests mainly in smaller Asian quoted companies. Other financial instruments comprise cash balances, short-term debtors, creditors and a fixed rate loan. The Investment Manager follows the investment process outlined on page 3 and in addition the Board conducts quarterly reviews with the Investment Management team. The Investment Manager's Risk and Compliance department monitors the Company's investment and borrowing powers to ensure that risks are controlled and minimised. Additionally, its Compliance and Risk Committee reviews risk management processes monthly.

The main risks that the Company faces from its financial instruments are market prices (comprising interest rate, currency and share price risks) and credit risk. As the Company's assets are mainly in readily realisable securities, other than in exceptional circumstances there is no significant liquidity risk. The Board, in conjunction with the Investment Manager, regularly reviews and agrees policies for managing each of these risks. The Investment Manager's policies for managing these risks are detailed below.

*Market Risk*

The fair value of, or future cash flows from, a financial instrument held by the Company will fluctuate because of changes in market prices. These valuations are deemed to represent the fair value of the investments.

# Notes on the Accounts – continued

## *Interest Rate Risk*

As the Company does not invest in either fixed or floating rate securities at present, interest rate risk exposure is restricted to interest receivable on bank deposits or interest payable on bank overdraft positions which will be affected by fluctuations in interest rates.

The possible effects on fair value and cash flows that could arise as a result of changes in interest rates are taken into account when making investment and borrowing decisions.

Movements in interest rates, to the extent that they affect the fair value of the Company's fixed rate borrowings, may also affect the amount by which the Company's share price is at a discount or a premium to the net asset vaue (assuming that the Company's share price is unaffected by movements in interest rates). During the year the Company drew down a US$32.5 million three year fixed rate bank loan.

## *Foreign Currency Risk*

The majority of the Company's assets, liabilities and income are denominated in currencies other than sterling (the currency which the Company reports its results) as at 31st August 2011. The Balance Sheet therefore can be significantly affected by movements in foreign exchange rates. It is not the Company's policy to hedge this risk on a continuing basis but the Company reserves the right to undertake foreign exchange hedging of its portfolio. The revenue account is subject to currency fluctuation arising on dividends paid in foreign currencies. The Company does not hedge this currency risk.

## *Foreign Currency Risk Exposure by Currency of Denomination*

| | **31st August 2011** | | | 31st August 2010 | | |
|---|---|---|---|---|---|---|
| | **Overseas investments £000** | **Net monetary assets £000** | **Total currency exposure £000** | Overseas investments £000 | Net monetary assets £000 | Total currency exposure £000 |
| Hong Kong dollars | 45,356 | 330 | 45,686 | 36,341 | 612 | 36,953 |
| Singapore dollars | 25,565 | 6,658 | 32,223 | 19,049 | 8,905 | 27,954 |
| Korean won | 24,727 | — | 24,727 | 17,630 | — | 17,630 |
| Taiwanese dollars | 23,434 | 636 | 24,070 | 20,284 | 1,511 | 21,795 |
| Malaysian ringgits | 15,724 | 77 | 15,801 | 12,815 | 62 | 12,877 |
| Thai baht | 15,691 | 37 | 15,728 | 20,035 | (162) | 19,873 |
| Indonesian rupiahs | 7,848 | — | 7,848 | 9,325 | 56 | 9,381 |
| Philippine pesos | 7,701 | — | 7,701 | 9,645 | — | 9,645 |
| Sterling | 2,299 | 1,597 | 3,896 | 2,207 | 1,004 | 3,211 |
| Sri Lankan rupees | 2,871 | — | 2,871 | 3,609 | 72 | 3,681 |
| Indian rupees | 2,764 | 19 | 2,783 | 2,542 | — | 2,542 |
| US dollars | 1,935 | (15) | 1,920 | 2,226 | (3) | 2,223 |
| Chinese yuan | 1,634 | — | 1,634 | — | — | — |
| Total | **177,549** | **9,339** | **186,888** | 155,708 | 12,057 | 167,765 |

# Notes on the Accounts – continued

### *Other Price Risk*

Changes in market prices, other than those arising from interest rate or currency risk, will affect the value of quoted investments. It is the Board's policy to hold an appropriate spread of investments in the portfolio in order to reduce the risk arising from factors specific to a particular country or sector. The Investment Manager monitors market prices throughout the year and reports to the Board on a regular basis.

### *Other Price Risk Sensitivity*

If market values at the Balance Sheet date had been 10% higher or lower with all other variables remaining constant, the return attributable to ordinary shareholders for the year ending 31st August 2011 would have increased/(decreased) by £18,689,000 (2010 increased/(decreased) by £16,776,000) and equity reserves would have increased/(decreased) by the same amount.

### *Credit Risk*

This is the risk that a failure of a counterparty to a transaction to discharge its obligations under that transaction could result in a loss to the Company.

Investment transactions are carried out with a large number of approved brokers, whose credit-standing is reviewed periodically by the Investment Manager.

Cash exposures are carefully managed to ensure that money is placed on deposit with reputable counterparties meeting a minimum credit rating.

In summary, compared to the amounts in the Balance Sheet, the maximum exposure to credit risk at 31st August 2011 was as follows:

| | **2011** | | 2010 | |
|---|---|---|---|---|
| **Current assets** | **Balance sheet £000** | **Maximum exposure £000** | Balance sheet £000 | Maximum exposure £000 |
| Receivables | **999** | **999** | 1,314 | 1,314 |
| Cash at bank | **31,328** | **31,328** | 12,650 | 12,650 |
| | **32,327** | **32,327** | 13,964 | 13,964 |

## 17. Related Party Transactions

The Directors' fees for the year are detailed in the Directors' Remuneration Report on pages 29 and 30. No Director has a contract of service with the Company. During the year no Director was interested in any matter requiring disclosure under section 412 of the Companies Act 2006.

# Report of the Independent Auditor

## *Independent Auditor's Report to the members of The Scottish Oriental Smaller Companies Trust PLC*

We have audited the financial statements of The Scottish Oriental Smaller Companies Trust PLC for the year ended 31st August 2011 which comprise the Income Statement, the Balance Sheet, the Cash Flow Statement, the Reconciliation of Movements in Shareholders' Funds and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the Company's members, as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006. 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 auditor*

As explained more fully in the Directors' Responsibilities Statement set out on page 31, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

## *Scope of the audit of the financial statements*

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

## *Opinion on financial statements*

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31st August 2011 and of its return for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

# Report of the Independent Auditor – continued

### *Opinion on other matters prescribed by the Companies Act 2006*

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

### *Matters on which we are required to report by exception*

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statement, set out on page 22, in relation to going concern;
- the part of the Directors' Statement on Corporate Governance relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review; and
- certain elements of the report to the shareholders by the Board on directors' remuneration.

**Kenneth McDowell CA (Senior Statutory Auditor)**
For and on behalf of CHIENE + TAIT
Chartered Accountants & Statutory Auditor
61 Dublin Street
Edinburgh
EH3 6NL

31st October 2011

# Notice of Annual General Meeting

Notice is hereby given that the Annual General Meeting of The Scottish Oriental Smaller Companies Trust PLC will be held at 23 St Andrew Square, Edinburgh on 6th February 2012 at 12.15 pm for the purpose of transacting the following business:

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

1. To receive the reports of the Directors and Auditors and to adopt the Report and Accounts for the financial year ended 31st August 2011.

2. To approve the dividend of 9.00p per ordinary share of 25p each in the capital of the Company.

3. To re-elect James Ferguson as a Director. James Ferguson's biographical details can be found on page 5 of the Report and Accounts.

4. To re-elect Alexandra Mackesy as a Director. Alexandra Mackesy's biographical details can be found on page 5 of the Report and Accounts.

5. To re-elect Dr Janet Morgan as a Director. Dr Janet Morgan's biographical details can be found on page 5 of the Report and Accounts.

6. To re-appoint Chiene + Tait, Chartered Accountants and Statutory Auditor, as Auditor and to authorise the Directors to fix their remuneration.

7. To approve the Directors' Remuneration Report within the Report and Accounts for the financial year ended 31st August 2011.

8. That, in substitution for any existing authority, but without prejudice to the exercise of any such authority prior to the date hereof, the Directors of the Company be and are hereby generally and unconditionally authorised in accordance with Section 551 of the Companies Act 2006 (the "Act") to exercise all the powers of the Company to allot shares in the Company and to grant rights to subscribe for or to convert any security into shares in the Company ("Securities") provided that such authority shall be limited to the allotment of shares and the grant of rights in respect of shares with an aggregate nominal value of up to £636,646, such authority to expire at the conclusion of the next Annual General Meeting of the Company after the passing of this resolution or on the expiry of 15 months from the passing of this resolution, whichever is the earlier, unless previously revoked, varied or extended by the Company in a general meeting, save that the Company may at any time prior to the expiry of this authority make an offer or enter into an agreement which would or might require Securities to be allotted or granted after the expiry of such authority and the Directors shall be entitled to allot or grant Securities in pursuance of such an offer or agreement as if such authority had not expired.

To consider and, if thought fit, pass the following resolutions as special resolutions of the Company:

9. That, subject to the passing of resolution number 8 above, and in substitution for any existing power but without prejudice to the exercise of any such power prior to the date hereof, the Directors of the Company be and are hereby generally empowered, pursuant to Section 570 of the Companies Act 2006 (the "Act"), to allot equity securities (as defined in Section 560 of the Act), including the grant of rights to subscribe for, or to convert securities into ordinary shares held by the Company as treasury shares (as defined in Section 724 of the Act) for cash pursuant to the authority given by resolution number 8 above as if Section 561(1) of the Act did not apply to any such allotment of equity securities, provided that this power:

# Notice of Annual General Meeting – continued

(a) expires at the conclusion of the next Annual General Meeting of the Company after the passing of this resolution or on the expiry of 15 months from the passing of this resolution, whichever is the earlier, 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 Directors may allot equity securities in pursuance of any such offer or agreement as if the power conferred hereby had not expired; and

(b) shall be limited to the allotment of equity securities up to an aggregate nominal value of £377,670 being approximately 5% of the nominal value of the issued share capital of the Company, (excluding treasury shares) as at 31st October 2011.

10. That, in substitution for any existing authority but without prejudice to the exercise of any such authority prior to the date hereof, the Company be and is hereby generally and unconditionally authorised, pursuant to and in accordance with section 701 of the Companies Act 2006 (the “Act”) to make market purchases (within the meaning of section 693(4) of the Act) of fully paid ordinary shares of 25 pence each in the capital of the Company (“ordinary shares”) (either for retention as treasury shares for future reissue, resale or transfer or for cancellation), provided that:

(a) the maximum aggregate number of ordinary shares hereby authorised to be purchased is 4,532,047 ordinary shares representing 14.99% of the Company’s issued share capital (excluding treasury shares);

(b) the minimum price (excluding expenses) which may be paid for each ordinary share is 25 pence;

(c) the maximum price (excluding expenses) which may be paid for each ordinary share shall not be more than the higher of:

(i) 5 per cent above the average of the middle market quotations (as derived from the daily official list of the London Stock Exchange) for the ordinary shares over the five business days immediately preceding the date of purchase; and

(ii) the higher of the last independent trade and the highest current independent bid on the London Stock Exchange; and

(d) unless previously varied, revoked or renewed by the Company in a general meeting, the authority hereby conferred shall expire at the conclusion of the Company’s next Annual General Meeting or 15 months from the passing of this Resolution 10, whichever is the earlier, save that the Company may, prior to such expiry, enter into a contract to purchase ordinary shares under such authority which will or might be completed or executed wholly or partly after the expiration of such authority and may make a purchase of ordinary shares pursuant to any such contract.

11. That the Company be and is hereby generally and unconditionally authorised to hold general meetings (other than annual general meetings) on 14 clear days’ notice, such authority to expire at the conclusion of the next annual general meeting of the Company.

Dated: 31st October 2011 — By Order of the Board

Registered Office:
10 St. Colme Street
Edinburgh EH3 6AA

Steven K Davidson
*Company Secretary*

# Notice of Annual General Meeting – continued

*Notes*

(1) To be entitled to attend and vote at the meeting (and for the purpose of the determination by the Company of the number of votes they may cast), members must be entered on the Company's register of members at close of business on 2nd February 2012 ("the specified time"). If the meeting is adjourned to a time not more than 48 hours after the specified time applicable to the original meeting, the specified time will also apply for the purpose of determining the entitlement of members to attend and vote (and for the purpose of determining the number of votes they may cast) at the adjourned meeting. If, however, the meeting is adjourned for a longer period then, to be so entitled, members must be entered on the Company's register of members at the time which is 48 hours (excluding non working days) before the time fixed for the adjourned meeting or, if the Company gives notice of the adjourned meeting, at the time specified in that notice.

(2) If you wish to attend the meeting in person, you should present your attendance card, attached to their Form of Proxy, to the registration desk on the day of the meeting. Alternatively, please ensure you pre-register in accordance with the instructions on your Form of Proxy. Failure to do so may result in your being prohibited from voting on resolutions during the meeting. These forms must be submitted no later than 12.15 pm on 2nd February 2012. Attendance by non shareholders will be at the discretion of the Company.

(3) Information regarding the Annual General Meeting, including information required by section 311A of the Companies Act 2006, is available from www.scottishoriental.com.

(4) Holders of ordinary shares who are entitled to attend and vote at the meeting convened by the foregoing notice may appoint one or more proxies (who need not be a member or members) to attend, speak and vote in their place. If appointing more than one proxy, each proxy must be appointed to exercise rights attaching to different shares held by the holder. The instruments appointing a proxy and the power of attorney or other authority (if any) under which it is signed or a notarially certified copy of that power or authority must be delivered to the offices of the Company's Registrars, Computershare Investor Services PLC, PO Box 1075, Bristol, BS99 3FA or www.eproxyappointment.com; (i) in the case of a meeting or adjourned meeting, 48 hours (excluding non-working days) before the time for holding the meeting or adjourned meeting; or (ii) in the case of a poll taken 48 hours after it was demanded, 24 hours before the time appointed for the taking of the poll. Return of a completed form of proxy will not preclude a member from attending and voting personally at the meeting. Members may not use any electronic address provided in this notice or in any related documents to communicate with the Company for any purpose other than those expressly stated.

(5) CREST members who wish to appoint a proxy or proxies through the CREST electronic proxy appointment service may do so by using the procedures described in the CREST Manual and by logging on to the website www.euroclear.com/CREST. CREST personal members or other CREST sponsored members, and those CREST members who have appointed a voting service provider(s), should refer to their CREST sponsor or voting service provider(s), who will be able to take the appropriate action on their behalf.

(6) In order for a proxy appointment or instruction made using the CREST service to be valid, the appropriate CREST message (a "CREST Proxy Instruction") must be properly authenticated in accordance with Euroclear UK & Ireland Limited's specifications, and must contain the information required for such instruction, as described in the CREST Manual. The message, regardless of whether it constitutes the appointment of a proxy or is an amendment to the instruction given to a previously appointed proxy, must, in order to be valid, be transmitted so as to be received by the Company's registrar (ID number 3RA50) no later 48 hours (excluding non-working days) before the time of the meeting or any adjournment.

# Notice of Annual General Meeting – continued

For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by the CREST Application Host) from which the Company's registrar is able to retrieve the message by enquiry to CREST in the manner prescribed by CREST. After this time any change of instructions to proxies appointed through CREST should be communicated to the appointee through other means.

(7) CREST members and, where applicable, their CREST sponsors, or voting service providers should note that Euroclear UK & Ireland Limited does not make available special procedures in CREST for any particular message. Normal system timings and limitations will, therefore, apply in relation to the input of CREST Proxy Instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member is a CREST personal member, or sponsored member, or has appointed a voting service provider(s), to procure that his CREST sponsor or voting service provider(s) take(s)) such action as shall be necessary to ensure that a message is transmitted by means of the CREST system by any particular time. In this connection, CREST members and, where applicable, their CREST sponsors or voting system providers are referred, in particular, to those sections of the CREST Manual concerning practical limitations of the CREST system and timings.

(8) The Company may treat as invalid a CREST Proxy Instruction in the circumstances set out in Regulation 35(5)(a) of the Uncertificated Securities Regulations 2001.

(9) The letters of appointment of the Directors are available for inspection at 10 St. Colme Street, Edinburgh EH3 6AA before, during and after the meeting. They will also be available on the date of the meeting at 23 St Andrew Square, Edinburgh from 12 pm until the conclusion of the meeting.

(10) As at close of business on 31st October 2011, the Company's issued share capital comprised 30,213,650 ordinary shares of 25p each. Each ordinary share carries the right to one vote at a general meeting of the Company and, therefore, the total number of voting rights in the Company as at 31st October 2011 is 30,213,650.

(11) Any person holding 3% of the total voting rights in the Company who appoints a person other than the Chairman as his proxy will need to ensure that both he and such third party complies with their respective disclosure obligations under the Disclosure and Transparency Rules.

(12) Under section 319A of the Companies Act 2006, the Company must answer any question relating to the business being dealt with at the meeting put by a member attending the meeting unless:

(a) answering the question would interfere unduly with the preparation for the meeting or involve the disclosure of confidential information;
(b) the answer has already been given on a website in the form of an answer to a question; or
(c) it is undesirable in the interests of the Company or the good order of the meeting that the question be answered.

(13) The members of the Company may require the Company (without payment) to publish, on its website, a statement (which is also to be passed to the auditors) setting out any matter relating to the audit of the company's accounts, including the auditors report and the conduct of the audit. The Company will be required to do so once it has received such requests from either members representing at least 5% of the total voting rights of the Company or at least 100 members who have a relevant right to vote and hold shares in the Company on which there has been paid up an average sum per member of at least £100. Such requests must be made in writing and must state your full name and address and be sent to the Company at 10 St. Colme Street, Edinburgh EH3 6AA.

(14) Members meeting the threshold requirements set out in the Companies Act 2006 have the right (a) to require the Company to give notice of any resolution which can properly be, and is to be, moved at the meeting pursuant to Section 338 of the Companies Act 2006, and/or (b) to include a matter in the business to be dealt with at the meeting, pursuant to Section 338A of the Companies Act 2006.

(15) Any corporation which is a member can appoint one or more corporate representatives. Members can only appoint more than one corporate representative where each corporate representative is appointed to exercise rights attached to different shares. Members cannot appoint more than one corporate representative to exercise the rights attached to the same share(s).

(16) In the case of joint holders, where more than one of the joint holders purports to appoint one or more proxies, only the purported appointment submitted by the most senior holder will be accepted. Seniority is determined by the order in which the names of the joint holders appear in the Company's register of members in respect of the joint holding (the first named being the most senior).

(17) Any person to whom this notice is sent who is a person nominated under section 146 of the Companies Act 2006 to enjoy information rights (a "Nominated Person") may, under an agreement between him/her and the member by whom he/she was nominated, have a right to be appointed (or to have someone else appointed) as a proxy for the meeting. If a Nominated Person has no such proxy appointment right or does not wish to exercise it, he/she may, under any such agreement, have a right to give instructions to the member as to the exercise of voting rights.

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