

Shires Smaller Companies plc



INTERIM REPORT
30 JUNE 2004

MANAGED BY

GLASGOW
INVESTMENT MANAGERS

Contents

Objective	1
Financial Highlights	1
Performance	1
Chairman's Statement	3
Consolidated Statement of Total Return	4
Group Balance Sheet	6
Consolidated Cash Flow Statement	7
Analysis of Changes in Net Debt	7
Analysis of Equity Portfolio	8
Portfolio of Investments	9
Distribution of Assets	10

Objective

The objective of the Company is to provide a high and growing dividend and capital growth from a portfolio invested principally in the ordinary shares of smaller UK companies and UK fixed income securities.

Financial Highlights

	As at 30 June 2004	As at 31 December 2003	%
			change
Total assets less current liabilities	£69.52m	£64.64m	+7.5
Shareholders' funds	£43.26m	£38.87m	+11.3
Net asset value per share	197.7p	177.6p	+11.3
Share price	189.0p	184.0p	+2.7
(Discount)/Premium (share price to net asset value)	(4.4%)	3.6%	
Dividends per share	6.0p	6.0p*	

* Half year to 30 June 2003.

Performance

(periods to 30 June 2004)

	6 months	1 year	3 years	5 years
	%	%	%	%
Shires Smaller Companies plc				
– Net asset value total return	14.7▲	27.7†	11.2‡	32.9‡
– Share price total return	6.0▲	29.8†	16.9‡	63.7‡
FTSE SmallCap Index (excluding Investment Companies)‡	6.0	25.9	(2.3)	14.0
FTSE All-Share Index‡	2.8	16.9	(10.1)	(12.8)

Performance

(Continued)

Performance

Year to:	30 June 2000	30 June 2001	30 June 2002	30 June 2003	30 June 2004
	16.7%†	20.1%†	5.1%†	(14.3)%†	29.8%†

Mid to mid closing share price, net income re-invested.

Past performance should not be seen as an indication of future performance.

	As at 30 June 2004	As at 31 December 2003
Net Dividend Yield		
Shires Smaller Companies plc▲	7.3%•	7.5%
FTSE SmallCap Index (excluding Investment Companies)‡	2.4%	2.5%
FTSE All-Share Index‡	3.2%	3.1%

▲ Source: Glasgow Investment Managers Limited.

† Source: Prepared for the Association of Investment Trust Companies by Fundamental Data.

‡ Source: Datastream.

• Based on share price and last four quarterly dividends.

Chairman's Statement

Financial Highlights

I am pleased to report that the first half of the Company's financial year saw continued progress. The net asset value per share rose by 11.3% from 177.6p to 197.7p. Dividends paid and declared to date are at the same level as last year, producing a dividend yield of 7.3% based upon the share price of 189p at 30 June 2004.

Investment Returns

The total return on net assets was 14.7%, significantly above the return of 6.0% on the FTSE SmallCap Index (excluding Investment Companies), the Company's benchmark. Larger quoted UK companies continued to perform less well than smaller companies with the FTSE All-Share Index rising by 2.8% over the same period.

The total return to shareholders at 6.0% was lower than the return on net assets, reflecting the fact that the premium of 3.6% at which the share price stood to net asset value per share at 31 December 2003 gave way to a small discount of 4.4% at 30 June 2004. The total return to shareholders was, however, still in line with that of the Company's benchmark.

Earnings and Dividends

The revenue return per share was 6.9p over the six months to 30 June 2004. On 6 July 2004 the Board declared a second interim dividend of 3.0p per share which was paid on 30 July 2004 to shareholders on the register at close of business on 16 July 2004. A first interim dividend of 3.0p per share was paid on 30 April 2004. Total dividends paid and declared to date in 2004 therefore total 6.0p, the same level as last year.

Portfolio Profile

The distribution of assets shows that 100.2% of net assets was invested in ordinary shares compared with 98.7% at 31 December 2003. Total gearing at 30 June 2004 was 65.6% of net assets, down from 72.2%, due to the rise in value of the Company's portfolio of ordinary shares. All of this gearing is invested in the high-yielding fixed income securities which make a major contribution to the high level of income distributed to shareholders.

Outlook

A moderate rise in UK interest rates is expected over the next twelve months. This is aimed at slowing the consumer and housing sectors, and thereby reducing the prospects of higher inflation. Smaller companies in general have produced healthy increases in earnings and dividends in the last year and although corporate earnings growth may slow somewhat in the future, further progress is likely.



H S Cathcart
Chairman

Consolidated Statement of Total Return

(incorporating the Revenue Account)

for the half year ended 30 June 2004

	Half year to 30 June 2004 (unaudited)		Total £000
	Revenue £000	Capital £000	
Gains on investments	–	5,067	5,067
Dividends and interest receivable	1,993	–	1,993
Profits less losses of dealing subsidiary	35	–	35
Underwriting commission	2	–	2
Investment management fee	(143)	(143)	(286)
Other administrative expenses	(128)	–	(128)
Net return before finance costs and taxation	1,759	4,924	6,683
Finance costs of borrowings	(247)	(247)	(494)
Zero coupon finance	–	(484)	(484)
Return on ordinary activities before taxation	1,512	4,193	5,705
Taxation	–	–	–
Return on ordinary activities after taxation for the period	1,512	4,193	5,705
Dividends on equity shares	(1,313)	–	(1,313)
Transfer to reserves	199	4,193	4,392
Return per share	6.91p	19.16p	26.07p
Dividends per share	6.00p		

Consolidated Statement of Total Return

(Continued)

Half year to 30 June 2003 (unaudited)			Year to 31 December 2003 (audited)		
Revenue £000	Capital £000	Total £000	Revenue £000	Capital £000	Total £000
–	4,721	4,721	–	8,709	8,709
2,125	–	2,125	4,197	–	4,197
16	–	16	7	–	7
–	–	–	1	–	1
(121)	(121)	(242)	(260)	(260)	(520)
(129)	–	(129)	(283)	–	(283)
<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>
1,891	4,600	6,491	3,662	8,449	12,111
(243)	(243)	(486)	(497)	(497)	(994)
<u>–</u>	<u>(503)</u>	<u>(503)</u>	<u>–</u>	<u>(1,546)</u>	<u>(1,546)</u>
1,648	3,854	5,502	3,165	6,406	9,571
(104)	104	–	–	–	–
<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>
1,544	3,958	5,502	3,165	6,406	9,571
(1,313)	–	(1,313)	(3,009)	–	(3,009)
<u>231</u>	<u>3,958</u>	<u>4,189</u>	<u>156</u>	<u>6,406</u>	<u>6,562</u>
7.05p	18.08p	25.13p	14.46p	29.27p	43.73p
6.00p			13.75p		

Group Balance Sheet

as at 30 June 2004

	30 June 2004 (unaudited) £000	31 December 2003 (audited) £000	30 June 2003 (unaudited) £000
Fixed assets			
Listed investments			
Ordinary shares	43,360	38,354	34,813
Convertibles	2,646	2,912	3,736
Corporate bonds	23,070	23,074	23,664
Other fixed interest	2,577	2,613	1,227
	<u>71,653</u>	<u>66,953</u>	<u>63,440</u>
Current assets			
Debtors	795	734	886
Investment of dealing subsidiary	–	147	156
Cash at bank and in hand	–	465	–
	795	1,346	1,042
Creditors: amounts falling due within one year	<u>(2,925)</u>	<u>(3,655)</u>	<u>(3,296)</u>
Net current liabilities	<u>(2,130)</u>	<u>(2,309)</u>	<u>(2,254)</u>
Total assets less current liabilities	69,523	64,644	61,186
Creditors: amounts falling due after more than one year			
Long-term loan	(9,992)	(9,989)	(9,987)
Zero coupon finance	(16,269)	(15,785)	(14,702)
Net assets	<u>43,262</u>	<u>38,870</u>	<u>36,497</u>
Capital and reserves			
Called up share capital	10,943	10,943	10,943
Share premium account	11,490	11,490	11,490
Capital redemption reserve	2,032	2,032	2,032
Realised capital reserve	9,010	9,031	10,537
Unrealised capital reserve	8,610	4,396	442
Revenue reserve	1,177	978	1,053
Equity shareholders' funds	<u>43,262</u>	<u>38,870</u>	<u>36,497</u>
Net asset value per share	197.7p	177.6p	166.8p

Note: These are not statutory accounts under section 240 of the Companies Act 1985 and are unaudited. The information relating to the group balance sheet at 31 December 2003 is an extract from the latest audited accounts which have been delivered to the Registrar of Companies; the report of the auditors on these accounts was unqualified and did not contain a statement under Section 237(2) or (3) of the Companies Act 1985.

Consolidated Cash Flow Statement

for the half year ended 30 June 2004

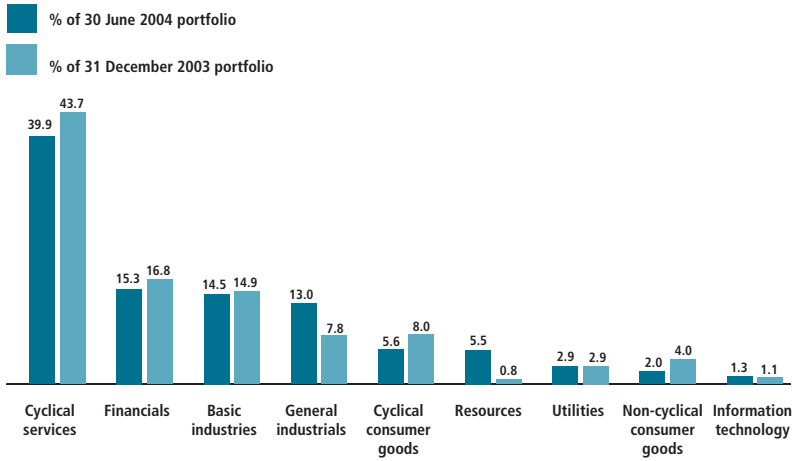
	Half year to 30 June 2004 (unaudited) £000	Half year to 30 June 2003 (unaudited) £000	Year to 31 December 2003 (audited) £000
Net cash inflow from operating activities	1,695	1,694	3,513
Servicing of finance			
Interest paid	(940)	(480)	(535)
Taxation			
Corporation tax	4	–	–
Investing activities			
Purchases of investments	(15,005)	(10,341)	(24,158)
Sales of investments	15,372	11,372	25,575
	367	1,031	1,417
Equity dividends paid	<u>(1,696)</u>	<u>(1,696)</u>	<u>(3,009)</u>
Net cash (outflow)/inflow before financing	(570)	549	1,386
Financing			
Zero coupon finance	–	–	40
Debt due within one year			
– increase/(decrease) in short-term borrowings	50	(2,000)	(1,050)
(Decrease)/increase in cash	<u>(520)</u>	<u>(1,451)</u>	<u>376</u>

Analysis of Changes in Net Debt

	As at 31 December 2003 £000	Cash flows £000	Other non-cash changes £000	As at 30 June 2004 £000
Cash at bank and in hand	465	(465)	–	–
Bank overdrafts	–	(55)	–	(55)
Short-term borrowings	(1,950)	(50)	–	(2,000)
Long-term loan	(9,989)	–	(3)	(9,992)
Zero coupon finance	(15,785)	–	(484)	(16,269)
	<u>(27,259)</u>	<u>(570)</u>	<u>(487)</u>	<u>(28,316)</u>

Analysis of Equity Portfolio

(based on value of Ordinary Shares)



Distribution of Assets

	Valuation at 31 December 2003 (audited)		Purchases	Sales	Appreciation/ (Depreciation)	Valuation at 30 June 2004 (unaudited)	
	£000	%	£000	£000	£000	£000	%
Listed investments							
Ordinary shares	38,354	98.7	3,906	(5,072)	6,172	43,360	100.2
Convertibles	2,912	7.5	—	—	(266)	2,646	6.1
Corporate bonds	23,074	59.3	5,661	(5,113)	(552)	23,070	53.3
Other fixed interest	2,613	6.7	5,438	(5,187)	(287)	2,577	6.0
	<u>66,953</u>	<u>172.2</u>	<u>15,005</u>	<u>(15,372)</u>	<u>5,067</u>	<u>71,653</u>	<u>165.6</u>
Net current liabilities	<u>(2,309)</u>	<u>(5.9)</u>				<u>(2,130)</u>	<u>(4.9)</u>
Total assets less current liabilities	64,644	166.3				69,523	160.7
Long-term loan	(9,989)	(25.7)				(9,992)	(23.1)
Zero coupon finance	(15,785)	(40.6)				(16,269)	(37.6)
Net assets	<u>38,870</u>	<u>100.0</u>				<u>43,262</u>	<u>100.0</u>
Net asset value per share	177.6p					197.7p	

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Past performance is not indicative of future performance. The price of shares and the income from them may go down as well as up and it is possible that investors may not get back the full amount invested on disposal of the shares. Changes in the rates of exchange may cause the value of overseas investments to go down or up. High income investments, in order to meet their income objectives, may charge expenses to capital which in turn may erode the capital value of the investment to less than the amount invested. Funds that invest in the securities of smaller companies are likely to carry a higher degree of risk than most funds. In certain circumstances, the Manager may enter into derivatives transactions in order to manage risk in the portfolio and generate income. The market in these instruments can be highly volatile and there is a high risk of loss. Derivatives may only be used subject to the restrictions set out for the Trust.

Investment Trusts have the facility to borrow, which is known as “gearing.” Shires Smaller Companies plc participates in gearing. Normally gearing is measured as a percentage. A gearing percentage of 110% means that an Investment Trust with equity of £100 million has £10 million of borrowing(s). The level of gearing can change quite significantly depending on fluctuations in market levels. When there is a change in value of the Investment Trust’s underlying portfolio, the use of gearing may result in exaggerated movements in the Trust’s net asset value. Gearing may also result in Investment Trust price movements being more volatile than the price movements in the Trust’s underlying investment portfolio.

The favourable tax treatment of PEPs and ISAs is subject to government legislation, and as such, may be changed. The value of tax relief will depend upon your individual circumstances.

Glasgow Investment Managers Limited,
Sutherland House,
149 St Vincent Street,
Glasgow G2 5DR
Tel: 0141 572 2700 Fax: 0141 572 2777 Email: information@gimltd.co.uk
Website: www.glasgowinvestmentmanagers.co.uk

GLASGOW

INVESTMENT MANAGERS

Authorised and regulated by the Financial Services Authority

Glasgow Investment Managers Limited, Sutherland House, 149 St Vincent Street, Glasgow G2 5DR

Tel: 0141 572 2700 Fax: 0141 572 2777 Email: information@gimltd.co.uk

Website: www.glasgowinvestmentmanagers.co.uk