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Investment Objective

The objective of the Company is to provide shareholders with long-term capital appreciation from investment in unquoted companies.
The Company provides investors with an exposure to management buy-outs, management buy-ins and expansion capital investments.

Financial Highlights

Attributable to ordinary shareholders	**At 31 December 2002**	At 31 December 2001	% change
Assets			
Net assets (£'000)	**83,837**	95,795	(12.5)
Net assets per share	**332.9p**	380.3p	(12.5)
Share price (mid-market)	**219.5p**	294.0p	(25.3)
	Year ended 31 December 2002	Year ended 31 December 2001	% change
Revenue			
Net revenue (£'000)	**2,148**	2,420	(11.2)
Earnings per share	**8.53p**	9.61p	(11.2)
Dividend per share	**8.00p**	8.00p	–

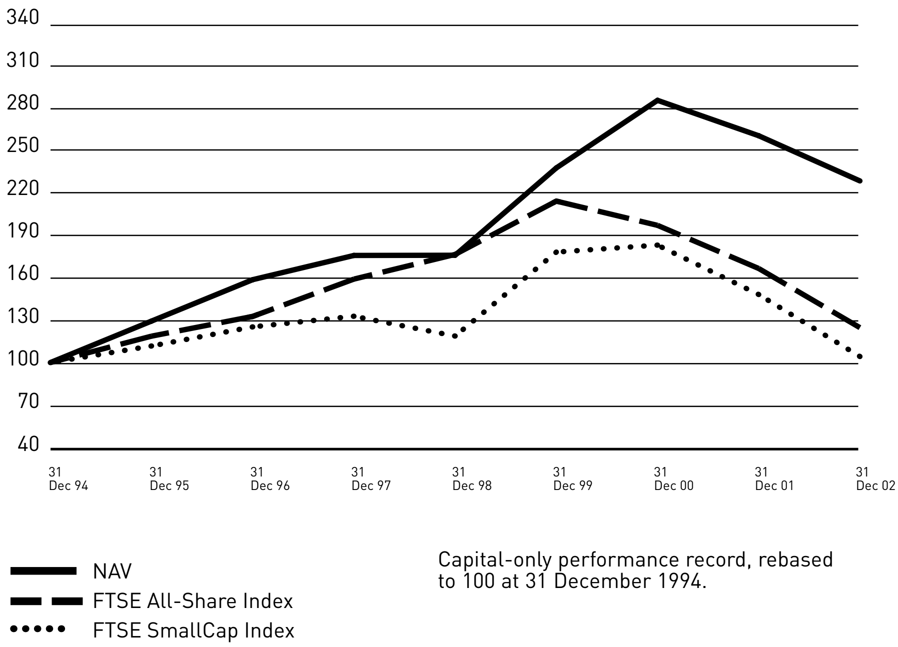
Performance Record

Year ended 31 December	Net assets attributable to ordinary shareholders £'000	Net asset value per ordinary share p	Ordinary share price p	Gross revenue £'000	Revenue available for ordinary shareholders £'000	Earnings per ordinary share p	Dividends paid per ordinary share p
1995	49,029	189.1	140.0	2,948	1,478	5.70	4.50
1996	60,313	232.6	176.0	2,717	1,276	4.92	4.50
1997	66,796	257.6	193.0	3,563	1,688	6.51	4.95
1998	66,851	257.8	208.0	2,495	1,359	5.24	4.95
1999	89,863	346.5	289.0	3,901	2,481	9.57	8.00
2000	103,521	411.0	356.5	7,332	4,623	17.89	14.50
2001	95,795	380.3	294.0	3,893	2,420	9.61	8.00
2002	**83,837**	**332.9**	**219.5**	**3,528**	**2,148**	**8.53**	**8.00**

Chairman's Statement

The Company continues to be in a good position to take advantage of investment opportunities as they arise.

NAV performance since December 1994



Capital-only performance record, rebased to 100 at 31 December 1994.

In line with the general negative trend of equity markets, the Company's net asset value per share fell over the year by 12.5%, from 380.3p at the beginning of the year to 332.9p on 31 December 2002. Over the same period, the FTSE All-Share Index and the FTSE SmallCap Index fell by 25.0% and 29.4% respectively, all in capital-only terms.

Revenue for the year was 8.53p per share, compared with 9.61p in 2001. The Board is recommending an unchanged final dividend for the year ended 31 December 2002 of 8.00p per share.

The Company invested £24.0 million in new and follow-on investments and realised £20.2 million in cash. Details are given in the Investment Manager's Review, which starts on page 3. As at 31 December 2002, the Company's cash resources amounted to £14.9 million, with an additional £25.0 million available in the form of a borrowing facility. The Company therefore continues to be in a good position to take advantage of attractive investment opportunities as they arise.

World economic uncertainty and the current situation in the Middle East will continue to have a negative impact on the outlook for 2003. Despite this, we remain optimistic that the Company is well placed for the longer term.

Although none of the Company's ordinary shares were bought back during the year, this matter is kept under constant review by the Board and we will again be seeking a renewal of the power to purchase shares in the market for cancellation at the forthcoming Annual General Meeting.

Lastly, discussions in respect of the direct contractual relationship between the Company and HgCapital rather than via Merrill Lynch Investment Managers have now been completed. The terms of the new management arrangements and related resolutions will be put to shareholders for approval at an Extraordinary General Meeting, details of which will be set out in a circular to be posted to shareholders shortly.

David Bucks
18 March 2003

Investment Manager's Review

Falling valuations create favourable buying conditions.

Economic outlook
The weak economic environment during 2002 looks likely to persist in 2003 with any positive trends being overshadowed by the overall downturn of the world's two largest economies, the US and Japan. This gloomy outlook is exacerbated by uncertainties in the Middle East.

While the UK economy has continued to outperform its peers, there are indications that activity will slow down and recession will become a reality for many businesses. However, there are some signs of optimism, particularly for industries such as healthcare, which are benefiting from the rapid expansion in Government spending.

The slump in the capital markets that prevailed throughout 2002 is unlikely to be reversed in the foreseeable future. As corporate valuations fall, the unrealistic pricing expectations of vendors, apparent in 2002, will lessen. We are taking advantage of these favourable buying conditions to make new investments and to support companies within the portfolio to make acquisitions at good prices.

In Germany, where the economic environment is bleaker still, financial pressures are forcing corporations to focus on core business interests and to dispose of peripheral activities. Notwithstanding the decision by some investors, most notably several larger banks, to reduce their presence in Germany, we are cautiously optimistic about the opportunity to deploy capital.

Investment review
During the year, the Company invested a total of £24.0 million (2001: £22.7 million) and participated in four new investments. The largest investment was in the €149 million management buy-out of automotive supplier, FTE Automotive GmbH, HgCapital's fourth deal in the German market. Two other leveraged buy-outs were completed, both in the healthcare sector: the €90 million secondary buy-out of Dutch clinical research company, Pharma Bio-Research BV, and the £56 million management buy-out of Castlebeck Group Ltd, a care homes operator. In addition, a small number of shares were purchased in Ardagh plc, the largest manufacturer of glass containers in the UK.

Realisation proceeds amounted to £20.2 million (2001: £19.5 million), most notably from the sale of PII Group to GE Power Systems.

The Company's investment performance over the year compared favourably with returns produced by quoted securities but was, nonetheless, disappointing. However, the portfolio is prudently valued and is positioned well for long-term capital gains.

Pages 4 to 19 of the report form part of the Investment Manager's Review.

The Company invests alongside other clients of HgCapital. Typically, the Company's holding forms part of a much larger stake controlled by HgCapital.

HgCapital
Investment Manager
18 March 2003

Investment Strategy

Successful private equity investing depends on taking advantage of companies and sectors that offer real potential.

HgCapital provides private equity capital to companies based in western Europe, focusing on the UK, Ireland, Germany and The Netherlands. We have developed specialist knowledge in six sectors, namely business services, consumer, healthcare, industrials, media and technology.

We seek leveraged buy-out transactions in companies with values ranging from £25 million to £250 million and provide expansion capital in excess of £10 million. We focus on businesses that have attractive economics and are experiencing favourable structural change.

We have chosen to concentrate on the "mid-market" segment for a variety of reasons. Firstly, information flows are less than perfect, companies are not always conventionally auctioned and, where they are, relationships are critical as price may not be the only criterion. Secondly, the companies tend to have more growth potential than larger enterprises. Thirdly, they offer scope for us to have a significant influence on outcomes through our close involvement. Finally, the volume of opportunities is greater. Overall, we believe that this segment of the market offers better value.

Our role is to invest capital and to support and develop excellent management teams to attain goals that we have agreed with them. Creating real economic value normally implies a mixture of growth, innovation and change, which impacts on strategy and operations.

Success in our business comes from good teamwork and from the application of energy, hard work and commercial insight, focused on the achievement of well-considered goals.

Portfolio Analysis

Falling valuations created attractive investment conditions in the healthcare and industrial sectors.

	No	£'000
New investments	4	14,627
Further investments	15	9,406
Full realisations	5	18,793
Partial realisations	6	1,453

At the end of 2002, the Company's portfolio consisted of 49 investments (2001: 50) of which the ten principal investments represented about 68% of the value excluding cash.

Four new investments were made during the year, three of which were management buy-outs within the healthcare and technology sectors. Two of these investments were in companies based in Germany and The Netherlands. This has considerably increased the Company's exposure to continental Europe in line with HgCapital's investment strategy.

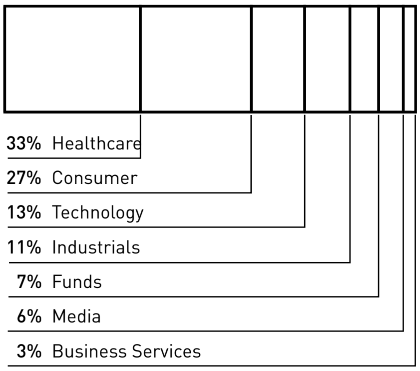
Five investments were fully realised. In addition, deferred sale proceeds were received from Braitrim Holdings Ltd (sold in 2001) and from Priory Healthcare Ltd (sold in 2000). These realisations produced an 11% uplift on carrying value and a 105% uplift from cost.

The portfolio valuation, excluding cash, is £67.7 million. This reduced valuation predominantly arises from the write-down of early-stage investments and from falls in quoted stock prices.

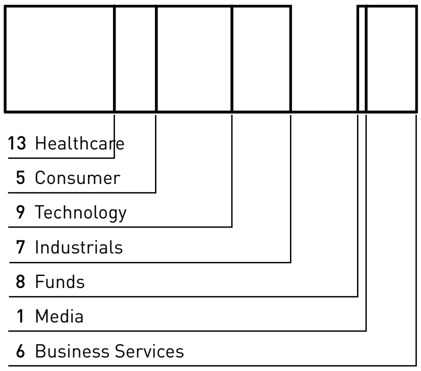
A list of investments is given on page 19.

Cash resources and an undrawn borrowing facility, amounting to £39.9 million, give the Company the financial flexibility to take advantage of an increasingly attractive environment for new investment.

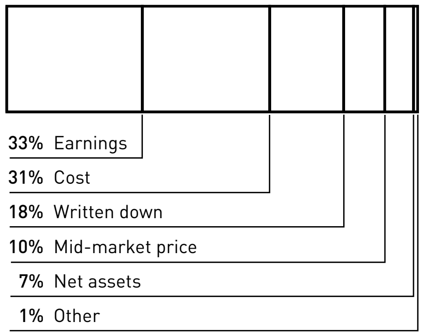
Sector by value



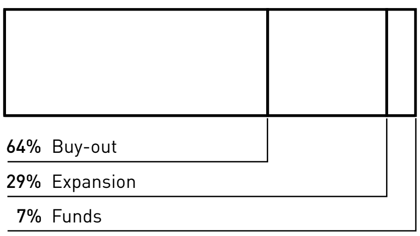
Sector by number



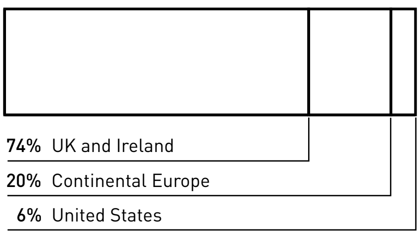
Valuation basis



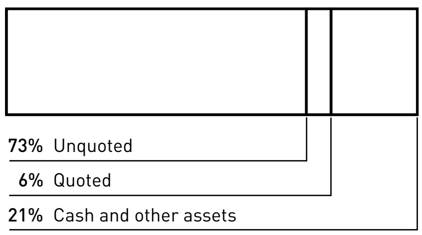
Stage



Geographic spread



Asset class



Business Services

The business services sector is broad, with several sub-sectors. A common element to each is the idea that businesses can reduce their costs and increase effectiveness by concentrating on core competencies and outsourcing other functions to specialists who can capture and share economies of scale with their customers.

The sector has been affected by the current economic slow down and by pressure to reduce prices from better-informed customers. Nonetheless, the imperative for companies to become more efficient continues to fuel the drive towards outsourcing.

HgCapital's strongest interest lies in 'white collar' business process outsourcing, such as human resources, legal services and administration. Our investment focus in the UK is targeted at companies serving industries where the use of outsourcing is less pronounced, such as insurance and professional services. In Germany, where the market is not so mature, our interest is naturally broader and encompasses all elements of the market.

Business Services Investments

Significant value was realised from two investments.

Realisations	Exit route	Residual cost £'000	Proceeds £'000
PII Group Ltd	Trade sale	6,635	17,460
Dechra Pharmaceuticals plc	Quoted sale	12	673
Braitrim Holdings Ltd	Deferred consideration	–	499
		6,647	18,632

	No	£'000
Further investments	1	207
Full realisations	2	18,632

	Stage	Residual cost £'000	Valuation £'000	Valuation basis	Portfolio value %
Patientline plc#	Expansion	413	1,720	Discount to mid-market price	2.5
SGI (Holdings) Ltd	MBO	2,966	207	Written down	0.3
Bertram Group Holdings Ltd	MBO	3,309	133	Written down	0.2
Orbis plc*	MBO	3,378	65	Mid-market price	0.1
Other (2)		313	56		0.1
		10,379	2,181		3.2

Traded on the Alternative Investment Market.
* Listed on the London Stock Exchange.

PII
We acquired PII, the world leader in the oil and gas pipeline inspection market, from British Gas in 1998, attracted by its strong core business, high market share, unique technology and potential for significant improvement in operating performance. In 1999 PII acquired its principal competitor, Pipetronix GmbH, from Preussag AG. The operations were rationalised and restructured, becoming customer-led rather than production-driven. PII Group was sold to GE Power Systems in March 2002. The total consideration amounted to £310 million in cash, which equates to a return of some four times the cost of investment. 13% of the sale proceeds, amounting to some £2.5 million for the Company, are held in escrow pending warranty claims and have not been ascribed a value.

Dechra Pharmaceuticals
Dechra Pharmaceuticals is the largest distributor of veterinary pharmaceuticals in the UK. The management buy-out completed in 1997 and the company floated on the London Stock Exchange in 2000. We realised our remaining holding during the year. Dechra delivered a strong performance over the course of our investment and yielded proceeds for the Company totalling £7.8 million, equivalent to 2.9 times overall cost.

Braitrim
Final deferred sale proceeds were received from the sale of Braitrim in 2001. This investment generated overall proceeds of £7.2 million for the Company, which equates to 1.5 times total cost.

Patientline
Patientline, originally an early-stage company in which we invested in 1996, is now the leading provider of bedside entertainment, communication and information services to UK and Dutch hospitals. The business floated on AIM in 2001 and, in May 2002, raised £35 million of new equity in order to accelerate the installation of its services in NHS hospitals in the UK. Patientline achieved strong revenue growth during the year, although its share price fell in line with general market sentiment. In total, the Company invested £3.2 million in Patientline and, in addition to the current valuation, has received cash proceeds of £4.8 million.

SGI
The management buy-out of SGI, a provider of property facilities management services, completed in 1999. Accounting irregularities led to a material over-statement of pre-acquisition profits. A warranty claim is being pursued against the vendor and a small amount of further funding was provided during the year to cover legal costs. Following a review of its business activities, the board concluded that shareholder interests were best served by a sale of the business and, in June 2002, the operating activities were sold to Babcock plc. Proceeds were used to repay bank debt.

Bertram
The management buy-out of Bertram, the UK's second-largest book wholesaler, completed in 1999. Turnover grew significantly in the first year but the expansion was mishandled and the company over-extended on the range of books offered. The business was realigned under new leadership and the banking facilities were renegotiated. The company benefited from these actions, recording a significant increase in profits in the year to June 2002. Since then, the market has deteriorated, resulting in increased pricing pressures. As profits in 2003 are unlikely to match those of 2002, we have written down this investment.

Orbis
Orbis is the UK market leader in the business of protecting empty properties. The original investment was in the management buy-out of Sitex Group, which was subsequently sold to Orbis, a quoted company, for a cash consideration and shares. Orbis has performed poorly, plans for its sale were aborted and the share price collapsed.

Consumer

HgCapital covers three principal sub-sectors of the consumer sector, namely leisure, consumer goods and retail.

Prospects for the general level of consumer spending have deteriorated across northern Europe. Accordingly, our interest is very opportunistic and focused on finding value in well-managed companies with good businesses that have been indiscriminately under-valued by the market.

Raymarine, Travelsphere, Paddy Power and The Sanctuary Spa Group are all examples of investments that have met these requirements.

Consumer Investments

Companies are performing well in a difficult environment.

	Stage	Residual cost £'000	Valuation £'000	Valuation basis	Portfolio value %
Raymarine Group Ltd	LBO	6,015	11,605	Earnings	17.2
Travelsphere Holdings Ltd	LBO	4,046	4,053	Earnings	6.0
Paddy Power plc~	Expansion	445	1,722	Mid-market price	2.5
The Sanctuary Spa Group Ltd	Expansion	342	526	Earnings	0.8
Corinthian Marketing plc	Expansion	750	386	Other	0.6
		11,598	18,292		27.1

~ Listed on the London and Dublin Stock Exchanges.

	No	£'000
Further investments	1	3,245
Partial realisations	2	706

Raymarine
Raymarine is dedicated to the design, manufacture, distribution and servicing of electronic equipment for the recreational boating market. It is the leading global supplier of instrumentation, radar and autopilots. Following a strong performance in 2001, profits fell slightly during 2002, although some of the reduction is represented by new product development spend. The company made a small prepayment of our loan stock and accrued interest at the year-end from its surplus cash.

Travelsphere
Travelsphere is one of the UK's leading escorted tour operators, providing overseas coach holidays for the 45+ age group. In a difficult year for the travel industry the company performed well and has increased profits by better management of margins and costs. The remaining tranche of our initial investment was paid during the year.

Paddy Power
Paddy Power is Ireland's largest chain of bookmakers, with a 30% market share. It conducts its business from 126 units, as well as on-course, and has successful telephone and on-line betting operations. The company is trading strongly and there was excess demand for a secondary share placing in March 2002. We chose not to sell any shares in anticipation of a continued growth in value over the next few years.

The Sanctuary Spa Group
The Sanctuary Spa Group operates a women-only day spa, 'The Sanctuary', in Covent Garden and also licenses a range of toiletries that are distributed through The Sanctuary and through Boots the Chemist. During the year the management team was strengthened and the Covent Garden operation is now trading well, having benefited from a major refurbishment. A tranche of shares was sold to management under the terms of the option agreement.

Corinthian Marketing
Our investment in Corinthian Marketing, a supplier of collectable sporting figurines, was sold after the year-end at the carrying valuation.

Healthcare

UK public expenditure on healthcare is likely to witness its greatest-ever rate of increase in the forthcoming four to five years. The Government's pledges add up to around 8% growth per annum, lifting total annual expenditure from £60 billion to £90 billion over that period.

The implications for private sector investment opportunities are positive as spending on supplies, infrastructure, medical devices and labour increases. In addition, companies that pioneer new products, such as Verigen, will benefit from the potential afforded by the NHS's increased attention to efficiency and value for money. Opportunities should also emerge within telemedicine and remote monitoring where the cost-benefit arguments are compelling.

Of course, a limiting factor to growth is the pace at which working practices in the NHS will change. Successful commercial exploitation will therefore require both a well-informed strategy and patience.

Healthcare Investments

The healthcare market yielded several good investment opportunities.

	Stage	Residual cost £'000	Valuation £'000	Valuation basis	Portfolio value %
Match Holdings Ltd	MBO	3,854	4,076	Earnings	6.0
Pharma Bio-Research BV†	MBO	3,949	4,006	Cost	5.9
Castlebeck Group Ltd	MBI	3,731	3,731	Cost	5.5
Tunstall Holdings Ltd	MBO	6,295	2,939	Written down	4.3
ClinPhone Holdings Ltd	Expansion	613	2,248	Earnings	3.3
Alizyme plc*	Expansion	2,333	1,972	Mid-market price	2.9
Verigen AG	Expansion	2,473	1,323	Written down	2.0
Profiad Ltd	Expansion	1,653	948	Written down	1.4
Newchurch Ltd	Expansion	1,927	592	Written down	0.9
Other (4)		2,653	542		0.8
		29,481	22,377		33.0

* Listed on the London Stock Exchange.
† The difference between cost and value is due to foreign exchange rate movements.

	No	£'000
New investments	2	7,680
Further investments	7	2,560
Full realisations	1	161

Match
Match is one of the UK's principal providers of comprehensive labour management, recruitment and deployment services in the healthcare sector. During the year we invested £4 million in a rights issue to fund a deferred consideration from the acquisition of Quality Locum Services, followed by an additional £2 million to acquire the former chief executive's shares. In the year to 31 December 2002, the business increased profitability by 50% following a record year in 2001.

Pharma Bio-Research
The €90 million leveraged buy-out of Pharma Bio-Research completed in December 2002. The company, which is based in The Netherlands, is a contract research organisation that manages early-phase clinical trials of new drugs on behalf of many of the world's leading blue-chip pharmaceutical and biotechnology firms. It has built an enviable reputation for managing complex trials and offering faster access to data.

Castlebeck
The £50 million leveraged buy-out of Castlebeck completed in July 2002. The company is the second-largest provider of residential healthcare to adults with learning disabilities and challenging behaviour. It operates ten independent hospitals and homes based in the north-east of England and Scotland. Demand for beds significantly outstrips supply and Castlebeck is planning to open further properties in the near future.

Tunstall
Tunstall is Europe's leading supplier of personal and home reassurance systems. Its unique emergency communication technology provides access to direct help for the elderly, disabled and vulnerable. Although profits rebounded during 2002, fuelled by an increase in sales and a record order intake, we continue to apply a reduced valuation based on the December 2001 audited accounts in accordance with our valuation policy.

ClinPhone
ClinPhone's telephone-based response system allows rapid communication of data between doctors conducting clinical trials and pharmaceutical companies. The system speeds up the collection of data, allowing pharmaceutical companies to bring drugs to market more quickly. The company continues to trade strongly. We took the opportunity to acquire shares from the founders, increasing our stake in the business to 24%.

Alizyme
Alizyme develops prescription drugs for the treatment of diseases of the gut and obesity. Progress with clinical trials continues to meet expectations. Although the company's share price suffered a significant fall in line with poor sentiment towards biotechnology stock, it saw a marked recovery towards the end of 2002.

Verigen
Verigen specialises in the fast-emerging field of tissue engineering and has developed a minimally-invasive technique for repairing cartilage in damaged joints, especially knees. Although clinical results are good, the number of operations being performed is significantly behind plan. NHS uptake is dependent on successful completion of the next clinical trial, which should also stimulate interest and awareness in Germany. We have therefore written down the valuation of this investment until revenues improve.

Profiad
Profiad offers clinical trials services to pharmaceutical companies, clinical research organisations and biotechnology companies via a network of general practitioners. The business failed to meet aggressive sales targets in the second half of the year and we have, accordingly, reduced this investment's valuation. The management team was strengthened and a cost-cutting programme implemented. £1.9 million was paid to the company during the year as part of our £6.5 million commitment.

Newchurch
Newchurch provides a range of internet-enabled services to the healthcare market, including support services and patient management programmes. Although the business has made significant progress in securing pilot sites and sales leads, conversion rates have been slower than planned. We have therefore written down this investment and supported the business with an additional £2.8 million. A further £1.8 million is committed for 2003 subject to the company reaching its milestones.

Industrials

HgCapital has a successful record of investment in the industrials sector through leveraged buy-outs of established businesses.

Our focus is on identifying situations with potential for growth in value beyond the benefits of financial gearing. In the past, we have achieved attractive returns from businesses where value was created through greater management focus and operational restructuring, as well as demand growth.

We believe that interesting investment opportunities will arise in Germany as companies come to the market as a result of economic pressures forcing the more diverse conglomerates to focus on their core business.

2002 saw completion of the first MBO in the German market.

	Stage	Residual cost £'000	Valuation £'000	Valuation basis	Portfolio value %
FTE Automotive GmbH†	MBO	6,805	6,909	Cost	10.2
Greycoat Estates Ltd	MBO	41	246	Net assets	0.4
Worldmark International Ltd	MBO	2,266	30	Written down	–
Other (4)		680	192		0.3
		9,792	7,377		10.9

† The difference between cost and value is due to foreign exchange rate movements.

	No	£'000
New investments	2	6,947
Further investments	1	31
Full realisations	1	–

FTE Automotive
The €149 million management buy-out of German automotive supplier, FTE Automotive, from US-based Dana Corporation completed in December 2002. FTE Automotive is the world market leader for clutch and brake actuation systems, supplying most of the major European and North American car manufacturers. The company has a long track record of product quality and innovation and enjoys longstanding, close relationships with its customer base.

Greycoat Estates
Our investment in Greycoat Estates has to date yielded a return of around 1.5 times invested capital as a result of the company's controlled and well-executed liquidation strategy combined with a re-gearing of its remaining property portfolio. However, the current property investment market in central London will prove a challenging environment in which to sell the remaining minor property interests.

Worldmark International
Worldmark International supplies product identification systems and components to the electronics industry. Worldmark's markets deteriorated rapidly during 2001. The company responded by switching a large proportion of manufacturing to low-cost locations in China, Mexico and Hungary and the business is now showing signs of recovery. We made a commitment to invest a further £3.0 million, the first tranche of which the company received during the year.

Technology

Technology is a large and complex area encompassing electronics, communications and information technology hardware, software and services.

HgCapital focuses on management buy-outs of mature companies across all areas of technology. We also selectively consider technology investments with high growth potential that are in early stages, focusing on specific areas such as communications software, financial services software or inter-business process enablement software. In each of these areas, software is used to help large corporations cut internal overheads and drive greater efficiencies from back-office processes.

Unrealistic valuations made it difficult to find good management buy-out opportunities in technology between 1999 and 2001. However, in 2002 the economic slow down caused these conditions to reverse, with parent companies increasingly inclined to dispose of non-core technology businesses. Whilst this did not result in significant management buy-out investment activity during 2002, we believe it bodes well for our investment potential in 2003 and 2004.

Technology Investments

Turmoil within the industry affected valuations.

	Stage	Residual cost £'000	Valuation £'000	Valuation basis	Portfolio value %
Acuid Ltd†	Expansion	2,832	2,574	Cost	3.8
Orbiscom Ltd	Expansion	2,791	1,441	Written down	2.1
Comnitel Technologies	Expansion	2,405	1,438	Written down	2.1
Trados, Inc	Expansion	2,492	982	Written down	1.5
Axiom Holdings Ltd	Expansion	1,647	909	Written down	1.3
Burns e-Commerce Solutions	MBI	2,211	797	Written down	1.2
Bottomline Technologies, Inc**	MBO	952	789	Mid-market price	1.2
Other (2)		1,114	157		0.2
		16,444	9,087		13.4

** Traded on NASDAQ.
† The difference between cost and value is due to foreign exchange rate movements.

	No	£'000
Further investments	4	3,334
Full realisations	1	–

2002 was a difficult year for the technology industry as a whole, reflected in the performance of companies within the portfolio. Most software suppliers suffered as customers applied strict financial criteria to capital expenditure commitments. Sales were lower than anticipated on longer lead times and management teams adopted a policy of retrenchment. Accordingly, we have written down the valuations of the majority of the technology investments.

Acuid
Acuid develops intellectual property for high-speed data communication between micro-chips that is considerably faster than current, equivalent technology. Reaction to Acuid's low-cost product has been extremely positive. We invested a further $4 million and have committed to invest an additional $4 million in February 2003.

Orbiscom
Orbiscom supplies secure-on-line payment card technology to large financial institutions, which provides its customers with a continuous and immediate communication channel and protects cardholders against fraud.

Comnitel Technologies
Comnitel provides operating support system software that enables mobile telecommunications operators to improve the services delivered by their networks. We participated in a further €10 million funding round, investing an additional €5.2 million.

Trados
Trados is the global market leader in software for the translations industry. Some 17% of the world's translators rely on its technology, which improves the quality and consistency of their work.

Axiom
Axiom is a leading innovator in the telecommunications software market, enabling communications operators to automate the entire complex process required to deliver a new service, such as cable television. We participated in a further £2 million financing round, investing £0.8 million.

Burns e-Commerce Solutions
Burns e-Commerce Solutions' simple and affordable on-line invoicing and payment processing products deliver efficiencies and cost-savings by streamlining transactions. The company received further funding during the year, amounting to £4.6 million.

Bottomline Technologies
The holding in Bottomline Technologies was acquired through the sale of Checkpoint, which develops electronic bill presentment and payment software. Bottomline's share price has suffered from the volatility of NASDAQ. However, the company made a small profit compared with a significant loss in the previous year.

Media

Media is the most cyclical of the industries in which we invest but it is one that offers attractive returns to those willing to take a long-term view. International consolidation, deregulation and new technology are all driving profound change.

The media industry has been adversely affected by the economic slowdown, the advertising recession and by the bursting of the technology, media and telecommunications bubble. We believe that these forces will influence media groups to sell secondary businesses, producing good investment opportunities over the next few years.

Our focus is on specialist publishing: the creation or exploitation and distribution of high-value content or intellectual property rights for an established customer base. When the economy reaches its low point we will start considering advertising-based businesses.

Media Investments

	Stage	Residual cost £'000	Valuation £'000	Valuation basis	Portfolio value %
Eagle Rock Entertainment Ltd	MBO	3,668	3,668	Cost	5.4

Eagle Rock Entertainment
Eagle Rock Entertainment creates and acquires audio and visual programming entertainment rights with a focus on music-related content by established artists such as James Brown, Simple Minds, Tina Turner and Janet Jackson.

The end products are principally CDs and DVDs, typically sold to the consumer by specialist or secondary retailers. The company also licenses its rights to third parties, mainly TV networks.

Fund Investments

Overseas funds are mostly in their realisation phases.

	Residual cost £'000	Valuation £'000	Valuation basis	Portfolio value %
Weston Presidio Capital LP (I, II and III)	3,027	3,569	Net assets	5.3
Euroknights III, LP	1,469	509	Net assets	0.8
Wand Equity Portfolio II, LP	643	439	Net assets	0.7
Other (3)	121	172		0.2
	5,260	4,689		7.0

	No	£'000
Further investment	1	29
Partial realisations	4	747

Weston Presidio Capital
Weston Presidio Capital invests equity capital into later-stage, privately-held emerging-growth companies in the United States. It has raised three funds in which HgCapital has invested. The first fund is fully invested and has five remaining investments. Its performance has been good with a net IRR to limited partners to date of 21%. The second fund comprises seven investments, is 85% drawn and has produced a net IRR to date of 28%. The third fund comprises 26 investments and is 78% drawn. Proceeds arose from a sale of shares following the successful IPO of JetBlue Airways, a start-up airline company in which the second and third funds are invested.

Euroknights III
Euroknights III invests in medium-sized companies in continental Europe and is fully invested. Its remaining seven investments are under-performing. It made a cash distribution during the year.

Wand Equity Portfolio II
Wand Equity Portfolio II invests in mid-size LBOs and development capital opportunities in the USA. It has a portfolio of 18 investments and is 89% drawn. It made two calls of capital during the year.

Review of Principal Investments

Company	Accounting date	Currency	Turnover	PBIT/(LBIT)	PBT/(LBT)	Net assets/ (liabilities)	MGT income accrued 2002 £'000	% ordinary share capital (a)
Acuid Ltd	Dec 2001	$'m	0.7	(3.5)	(3.5)	4.2	–	7.5
Alizyme plc*	Dec 2001	£'m	–	(8.8)	(6.6)	14.0	–	7.3
Castlebeck Group Ltd			***	***	***	***	171	15.3
ClinPhone Holdings Ltd	Feb 2002	£'m	15.2	2.7	2.0	(0.1)	–	12.7
Comnitel Technologies	Dec 2001	€'m	–	(7.4)	(7.3)	6.2	–	11.9
Eagle Rock Entertainment Ltd			***	***	***	***	289	14.6
FTE Automotive GmbH			***	***	***	***	39	17.1
Match Holdings Ltd	Dec 2001	£'m	182.0	10.8	(1.4)	(12.7)	662	6.3
Orbiscom Ltd	Dec 2001	$'m	7.7	(12.0)	(11.8)	10.3	–	2.8
Paddy Power plc~	Dec 2001	€'m	461.0	8.5	9.1	30.7	–	1.1
Patientline plc#	Mar 2002	£'m	13.3	(3.0)	(3.5)	25.3	–	3.9
Pharma Bio-Research BV		€'m	***	***	***	***	13	13.0
Profiad Ltd	Dec 2001	£'m	3.4	(2.1)	(2.1)	2.3	–	13.8
Raymarine Group Ltd	Dec 2001	$'m	138.6	18.2	3.7	6.0	1,288	14.1
Trados, Inc	Dec 2001	$'m	15.7	1.2	(9.2)	5.4	–	5.4
Travelsphere Holdings Ltd	Nov 2001	£'m	106.5	9.0	(2.8)	(2.2)	798	8.0
Tunstall Holdings Ltd	Sep 2001	£'m	55.5	7.7	(7.5)	(9.8)	–	9.2
Verigen AG	Dec 2001	€'m	1.5	(7.3)	(6.8)	16.7	–	0.3
Weston Presidio Capital II, LP	Dec 2001	$'m	n/a	n/a	n/a	60.2	–	2.2
Weston Presidio Capital III, LP	Dec 2001	$'m	n/a	n/a	n/a	271.4	–	1.2

(a) Percentage of the total issued ordinary share capital held by the Company as at 31 December 2002.

* Listed on the London Stock Exchange.
~ Listed on the London and Dublin Stock Exchanges.
\# Traded on the Alternative Investment Market.
*** No audited accounts have been produced since investment.

Paddy Power plc paid total dividends of €0.068 per share in 2002. None of the other companies listed above paid any dividends in 2002.

Investment Listing

Company	Activity	Residual cost £'000	Valuation £'000	Year of investment	Value %
ACT Venture Capital Ltd	Irish venture fund	–	156	1994	0.2
Acuid Ltd	High-speed communication technology	2,832	2,574	2001	3.8
Alizyme plc*	Biotechnology for gut disease and obesity	2,333	1,972	1998	2.9
Ardagh plc~	Glass manufacturer	142	180	2002	0.3
Axiom Holdings Ltd	Communications software	1,647	909	2001	1.3
Azinger Ltd (in liquidation)	Grocery importer and distributor	267	56	1993	0.1
Bertram Group Holdings Ltd+	Wholesale supplier of books	3,309	133	1999	0.2
Biocode Inc	Molecular markers	531	127	1997	0.2
Biovector Therapeutics SA	Biopharmaceuticals	998	–	1997	–
Bottomline Technologies, Inc**	B2B electronic banking software	952	789	1999	1.2
Burns e-Commerce Solutions+	B2B electronic payments software	2,211	797	2001	1.2
Castlebeck Group Ltd+	Care homes	3,731	3,731	2002	5.5
ClinPhone Holdings Ltd	Pharmaceutical and clinical research services	613	2,248	1996	3.3
Comnitel Technologies	Network management software	2,405	1,438	2001	2.1
Corinthian Marketing plc	Plastic collectable figurines	750	386	1995	0.6
Creos International plc* (in liquidation)	Power supplies for x-ray machines	594	–	1994	–
Eagle Rock Entertainment Ltd+	Entertainment intellectual property rights	3,668	3,668	2001	5.4
Euroknights III LP	European venture fund	1,469	509	1996	0.8
Euroknights International Ltd	European venture fund	83	–	1990	–
FTE Automotive GmbH+	Clutch and brake components	6,805	6,909	2002	10.2
Global People Network Ltd	On-line staffing software	520	157	1999	0.2
Greycoat Estates Ltd	Property development	41	246	1999	0.4
JBS Industries Ltd	Building products	12	12	1994	–
Luxfer Holdings plc	Aluminium products	46	–	1996	–
Match Holdings Ltd	Staffing services to NHS trust hospitals	3,854	4,076	1999	6.0
MedNova Ltd	Medical devices	120	415	1998	0.6
Newchurch Ltd	IT services for the healthcare industry	1,927	592	2000	0.9
Nigra plc (in liquidation)	Central nervous system drugs	1,004	–	1996	–
Nova Homes Ltd (in liquidation)	Housebuilder	480	–	1993	–
Orbis plc*	Void property management	3,378	65	1997	0.1
Orbiscom Ltd	Secure card-based payments technology	2,791	1,441	2001	2.1
Paddy Power plc~	Bookmaker	445	1,722	2000	2.5
PARC Group Ltd	Manpower leasing	51	–	1995	–
Patientline plc#	Hospital services	413	1,720	1996	2.5
Pharma Bio-Research BV+	Clinical trials	3,949	4,006	2002	5.9
Profiad Ltd+	Patient recruitment for clinical trials	1,653	948	1999	1.4
Raymarine Group Ltd+	Recreational marine electronics	6,015	11,605	2001	17.2
SGI (Holdings) Ltd+	Outsourced services for the property sector	2,966	207	1999	0.3
The Sanctuary Spa Group Ltd+	Day spa	336	526	1995	0.8
Trados, Inc	Software for the translation industry	2,492	982	2000	1.5
Travelsphere Holdings Ltd	Overseas coach tour holidays	4,046	4,053	2000	6.0
Tunstall Holdings Ltd+	Security alarms for the elderly and infirm	6,295	2,939	1999	4.3
UPM Holdings BV	European venture fund	39	17	1991	–
Verigen AG	Tissue repair technology	2,473	1,323	2000	2.0
Wand Equity Portfolio II, LP	US LBO fund	643	439	1998	0.7
Weston Presidio Capital I, LP	US venture fund	–	21	1991	–
Weston Presidio Capital II, LP	US venture fund	–	931	1995	1.4
Weston Presidio Capital III, LP	US venture fund	3,027	2,616	1998	3.9
Worldmark International Ltd	Product identification systems	2,266	30	2000	–
Total		**86,622**	**67,671**		**100.0**

* Listed on the London Stock Exchange.
~ Listed on the London and Dublin Stock Exchanges.
\# Traded on the Alternative Investment Market.
** Traded on NASDAQ.
\+ HgCapital, through its management of the Company and other funds, controls more than 50% of the voting equity shares.

Board of Directors

David Bucks* (chairman)
Aged 68, was appointed as a director and became chairman of the Company in 1992. He is a chartered accountant with over 30 years' experience of working in the City.

Timothy John Amies*
Aged 64, was appointed to the Board in 1991. He is a chartered accountant with over 30 years' experience of working in the City. He was a partner of Laurie Milbank & Co, stockbrokers, for 16 years prior to its acquisition by Chase Manhattan Bank, where he was a director of Chase Investment Bank involved in mergers and acquisitions. He is chairman of the Audit and Valuation Committee of the Company.

Piers Leighton Brooke†
Aged 62, was appointed to the Board in 2001. He worked for 38 years in both commercial and merchant banking, holding a variety of general management positions in the UK, continental Europe, the Far East and North America; most recently he was the Director of Financial Strategy at National Westminster Bank. He is a non-executive director of Focus Solutions Group plc and other companies.

Anthony Dudley Vincent Crook*
Aged 66, became a director in 1989. He entered the venture capital industry in 1973 and was a founder of Grosvenor Venture Managers. His earlier career was in marketing in the computer, packaging and automotive industries.

Peter Gale*†
Aged 47, was appointed to the Board in 1991 and is deputy chairman of the Company. He has worked in many of the divisions of National Westminster Bank, specialising in investment management. In 1990 he became responsible for the investment management of National Westminster Bank Group Pension Funds, which has subsequently become RBS Pension Trustee Ltd.

Michael John Glover†
Aged 64, was appointed to the Board in 1991. Prior to becoming involved in private equity fund management in 1984, he was an executive with electronics companies operating in the UK, Far East and North America. His experience encompasses more than 15 years at chief executive and board level. He is a non-executive director of Biocode Inc, nominated by HgCapital.

* Member of the Audit and Valuation Committee.
† Member of the Management Engagement Committee.
All directors are members of the Nomination Committee.
All the directors are non-executive and independent.

Directors' Report

The directors present the annual report and financial statements of the Company for the year ended 31 December 2002.

Principal activity and business review
The principal activity of the Company is to operate as an investment trust providing development capital for unquoted companies.

A review of the business for the year is given in the Chairman's Statement on page 2 and in the Investment Manager's Review, which begins on page 3.

Status of the Company
The Inland Revenue has accepted the Company as an investment trust for the purposes of section 842 of the Income and Corporation Taxes Act 1988 ("ICTA") for the year ended 31 December 2001. In the opinion of the directors, the Company has conducted its affairs so as to enable it to continue to maintain acceptance as an investment trust since that date. It is the Company's intention to continue to seek authorisation under section 842 of ICTA.

The Company is not a close company within the meaning of the provisions of ICTA.

The Company is an investment company within the meaning of section 266 of the Companies Act 1985.

The Company's shares are eligible investments within the stocks and shares component of an Individual Savings Account.

Results and dividend
The revenue for the Company is set out in the Statement of Total Return on page 28. Revenue for the year, after taxation, was £2,148,000 (2001: £2,420,000).

The directors recommend the payment of a final dividend of 8.00p per ordinary share for the year ended 31 December 2002. Subject to the approval of this dividend at the forthcoming Annual General Meeting ("AGM"), it will be paid on 1 May 2003 to shareholders on the register of members at the close of business on 28 March 2003.

Derivative transactions
The Company has not entered into any derivative transactions during the year.

Directors
The directors of the Company are listed on page 20. In accordance with the Articles of Association, Mr T J Amies will retire by rotation at the Company's AGM and, being eligible, offers himself for re-election. None of the directors has a service contract with the Company.

The interests of those persons who were directors at the end of the year in the ordinary shares of the Company were as follows (all holdings are beneficial unless stated otherwise):

	31 December 2002	1 January 2002
T J Amies	**30,000**	30,000
P L Brooke	**–**	–
D Bucks	**6,400**	6,400
A D V Crook		
– beneficial	**14,835**	14,835
– non-beneficial	**200,000**	200,000
P Gale	**4,000**	4,000
M J Glover		
– beneficial	**2,121**	2,121
– non-beneficial	**52,001**	52,001

No notification of any change in the above interests has been received from 31 December 2002 to the date of this report.

Substantial interests
The Company is aware that the following shareholders had an interest in 3% or more of the issued share capital of the Company on 14 March 2003:

	Ordinary shares	% of issued share capital
Merrill Lynch Investment Managers Limited*	5,471,845	21.7
RBS Pension Trustee Ltd	3,030,659	12.0
HBOS plc	2,991,815	11.8
Wolverhampton Borough Council Superannuation Fund	2,481,788	9.8
Clients of Exeter Asset Management Limited	2,075,000	8.2
The Scottish Investment Trust PLC	1,600,000	6.3
The Co-operative Insurance Society Limited	1,350,000	5.3

*On behalf of discretionary and non-discretionary clients and staff, including 1,019,619 ordinary shares (4.0%) beneficially owned by BBC Pension Trust Limited Fund RW.

We are not aware that any other shareholder had an interest of 3% or more in the Company's ordinary share capital as at 14 March 2003.

Investment management and administration
The Company has an investment management agreement dated 30 March 1995 with Merrill Lynch Investment Managers Limited ("MLIM"), which sets out the terms under which MLIM is appointed as investment manager to the Company.

Under the terms of a delegation agreement between MLIM and Hg Investment Managers Limited ("HgCapital"), MLIM's duties as investment manager have been delegated to HgCapital.

The Company will be putting a resolution to shareholders to agree new management arrangements in order to put in place a direct contractual relationship with HgCapital. Details of the proposed new arrangements and Notice of an Extraordinary General Meeting will be sent to shareholders shortly. The details below relate to the current investment management agreement.

The agreement may be terminated without penalty on two years' notice by either party. The management fee is based on the value of the Company as at the end of each quarter and is set at 2.25% per annum on the value of unquoted investments and 0.75% per annum on the value of the Company's gross assets after deducting the value of unquoted investments, short-term liabilities and third party funds.

Merrill Lynch Investment Managers Group Services Limited ("MLIMGS") acts as the secretary and administrator of the Company and The Bank of New York Europe Limited ("BNYE") is the custodian of the Company's assets. The annual administration and custodian fee is 0.1% of the Company's gross assets. In addition, MLIM is reimbursed certain expenses incurred in the performance of its duties.

At 31 December 2002, MLIM and its subsidiaries beneficially held 581,306 ordinary shares or 2.3% of the issued share capital of the Company (2001: 600,806 or 2.3%).

Both MLIM and MLIMGS are subsidiaries of Merrill Lynch & Co., Inc.

Directors' remuneration report
The directors' remuneration report is set out on page 24. An ordinary resolution to note this report will be put to members at the forthcoming AGM. No person's entitlement to remuneration is conditional upon the resolution being passed.

Voting policy
The exercise of voting rights attached to the Company's portfolio has been delegated to MLIM.

MLIM's voting policy, by which HgCapital is bound, is:

- to vote at all general meetings of UK companies in which its clients are invested;
- to vote in favour of proposals which it expects to enhance shareholder value;
- to vote against proposals which it believes may damage shareholders' rights or economic interests; in these situations it would normally have raised its concerns with management in advance;
- to abstain on proposals which it feels unable to support but believes would be against its clients' interests to oppose publicly; and
- in all situations the economic interests of its clients will be paramount.

Donations
The Company made no political or charitable donations during the period.

Payment of suppliers
It is the general policy of the Company to pay for the supply of goods and services within 30 days of the date of any invoice. The Company has no trade creditors.

Annual General Meeting
The AGM of the Company will be held at the offices of CMS Cameron McKenna, Mitre House, 160 Aldersgate Street, London EC1A 4DD on Tuesday 29 April 2003 at 11.30 a.m. Notice of the AGM is given on page 43 of this report.

Authority to buy back shares
The directors' authority to buy back shares for cancellation was renewed at last year's AGM, and will expire on 10 October 2003.

Although no shares were bought back during the year, the directors are proposing to renew the authority at the forthcoming AGM, and are seeking authority to purchase up to 3,775,000 ordinary shares (being 14.99% of the issued share capital). This authority, unless renewed, will expire on 28 October 2004.

Purchases of ordinary shares will only be made through the market for cash at prices below the prevailing net asset value ("NAV") per ordinary share. Under the Listing Rules of the Financial Services Authority, the maximum price that can be paid is 5% above the average of the market values of the ordinary shares for the five business days before the purchase is made. The minimum price that may be paid will be 25p per share (being the nominal value of a share). Ordinary shares that are purchased will be cancelled. In making purchases, the Company will deal only with member firms of the London Stock Exchange.

Authority of directors to allot shares
Resolutions 8 and 9 to be proposed at the AGM are similar to the authorities given to the directors at last year's AGM. By law, directors are not permitted to allot new shares (or to grant rights over shares) unless authorised to do so by shareholders. Resolution 8 gives the directors, for the period until the conclusion of the AGM in 2004, the necessary authority to allot securities up to an aggregate nominal amount of £314,800, which is equivalent to 1,259,200 ordinary shares of 25p each and approximately 5% of the issued ordinary share capital.

Resolution 9 empowers the directors until the conclusion of the AGM in 2004, or if earlier, the expiry of 15 months from the date on which the resolution is passed, to allot securities for cash, otherwise than to existing shareholders on a pro rata basis, up to an aggregate nominal amount of £314,800, which is equivalent to 1,259,200 ordinary shares and approximately 5% of the issued share capital. In no circumstances would the directors use this authority to dilute the interests of existing shareholders by issuing shares at a price which is less than the NAV attributable to the shares at the time of issue.

Auditor
Ernst & Young LLP has indicated its willingness to continue in office as independent auditor and resolutions proposing its re-appointment and authorising the directors to determine its remuneration will be submitted at the AGM.

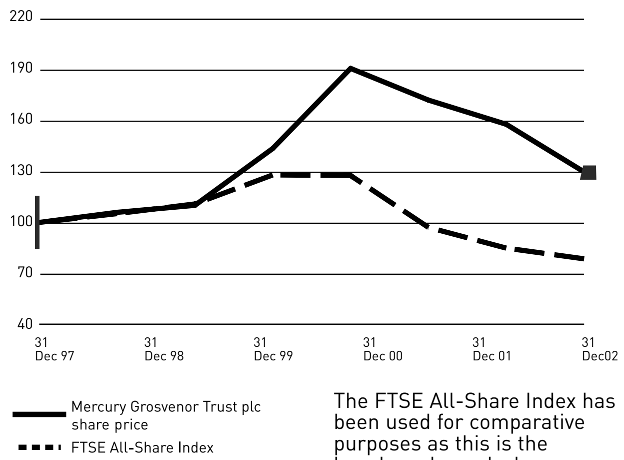
By order of the Board
Merrill Lynch Investment Managers Group Services Limited
Secretary
18 March 2003

Directors' Remuneration Report

The Company presents the directors' remuneration report for the year ended 31 December 2002.

Directors' Remuneration Committee
The Directors' Remuneration Committee consists of David Bucks (chairman), Timothy Amies, Piers Brooke and Peter Gale and meets when necessary to consider any change in the Company's directors' remuneration policy. The Company has no employees other than its directors, who are all non-executive. The secretary (whose duties are set out elsewhere in this report, and who is not appointed by the Directors' Remuneration Committee) provides a comparison of the directors' remuneration with other investment trusts of similar size and/or mandate. This comparison, together with consideration of any alteration in non-executive directors' responsibilities, is used to review whether any change in remuneration is necessary.

Share price performance from 31 December 1997 to 31 December 2002



Performance record rebased to 100 at 31 December 1997.

The FTSE All-Share Index has been used for comparative purposes as this is the benchmark used when reporting to shareholders. All figures are capital only.

No element of the directors' remuneration is performance related. The Company has not awarded any share options or long-term performance incentives to any of the directors.

Directors' remuneration

Director	Remuneration 2002 £	2001 £
Timothy Amies	**13,000**	13,000
Piers Brooke (appointed 1.5.01)	**13,000**	6,667
David Bucks (chairman)	**20,000**	20,000
Anthony Crook	**13,000**	13,000
Peter Gale*	**13,000**	13,000
Michael Glover	**13,000**	10,000

* Paid through a third party.
The information in this table and in the paragraphs below has been audited.

The remuneration of Mr Brooke and Mr Glover was increased from £10,000 to £13,000 per annum with effect from 1 January 2002. There have been no other changes to the remuneration levels in the period under review.

None of the directors receive any non-cash benefits or pension entitlements.

Compensation for loss of office
No past director has been compensated for loss of office.

Retirement of directors
All of the Company's directors are subject to retirement by rotation as per the Company's Articles of Association. No service contracts exist.

By order of the Board
Merrill Lynch Investment Managers Group Services Limited
Secretary
18 March 2003

Corporate Governance and Directors' Responsibilities

The Company is committed to high standards of corporate governance. The Board has put in place a framework for corporate governance which it believes is suitable for an investment trust and which enables the Company to comply with the Principles of Good Governance and Code of Best Practice ("the Combined Code") prepared by the Committee on Corporate Governance, published in June 1998.

The Board considers that the Company has complied with the provisions contained within Section 1 of the Combined Code throughout this accounting period, and this statement describes how the relevant principles of governance are applied to the Company.

The Board
The Board consists of six non-executive directors, all of whom the Company deem to be independent of the Investment Manager, even though five of them have served as directors for over ten years. Their biographies, on page 20, highlight their wide range of business experience. The structure of the Board is such that it is considered unnecessary to identify a senior non-executive director other than the chairman.

The Board is supplied in a timely manner with information in a form and of a quality appropriate to enable it to discharge its duties. Strategic issues and all operational matters of a material nature are determined by the Board.

The directors retire by rotation at every third Annual General Meeting ("AGM") and any directors appointed to the Board since the previous AGM also retire and stand for election. Directors who reach the age of 70 will retire at the next AGM of the Company and at each following AGM, but will be eligible for reappointment.

The Board meets at least five times a year and, between these meetings, there is regular contact with HgCapital. The directors also have access to the advice and services of the secretary, who is responsible to the Board for ensuring that Board procedures are followed and that applicable rules and regulations are complied with. Where necessary, in the furtherance of their duties, the directors may seek independent professional advice at the expense of the Company.

The Board has responsibility for ensuring that the Company keeps proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and enable it to ensure that the financial statements comply with the Companies Act 1985. The Board is also responsible for safeguarding the assets of the Company and for taking reasonable steps for the prevention and detection of fraud and other irregularities. Finally, it is the Board's responsibility to present a balanced and understandable assessment which extends to the interim and other price-sensitive public reports. The Board has delegated the following areas of responsibility:

Management and administration
The management of the investment portfolio has been delegated to MLIM and sub-delegated by MLIM to Hg Investment Managers Limited ("HgCapital"). Certain other functions have been delegated by the Board to MLIM and its subsidiary companies. Company secretarial functions are carried out by Merrill Lynch Investment Managers Group Services Limited. Custody and settlement services are undertaken by The Bank of New York Europe Limited ("BNYE"), a subsidiary of The Bank of New York.

The Board has delegated the exercise of voting rights attaching to the securities held in the portfolio to MLIM. Details of MLIM's voting policy, by which HgCapital is bound, are set out on page 22.

All other matters are reserved for the approval of the Board.

Board committees
As all the directors of the Company are non-executive, the Board as a whole fulfils the function of the Nomination Committee, which meets when necessary to select and propose suitable candidates for appointment.

The Directors' Remuneration Committee, which is made up of four directors, who are not employed by or are not former employees of MLIM, HgCapital or any of their associates or subsidiaries, meets when necessary to consider any change in directors' remuneration policy.

Separate Audit and Valuation and Management Engagement Committees have been established. These committees consist of at least three directors, the majority of whom are not employed by and are not former employees of MLIM, HgCapital or any of their associates or subsidiaries.

The Audit and Valuation Committee, which has written terms of reference detailing its scope and duties and which meets at least twice a year, examines the effectiveness of the control systems. The Committee reviews the interim and annual reports and also receives information from the corporate audit and compliance departments of MLIM and HgCapital. The Committee reviews the scope, results, cost effectiveness, independence and objectivity of the external auditor. Semi-annually, at each balance sheet date, the Committee reviews in detail the valuation of the unquoted investments within the portfolio.

The Management Engagement Committee, which also has written terms of reference detailing its scope and duties, regularly reviews the terms of the investment management and administration contracts.

Internal controls
The Board is responsible for the internal controls of the Company and for reviewing their effectiveness, for ensuring that financial information published or used within the business is reliable, and for regularly monitoring compliance with regulations governing the operation of investment trusts. The Board continually reviews the effectiveness of the internal control system, which has been

Corporate Governance and Directors' Responsibilities

continued

in place throughout the year under review. The processes indicated below have been put in place to ensure that the Company fully complied with the Combined Code for the year ended 31 December 2002 and will continue to do so for the year ending 31 December 2003.

As part of the Board's responsibility for the internal control system, an ongoing process has been established in conjunction with MLIM and HgCapital, for identifying, evaluating and managing the Company's significant risks. Controls of the risks identified, covering financial, operational, compliance and risk management, are embedded in the operations of MLIM, HgCapital and BNYE. There is a monitoring and reporting process to review controls put in place to track risks identified, carried out by MLIM's corporate audit department. MLIM reports to the Company its review of internal controls, which include checks on the custodian, formally on a semi-annual basis and verbally at each Board and Audit and Valuation Committee meeting.

MLIM, in conjunction with HgCapital, prepares revenue forecasts and management accounts, which allow the Board to assess the Company's activities and to review its performance.

The Board and HgCapital have agreed clearly defined investment criteria, specified levels of authority and exposure limits. Reports on these issues, including performance statistics and investment valuations, are submitted to the Board at each meeting. HgCapital's evaluation procedure and financial analysis of the companies within the portfolio includes detailed research and appraisal, and also takes into account environmental policies and other business issues.

The controls and procedures of MLIM and HgCapital are monitored by their respective corporate audit and compliance departments, who report to the Audit Committee. The Audit Committee also receives a report from BNYE on the internal controls of its custodial operations.

The Board recognises that these control systems can only be designed to manage rather than eliminate the risk of failure to achieve business objectives and to provide reasonable, but not absolute, assurance against material misstatement or loss. They rely on the operating controls established by MLIM, HgCapital and BNYE.

Financial statements
The Board is required to ensure that the financial statements give a true and fair view of the affairs of the Company as at the end of each financial year and of the profit of the Company for that period.

The Board considers that in preparing the financial statements on pages 28 to 38, the Company has used appropriate accounting policies, consistently applied (except where disclosed) and supported by reasonable and prudent judgements and estimates and that all accounting standards that it considers to be applicable have been followed.

The Board believes it is appropriate to adopt the going concern basis in preparing the financial statements.

Relations with shareholders
All shareholders have the opportunity to attend and vote at the AGM. The notice of the AGM sets out the business of the Meeting and any item not of an entirely routine nature is explained in the Directors' Report on pages 21 to 23. Separate resolutions are proposed for substantive issues.

In addition, both the Board and representatives of HgCapital are available to answer shareholders' questions at the AGM. Proxy voting figures are announced to shareholders at the AGM.

HgCapital holds regular discussions with major shareholders, the feedback from which is greatly valued by the Board. In addition, the chairman and directors are available to enter into dialogue and correspondence with shareholders regarding the progress and performance of the Company. The section of this report entitled "Shareholder Information", on pages 40 and 41, provides an overview of useful information available to shareholders.

Membership of the Board Committees

Audit and Valuation Committee
Timothy Amies (chairman)
David Bucks
Anthony Crook
Peter Gale

Directors' Remuneration Committee
David Bucks (chairman)
Timothy Amies
Piers Brooke
Peter Gale

Management Engagement Committee
David Bucks (chairman)
Piers Brooke
Peter Gale
Michael Glover

Nomination Committee
David Bucks (chairman)
Timothy Amies
Piers Brooke
Anthony Crook
Peter Gale
Michael Glover

Report of the Independent Auditor to the Members of Mercury Grosvenor Trust plc

We have audited the Company's financial statements for the year ended 31 December 2002, which comprise the Statement of Total Return (incorporating the Revenue Account), Balance Sheet, Cash Flow Statement and the related notes 1 to 20. These financial statements have been prepared on the basis of the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an independent 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 the independent auditor
The directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the statement on Corporate Governance and Directors' Responsibilities.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements, United Kingdom Auditing Standards and the Listing Rules of the Financial Services Authority.

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

We review whether the statement on Corporate Governance and Directors' Responsibilities reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the Board's statement on internal controls covers all risks and controls, or form an opinion on the effectiveness of either the Company's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. This other information comprises the Financial Highlights, Performance Record, Chairman's Statement, Investment Manager's Review, Analysis of Shareholders, Shareholder Information, Glossary, Notice of Annual General Meeting and Management and Administration. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

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

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

Opinion
In our opinion:

i) the financial statements give a true and fair view of the state of affairs of the Company as at 31 December 2002 and of the return of the Company for the year then ended; and

ii) the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985.

Ernst & Young LLP
Registered Auditor
London
18 March 2003

Statement of Total Return (incorporating the revenue account)
for the year ended 31 December 2002

		Revenue		Capital		Total	
	Note	**2002 £'000**	2001 £'000	**2002 £'000**	2001 £'000	**2002 £'000**	2001 £'000
Losses on investments	11	**–**	–	**(11,214)**	(7,142)	**(11,214)**	(7,142)
Income	2	**3,528**	3,893	**–**	–	**3,528**	3,893
Investment management fee	3	**(396)**	(449)	**(1,187)**	(1,346)	**(1,583)**	(1,795)
Other expenses	4	**(322)**	(329)	**–**	–	**(322)**	(329)
Net return before finance costs and taxation		**2,810**	3,115	**(12,401)**	(8,488)	**(9,591)**	(5,373)
Interest payable and similar charges	6	**(22)**	(22)	**(66)**	(66)	**(88)**	(88)
Return on ordinary activities before taxation		**2,788**	3,093	**(12,467)**	(8,554)	**(9,679)**	(5,461)
Taxation on ordinary activities	7	**(640)**	(673)	**376**	423	**(264)**	(250)
Return on ordinary activities after taxation		**2,148**	2,420	**(12,091)**	(8,131)	**(9,943)**	(5,711)
Dividend in respect of equity shares	8	**(2,015)**	(2,015)	**–**	–	**(2,015)**	(2,015)
Transfer to/(from) reserves		**133**	405	**(12,091)**	(8,131)	**(11,958)**	(7,726)
Return per ordinary share	9	**8.53p**	9.61p	**(48.01p)**	(32.28p)	**(39.48p)**	(22.67p)
Dividend per ordinary share	8	**8.00p**	8.00p	**–**	–	**8.00p**	8.00p

The revenue column of this statement is the profit and loss account of the Company.
The movements in reserves are set out in note 18 to the financial statements.
All revenue and capital items in the above statement derive from continuing operations.
No operations were acquired or discontinued during the year.

The notes on pages 31 to 38 form part of these financial statements.

Balance Sheet
as at 31 December 2002

	Note	2002 £'000	2001 £'000
Fixed assets			
Investments	10		
– Listed at mid-market valuation		**5,112**	14,238
– Unquoted at directors' valuation		**62,559**	60,970
		67,671	75,208
Current assets			
Debtors	12	**3,881**	4,371
Government securities	13	**13,843**	18,548
Cash	14	**1,031**	313
		18,755	23,232
Creditors - amounts falling due within one year	15	**(2,589)**	(2,645)
Net current assets		**16,166**	20,587
Net assets		**83,837**	95,795
Capital and reserves			
Called up share capital	17	**6,296**	6,296
Share premium account	18	**14,123**	14,123
Capital redemption reserve	18	**1,248**	1,248
Capital reserve - realised	18	**78,079**	68,723
Capital reserve - unrealised	18	**(19,059)**	2,388
Revenue reserve	18	**3,150**	3,017
Total equity shareholders' funds	19	**83,837**	95,795
Net asset value per ordinary share	9	**332.9p**	380.3p

The financial statements on pages 28 to 38 were approved by the Board of Directors on 18 March 2003 and were signed on its behalf by:

David Bucks, Chairman
Timothy Amies, Director

The notes on pages 31 to 38 form part of these financial statements.

Cash Flow Statement

for the year ended 31 December 2002

	Note	2002 £'000	2001 £'000
Net cash flow from operating activities	4(b)	**2,161**	2,043
Returns on investments and servicing of finance		**(7)**	104
Taxation received/(paid)		**383**	(493)
Capital expenditure and financial investment			
Purchase of fixed asset investments		**(24,033)**	(22,696)
Proceeds from the sale of fixed asset investments		**20,246**	19,470
Net cash outflow for capital expenditure and financial investment		**(3,787)**	(3,226)
Equity dividends paid		**(2,015)**	(3,652)
Net cash outflow before management of liquid resources		**(3,265)**	(5,224)
Management of liquid resources			
Purchase of Government securities		**(53,996)**	(50,687)
Sale/redemption of Government securities		**57,979**	47,185
Net cash inflow/(outflow) from management of liquid resources		**3,983**	(3,502)
Increase/(decrease) in cash in the period	14	**718**	(8,726)

The notes on pages 31 to 38 form part of these financial statements.

Notes to the Financial Statements

1. Accounting policies

Basis of preparation
The accounts have been prepared under the historical cost convention, modified to include the revaluation of investments, and are in accordance with section 230 of, and schedule 4 to, the Companies Act 1985, and with applicable accounting standards and the Statement of Recommended Practice "Financial Statements of Investment Trust Companies".

Associated undertakings
Certain venture capital investments deemed to be associated undertakings are carried at cost or valuation in accordance with the Company's normal accounting policy and Financial Reporting Standard ("FRS") 9.

Investment income and interest receivable
Income from equity investments, including taxes deducted at source, is included in revenue by reference to the date on which the investment is quoted ex-dividend. Where the Company elects to receive dividends in the form of additional shares rather than cash, the equivalent of the cash dividend is recognised as income in the revenue account and any excess in value of the shares received over the amount of the cash dividend is recognised in capital reserve - realised. Interest income is accounted for on an accruals basis. Dividends receivable on equity shares where there is no ex-dividend date and on non-equity shares are brought into account when the Company's right to receive payment is established.

The return on deep discounted loan stock and Government securities is recognised by allocating the net receipts that the holder is entitled to receive over the term of the debt security at a constant rate on the market value.

Management fee and finance costs
The annual investment management fee and finance costs are charged 75% to capital reserve - realised and 25% to the revenue account. This is in line with the Board's expected split of long-term returns, in the form of capital gains and income respectively, from the investment portfolio of the Company.

Expenses
All expenses are accounted for on an accruals basis. All administrative expenses, excluding the management fee, are charged wholly to the revenue account.

Expenses which are incidental to the purchase or sale of an investment are included within the cost or deducted from the proceeds of the investment.

Foreign currency
All transactions in foreign currencies are translated into sterling at the rates of exchange ruling on the dates of such transactions. Foreign currency assets and liabilities at the balance sheet date are translated into sterling at the exchange rates ruling at that date. Exchange differences arising on the revaluation of investments held as fixed assets are included in capital reserve - unrealised. Exchange differences arising on the translation of foreign currency assets and liabilities are taken to capital reserve - realised.

Taxation
Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more, or right to pay less, tax in the future have occurred at the balance sheet date. This is subject to deferred tax assets only being recognised if it is considered more likely than not that there will be suitable profits from which the future reversal of the underlying timing differences can be deducted. Timing differences are differences between the Company's taxable profits and its results, as stated in the financial statements, which are capable of reversal in one or more subsequent periods.

Investments
Listed:
Investments listed (or traded) on recognised stock exchanges are valued at closing middle market prices ruling on the balance sheet date subject to provisions for illiquidity or trading restrictions made at the Board's discretion.
Unquoted:
The directors' valuation of unquoted investments is based upon the British Venture Capital Association guidelines using the following criteria:

(i) initially, investments are valued at cost, including fees and transaction costs;
(ii) after the receipt of the first audited financial statements following initial investment, companies are valued by applying a discount of between 25% and 50% to the equivalent listed earnings multiple;
(iii) where more appropriate, investments are valued with reference to their net assets rather than to their earnings; and
(iv) appropriate provisions are made against all individual valuations where necessary to reflect unsatisfactory financial performance leading to diminution in value.

Both realised and unrealised gains and losses arising on investments are taken to capital reserves.

1. Accounting policies continued

Capital reserves
Capital reserve - realised
The following are accounted for in this reserve:
(i) gains and losses on the realisation of investments;
(ii) losses on investments within the portfolio where there is little prospect of realisation or recovering any value;
(iii) realised exchange differences of a capital nature; and
(iv) expenses, together with the related taxation effect, charged to this reserve in accordance with the above policies.

Capital reserve - unrealised
The following are accounted for in this reserve:
(i) increases and decreases in the valuation of investments held at the year end; and
(ii) unrealised exchange differences of a capital nature.

2. Income

	2002 £'000	2001 £'000
Income from investments		
UK listed dividends	**193**	205
UK unquoted investment income	**2,209**	2,622
Overseas listed dividends	**26**	6
	2,428	2,833
Other income		
Gilt interest	**1,060**	954
Deposit interest	**15**	104
Other fees	**25**	2
	1,100	1,060
Total income	**3,528**	3,893
Total income comprises:		
Dividends	**219**	211
Interest	**3,284**	3,680
Other fees	**25**	2
	3,528	3,893

3. Investment management fee

	Revenue		Capital		Total	
	2002	2001	2002	2001	2002	2001
Investment management fee	**337**	382	**1,010**	1,146	**1,347**	1,528
Irrecoverable VAT thereon	**59**	67	**177**	200	**236**	267
	396	449	**1,187**	1,346	**1,583**	1,795

Details of the investment management, custodian and administration contracts are disclosed in the directors' report on pages 21 and 22. The investment management fee is levied quarterly in arrears and is charged 75% to capital reserve – realised and 25% to the revenue account.

4. Other expenses

(a) Operating expenses

	2002 £'000	2001 £'000
Custodian and administration fees	**116**	126
Directors' emoluments (note 5)	**85**	76
Auditor's remuneration - audit services	**17**	17
- non-audit services (interim review and taxation compliance)	**14**	17
Other expenses	**90**	93
	322	329

	2002	2001
The Company's total expense ratio, calculated as a percentage of average net assets and including expenses, after relief for taxation, was:	**1.45%**	1.44%

(b) Reconciliation of net revenue return before finance costs and taxation to net cash flow from operating activities

	2002 £'000	2001 £'000
Net revenue return before finance costs and taxation	**2,810**	3,115
Investment management fee and finance costs charged to capital	**(1,253)**	(1,412)
Interest receivable	**(15)**	(104)
Decrease in accrued income	**357**	687
Decrease in creditors	**(56)**	(67)
Effective yield adjustment	**832**	462
Tax on investment income included within gross income	**(514)**	(638)
Net cash flow from operating activities	**2,161**	2,043

5. Directors' emoluments

The aggregate emoluments of the directors, excluding VAT, where applicable, for the year ended 31 December 2002 were £85,000 (2001: £76,000). The emoluments of the chairman, who was the highest paid director, were £20,000 (2001: £20,000). Emoluments of £13,000 were paid to a third party for making available the services of one director. The Company does not have a share option scheme or any incentive scheme. No pension contributions were made in respect of the directors. There were no employees other than the directors.

6. Interest payable and similar charges

	Revenue		Capital		Total	
	2002 £'000	2001 £'000	2002 £'000	2001 £'000	2002 £'000	2001 £'000
Finance charges	**22**	22	**66**	66	**88**	88

7. Taxation on ordinary activities

(a) Analysis of charge in period

	Revenue		Capital		Total	
	2002 £'000	2001 £'000	2002 £'000	2001 £'000	2002 £'000	2001 £'000
Current tax:						
UK corporation tax	**779**	867	**(376)**	423	**403**	444
Prior year adjustment	**(139)**	(194)	**–**	–	**(139)**	(194)
Total current tax (note 7(b))	**640**	673	**(376)**	(423)	**264**	250

7. Taxation on ordinary activities continued

(b) Factors affecting current revenue tax charge for the period
The tax assessed for the period is lower than the standard rate of corporation tax in the UK for a large company (30%). The differences are explained below:

	2002 £'000	2001 £'000
Revenue return on ordinary activities before taxation	**2,788**	3,093
UK corporation tax at 30% thereon	**837**	928
Effects of:		
Non taxable UK dividends	**(58)**	(68)
Expenses not deductible for tax	**–**	7
Tax deductible expenses in capital	**(376)**	(423)
Tax relief to the capital account	**376**	423
Prior year adjustment	**(139)**	(194)
	(197)	(255)
Current revenue tax charge for the period (note 7(a))	**640**	673

Investment trusts are exempt from corporation tax on capital gains provided the Company obtains agreement from the Inland Revenue that section 842 ICTA tests have been met.

8. Dividend in respect of equity shares

	2002 £'000	2001 £'000
Final proposed dividend of 8.00p (2001: 8.00p) payable on 1 May 2003	**2,015**	2,015

9. Return and net asset value per ordinary share

	2002	2001
Revenue and capital returns per share are shown below and have been calculated using the following:		
Net revenue attributable to equity shareholders after taxation	**£2,148,000**	£2,420,000
Net capital losses for the year	**(£12,091,000)**	(£8,131,000)
Number of shares in issue	**25,186,755**	25,186,755

	Revenue		Capital		Total	
	2002 £'000	2001 £'000	2002 £'000	2001 £'000	2002 £'000	2001 £'000
Return per ordinary share	**8.53p**	9.61p	**(48.01p)**	(32.28p)	**(39.48p)**	(22.67p)

The net asset value per ordinary share of 332.9p (2001: 380.3p) was calculated by dividing equity shareholders' funds of £83,837,000 (2001: £95,795,000) by the number of shares in issue at the year end of 25,186,755 (2001: 25,186,755).

10. Investments

	2002 £'000	2001 £'000
Investments listed on the London and Dublin Stock Exchanges	**2,603**	6,107
Investments traded on NASDAQ	**789**	1,564
Investments traded on the Alternative Investment Market	**1,720**	6,567
Unquoted investments	**62,559**	60,970
	67,671	75,208

10. Investments continued

	2002 £'000	2001 £'000
Equity shares	**17,150**	23,637
Convertible securities	**6,473**	12,024
Fixed income securities	**44,048**	39,547
	67,671	75,208

	Listed £'000	Unquoted £'000	Total £'000
Opening valuation	14,238	60,970	75,208
Opening unrealised (appreciation)/depreciation	(5,578)	3,190	(2,388)
Opening book cost	8,660	64,160	72,820
Movements in the year:			
Additions at cost	142	23,891	24,033
Disposals - proceeds	(678)	(19,568)	(20,246)
- realised gains on sales	133	9,882	10,015
Closing book cost of investments	8,257	78,365	86,622
Closing unrealised depreciation	(3,145)	(15,806)	(18,951)
Closing valuation of investments	5,112	62,559	67,671

Details of significant investments:
The Company has equity holdings of 10% or more of the following classes of share in the investee companies listed below.

Company	Shareholding	% of class*
Bertram Group Holdings Ltd	"A" Ord.	14.6
Bertram Group Holdings Ltd	"C" Ord.	12.6
Biocode Inc	"E" Pref.	11.1
Burns e-Commerce Solutions	Ord.	17.9
Burns e-Commerce Solutions	Pref. Ord.	18.9
Castlebeck Group Ltd	"B" Ord.	17.9
ClinPhone Holdings Ltd	"B" Ord.	13.1
Comnitel Technologies	"A" Ord.	22.8
Comnitel Technologies	Conv. Pref.	11.1
Corinthian Marketing plc	"A" Ord.	31.6
Eagle Rock Entertainment Ltd	Conv. Pref.	18.1
FTE Automotive GmbH	Pref. Ord.	16.4
Newchurch Ltd	"A" Ord.	12.5
Nova Homes Ltd	"A" Ord.	10.4
Orbiscom Ltd	Pref. Ord.	23.0
PARC Group Ltd	"B" Ord.	11.0
Pharma Bio-Research BV	Ord.	13.0
Profiad Ltd	"B" Ord.	13.9
Raymarine Group Ltd	Ord.	14.1
The Sanctuary Spa Group Ltd	"A" Ord.	15.3
SGI (Holdings) Ltd	"A" Ord.	14.8
Trados, Inc	Conv. Pref.	23.1
Trados, Inc	Pref. Ord.	11.5
Tunstall Holdings Ltd	"B" Ord.	12.8

* Investee companies may issue a number of different classes of share. The percentage of the total issued ordinary share capital of the 20 largest investments held by the Company is shown in the table on page 18.

10. Investments continued

The Company holds more than 20% of the total issued share capital (including preference shares) of Corinthian Marketing plc. For the most recent accounting period of this company, the net liabilities were £521,000 and the profit after tax was £232,000.

Further information on those investments which, in the opinion of the directors, have a significant effect on the Company's financial statements is contained in the Investment Manager's Review on pages 3 to 19.

11. Losses on investments and Government securities

	2002 £'000	2001 £'000
Realised gains on sales	**10,233**	5,798
Change in unrealised appreciation	**(21,447)**	(12,940)
	(11,214)	(7,142)

12. Debtors

	2002 £'000	2001 £'000
Taxation recoverable	**450**	583
Prepayments and accrued income	**3,431**	3,788
	3,881	4,371

13. Government securities

	2002 £'000	2001 £'000
Opening valuation	**18,548**	15,508
Purchases at cost	**53,996**	50,687
Sales and redemptions	**(57,979)**	(47,185)
Unrealised capital losses	**(108)**	(119)
Realised capital losses	**(614)**	(343)
Closing valuation	**13,843**	18,548

14. Movement in net funds

Reconciliation of net cash flow to movement in net funds

	2002 £'000	2001 £'000
Change in net funds	**718**	(8,726)
Net funds at 1 January	**313**	9,039
Net funds at 31 December	**1,031**	313

15. Creditors - amounts falling due within one year

	2002 £'000	2001 £'000
Proposed dividend	**2,015**	2,015
Sundry creditors	**574**	630
	2,589	2,645

16. Risk

The following disclosures relating to the risks faced by the Company are provided in accordance with FRS 13, "Derivatives and other financial instruments disclosures".

Financial instruments and risk profile
The Company's primary investment objective is to achieve long-term capital appreciation by investing in unquoted companies. Additionally, the Company may hold listed securities, gilts, cash and short-term deposits and items such as debtors and creditors arising directly from its operations. The numerical disclosures below exclude short-term debtors and creditors. By their very nature, investment activities undertaken to achieve the Company's objective involve certain inherent risks, primarily valuation. These are considered further below.

Valuation risk
The Company's exposure to valuation risk mainly comprises movements in the value of its underlying investments, the majority of which are unquoted. A breakdown of the Company's portfolio is given on page 19. In accordance with the Company's accounting policies, set out on pages 31 and 32, all underlying unquoted investments are valued by the directors in accordance with the current guidelines issued by the British Venture Capital Association. The Company does not hedge against movements in the value of these investments.

In the opinion of the directors, the diversified nature of the Company's portfolio significantly reduces the risks of investing in unquoted companies.

Currency risk
The Company is exposed to currency risk as a result of investing in funds and companies denominated in foreign currencies. The sterling value of these assets can be significantly influenced by movements in foreign exchange rates. The Company does not normally hedge against foreign currency movements affecting the value of its investments, but takes account of this risk when making investment decisions.

Interest rate risk
The Company has exposure to interest rate movements, through cash and gilt holdings.

Financial assets of the Company

	2002				2001			
	Fixed rate £'000	**Floating rate £'000**	**Non interest bearing £'000**	**Total £'000**	Fixed rate £'000	Floating rate £'000	Non interest bearing £'000	Total £'000
Sterling	**51,781**	**1,031**	**16,578**	**69,390**	52,174	313	22,766	75,253
Euro	**2,103**	**–**	**3,432**	**5,535**	1,757	–	8,055	9,812
US dollar	**4,007**	**–**	**3,613**	**7,620**	4,164	–	4,840	9,004
Total	**57,891**	**1,031**	**23,623**	**82,545**	58,095	313	35,661	94,069

The fixed rate assets comprise gilts and fixed rate lendings to investee companies. Fixed rate lendings have a weighted average interest rate of 11% per annum and a weighted average life to maturity of 5.7 years. The floating rate assets consist of cash. The non interest bearing assets represent the equity content of the investment portfolio.

The Company did not have any outstanding borrowings at the year end.

Currency exposure
The currency denomination of the Company's financial assets is shown above. Short-term debtors and creditors, which are excluded, are predominantly in sterling, the functional currency of the Company.

17. Share capital

	2002 Nominal No. '000	2002 £'000	2001 Nominal No. '000	2001 £'000
Authorised:				
Ordinary shares of 25p each	**40,000**	**10,000**	40,000	10,000
Allotted, called up and fully paid:				
Ordinary shares				
At 1 January	**25,187**	**6,296**	25,187	6,296
At 31 December	**25,187**	**6,296**	25,187	6,296

18. Share premium account and reserves

	Share premium account £'000	Capital redemption reserve £'000	Capital reserve – realised £'000	Capital reserve – unrealised £'000	Revenue reserve £'000
Opening reserves as at 1 January 2002	14,123	1,248	68,723	2,388	3,017
Transfer on disposal of investments	–	–	7,760	(7,760)	–
Net gain on sale of investments	–	–	2,255	–	–
Change in unrealised appreciation	–	–	–	(13,579)	–
Losses on Government securities	–	–	(614)	(108)	–
Effective yield adjustment	–	–	832	–	–
Retained net revenue for year	–	–	–	–	133
Management fee and finance costs charged to capital, after taxation	–	–	(877)	–	–
Closing reserves as at 31 December 2002	14,123	1,248	78,079	(19,059)	3,150

19. Reconciliation of movements in shareholders' funds

	2002 £'000	2001 £'000
Opening shareholders' funds	**95,795**	103,521
Revenue profits available for distribution	**2,148**	2,420
Ordinary dividend	**(2,015)**	(2,015)
Revenue surplus for the year	**133**	405
Recognised losses on investment portfolio	**(11,214)**	(7,142)
Management fee and finance costs charged to capital, after taxation	**(877)**	(989)
Movement in shareholders' funds	**(11,958)**	(7,726)
Closing shareholders' funds	**83,837**	95,795

20. Capital commitment and contingent liabilities

At 31 December 2002, investment purchases of £3,275,000 (2001: £6,262,000) had been authorised and contractually committed.

Analysis of Shareholders
31 December 2002

By type of holder

	Number of shares	% of total 2002	% of total 2001	Number of holders	% of total 2002	% of total 2001
Nominee companies	15,900,661	63.1	62.4	168	49.6	41.7
Direct private investors	1,364,309	5.4	5.9	139	41.0	40.5
Others	7,921,785	31.5	31.7	32	9.4	17.8
	25,186,755	100.0	100.0	339	100.0	100.0

By size of holding

	Number of shares	% of total 2002	% of total 2001	Number of holders	% of total 2002	% of total 2001
1 – 5,000	376,234	1.5	1.5	207	61.1	60.9
5,001 – 50,000	1,562,425	6.2	6.2	92	27.1	27.5
50,001 – 100,000	864,408	3.4	3.6	11	3.2	3.3
Over 100,000	22,383,688	88.9	88.7	29	8.6	8.3
	25,186,755	100.0	100.0	339	100.0	100.0

Shareholder Information

Financial calendar
The timing of the announcement and publication of the Company's results may normally be expected in the months shown below:

February/March	Preliminary results and final dividend for year announced. Annual report and financial statements published.
April	Annual General Meeting. Final dividend paid.
September	Interim figures announced and interim report published.

Dividend – 2002
The proposed final dividend in respect of the year ended 31 December 2002 is 8.00p per share.

Ex-dividend date (shares transferred without dividend)	26 March 2003
Record date (last date for registering transfers to receive the dividend)	28 March 2003
Last date for registering DRIP instructions	15 April 2003
Dividend payment date	1 May 2003

Payment of dividends
Cash dividends will be sent by cheque to the first-named shareholder at their registered address, together with a tax voucher. Alternatively, dividends may be paid direct into a shareholder's bank account via BACS (Bankers' Automated Clearing Service). This may be arranged by contacting the Company's registrar, Computershare Investor Services PLC ("Computershare"), on 0870 702 0131. Tax vouchers will be sent to shareholders at their registered address, unless other instructions have been given, to arrive on the payment date.

Dividend reinvestment scheme ("DRIP")
Shareholders may request that their dividends be used to purchase further shares in the Company. Dividend reinvestment forms may be obtained from Computershare on 0870 702 0131. Shareholders who have already opted for dividend reinvestment do not need to re-apply. The last date for registering for this service for the forthcoming dividend is 15 April 2003.

Share price
The Company's mid-market ordinary share price is published daily in the Financial Times under the section "Investment Trusts".

Share dealing
Investors wishing to purchase or sell shares in the Company may do so through a stockbroker. Most banks also offer this service.

Computershare has introduced a telephone share dealing service. This service is available on 0870 703 0084. To use this service, you will need your shareholder reference number, which is detailed on your certificate.

Uncertificated Securities Regulations 1995 – CREST
The Company's ordinary shares have joined CREST, an electronic system for uncertificated securities trading.

Private investors can continue to retain their share certificates and remain outside the CREST system. Private investors are able to buy and sell their holdings in the same way as they did prior to the introduction of CREST, although there may be differences in dealing charges.

Electronic communication/electronic proxy voting
Computershare has introduced electronic communication and electronic proxy voting services for shareholders, although they are not available for the forthcoming AGM. Please refer to the information enclosed with this report, or call 0870 702 0131 for more information.

Duration of the Company
The Company, as currently constituted, was established in 1989. The Articles of Association provide for an ordinary resolution to be put to shareholders at the Annual General Meeting in the year 2004, to call for an Extraordinary General Meeting ("EGM") in the year 2005 to wind up the Company voluntarily. If the convening of the EGM is not approved in 2004, a similar resolution will be put to shareholders in 2009 and every fifth year thereafter.

Nominee code
Where shares are held in a nominee company name, the Company undertakes:

- to provide the nominee company with multiple copies of shareholder communications, so long as an indication of quantities has been provided in advance; and
- to allow investors holding shares through a nominee company to attend general meetings, provided the correct authority from the nominee company is available.

Nominee companies are encouraged to provide the necessary authority to underlying shareholders to attend the Company's general meetings.

Shareholder Information continued

Performance
Past performance is not necessarily a guide to future performance. The value of investments and the income from them may go down as well as up and are not guaranteed. An investor may not get back the amount originally invested.

Publication of net asset value
The net asset value ("NAV") per share of the Company is calculated monthly with respect to cash, cash equivalents and listed investments in the portfolio. Unquoted investments are revalued bi-annually.

The NAV is released to the public by the Association of Investment Trust Companies and through the London Stock Exchange's Regulatory News Service.

Shareholder enquiries
In the event of queries regarding your holding of shares, please contact Computershare on 0870 702 0131. Changes of name or address must be notified in writing to:

Computershare Investor Services PLC
PO Box 435
Owen House
8 Bankhead Crossway North
Edinburgh EH11 4BR

Details relating to your holding can also be checked through the Computershare website. As a security check, specific information is required to gain access to an individual's account. This includes your shareholder reference number, available from either your share certificate or tax voucher. The address of the Computershare website is:
www.computershare.com/investorcentre/UK

General enquiries about the Company should be directed to:

The Secretary
Mercury Grosvenor Trust plc
33 King William Street
London EC4R 9AS
Telephone: 020 7743 3000

Glossary

Investment Trusts

Net asset value per share ("NAV")
This is the value of the Company's assets attributable to one ordinary share. It is calculated by dividing "shareholders' funds" by the total number of shares in issue. For example, as at 31 December 2002, shareholders' funds were £83,837,000 and there were 25,186,755 ordinary shares in issue; the NAV was therefore 332.9p per share.

Shareholders' funds are calculated by deducting current and long-term liabilities, and any provision for liabilities and charges, from the Company's total assets.

Discount
Investment trust shares frequently trade at a discount to NAV. This occurs when the share price is less than the NAV. In this circumstance, the price that an investor pays or receives for a share would be less than the value attributable to it by reference to the underlying assets. The discount is the difference between the share price and the NAV, expressed as a percentage of the NAV. For example, if the NAV were 400p and the share price were 360p, the discount would be 10%.

Premium
A premium occurs when the share price is higher than the NAV and investors would therefore be paying more than the value attributable to the shares by reference to the underlying assets. For example, if the share price were 450p and the NAV were 400p, the premium would be 12.5%.

Discounts and premiums are mainly the consequence of supply and demand for the shares on the stock market.

Private Equity

Expansion capital
The provision of capital to an existing, established business, to finance organic growth or acquisitions - sometimes also known as venture capital.

IPO (initial public offering)
An offering by a company of its share capital to the public with a view to seeking an admission of its shares to a recognised stock exchange.

IRR (internal rate of return)
The annual internal rate of return received by an investor in a fund. It is calculated from cash drawn from and returned to the investor together with the residual value of the fund unit.

LBO (leveraged buy-out)
The purchase of all or most of a company's share capital, usually by its managers, funded mainly by borrowings often secured on the company's assets, resulting in a post-financing capital structure of the company which is heavily geared.

LP (Limited Partnership)
An organisation made up of a managing general partner and limited partners, who invest money but have limited liability, are not involved in day-to-day management, and usually cannot lose more than their capital contribution. Usually limited partners receive income, capital gains and tax benefits; the general partner usually receives a fee and a percentage of capital gains and income.

MBI (management buy-in)
A change of ownership, where an incoming management team raises financial backing, normally a mix of equity and debt, to acquire a business.

MBO (management buy-out)
A change of ownership, where the incumbent management team raises financial backing, normally a mix of equity and debt, to acquire a business it manages.

P2P (public to private)
The purchase of all of a listed company's shares using a special-purpose vehicle funded with a mixture of debt and unquoted equity.

Quoted company
Any company whose shares are listed or traded on a recognised stock exchange.

Unquoted company
Any company whose shares are not listed or traded on a recognised stock exchange.

Notice of Annual General Meeting

Notice is hereby given that the Annual General Meeting of Mercury Grosvenor Trust plc will be held at the offices of CMS Cameron McKenna, Mitre House, 160 Aldersgate Street, London EC1A 4DD, on Tuesday, 29 April 2003 at 11.30 a.m. to transact the following business:

Ordinary business

1. To receive the report of the directors and the financial statements for the year ended 31 December 2002, together with the report of the independent auditor thereon.

2. To receive the directors' remuneration report.

3. To declare a dividend of 8.00p per share.

4. To re-elect Mr T J Amies as a director.

5. To re-appoint Ernst & Young LLP as independent auditor to the Company.

6. To authorise the directors to determine the independent auditor's remuneration.

Special business

To consider and, if thought fit, pass the following resolutions numbered 7 and 9 as special resolutions and resolution 8 as an ordinary resolution.

7. THAT in substitution for the Company's existing authority to make market purchases of ordinary shares of 25p in the Company ("ordinary shares"), the Company be and it is hereby authorised in accordance with section 166 of the Companies Act 1985 ("the Act") to make market purchases of ordinary shares (within the meaning of section 163 of the Act) provided that:

   (i) the maximum number of ordinary shares hereby authorised to be purchased is 3,775,000;

   (ii) the minimum price which may be paid for an ordinary share shall be 25p;

   (iii) the maximum price (exclusive of expenses) which may be paid for an ordinary share shall be the lower of 5% above the average of the market values of the ordinary shares for the five business days immediately preceding the date of the purchase and the net asset value per ordinary share on the date of purchase; and

   (iv) unless renewed, the authority hereby conferred shall expire on 28 October 2004 save that the Company may, prior to such expiry, enter into a contract to purchase ordinary shares which will or may be completed or executed wholly or partly after such expiry.

8. THAT:

   (i) the directors be and they are hereby generally and unconditionally authorised, in accordance with section 80 of the Companies Act 1985 ("the Act"), to exercise all the powers of the Company to allot relevant securities (as defined in that section) up to an aggregate nominal amount of £314,800 provided that this authority shall expire on the date of the next Annual General Meeting of the Company after the passing of this resolution, but so that this authority shall allow the Company, acting by its directors, to make offers or agreements before the expiry of this authority which would or might require relevant securities to be allotted after such expiry;

   (ii) all authorities previously conferred under section 80 of the Act be and they are hereby revoked, provided that such revocation shall not have retrospective effect; and

   (iii) words and expressions defined in or for the purposes of Part IV of the Act shall bear the same meanings in this resolution.

9. THAT, subject to and conditional upon the passing as an ordinary resolution of the resolution numbered 8 set out in the notice of this meeting, the directors be and they are hereby empowered, pursuant to section 95 of the Companies Act 1985 ("the Act"), to allot equity securities (as defined in section 94 of the Act) of the Company for cash pursuant to the authority conferred by the previous resolution as if section 89 (1) of the Act did not apply to any such allotment, provided that this power shall be limited to the allotment of equity securities:

   (i) which are, or are to be, wholly paid up in cash up to an aggregate nominal value of £314,800 at a price of not less than the net asset value per ordinary share as at the most recent practicable date, as determined by the directors;

   (ii) (otherwise than pursuant to sub-paragraph (i) above) in connection with issues by way of rights in favour of all holders of ordinary shares where the equity securities respectively attributable to the interests of all such holders are either proportionate (as nearly as may be) to the respective numbers of ordinary shares held by them or are otherwise allotted in accordance with the rights conferred on such equity securities (but subject in either case to such exclusions or other arrangements as the Board may deem necessary or expedient in relation to fractional entitlements or legal practical problems under the laws of, or the requirements of, any regulatory body or any stock exchange in any territory or otherwise howsoever);

   and shall expire on the earlier of the date which is 15 months after the date on which this resolution is passed and the date of the next Annual General Meeting of the Company after the passing of this resolution, save that the Company may before such expiry make an offer or agreement which would or might require equity securities to be allotted after such expiry;

(iii) all powers previously conferred under section 95 of the Act be and they are hereby revoked, provided that such revocation shall not have retrospective effect; and

(iv) words and expressions defined in or for the purposes of Part IV of the Act shall bear the same meanings in this resolution.

By order of the Board
Merrill Lynch Investment Managers Group Services Limited
Secretary
18 March 2003

Notes:

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

2. Proxy forms must reach the office of the Company's registrars in Bristol by 11.30 a.m. on 27 April 2003. A form of proxy is provided to shareholders with the annual report. Completion and return of the form of proxy will not prevent a member from attending the meeting and voting in person.

3. 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 11.00 p.m. on 27 April 2003 ("the specified time"). If the meeting is adjourned to a time not more than 48 hours after the 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 determining the numbers 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 before the time fixed for the adjourned meeting or, if the Company gives notice of the adjourned meeting, at any time specified in that notice.

4. No service contracts exist between the Company and any of the directors, who hold office in accordance with letters of appointment and the Articles of Association.

Management and Administration

Registered Office
(Registered in England No. 1525583)
33 King William Street
London EC4R 9AS

Investment Manager
HgCapital*
Third Floor, Minerva House
3-5 Montague Close
London SE1 9BB
Telephone: 020 7089 7888
www.hgcapital.net

Hg Investment Managers Limited, trading as HgCapital, was formed as an independent company in December 2000, until which time it had been a division of Merrill Lynch Investment Managers Limited ("MLIM"). The Company has an investment management agreement dated 30 March 1995 with MLIM, which has delegated its investment management duties thereunder to HgCapital.

Merrill Lynch Investment Managers Limited* is a subsidiary of Merrill Lynch & Co., Inc.

Secretary and Administrator
Merrill Lynch Investment Managers
Group Services Limited
33 King William Street
London EC4R 9AS
Telephone: 020 7743 3000

Stockbroker
Credit Lyonnais Securities Europe*
Broadwalk House
5 Appold Street
London EC2A 2DA

Custodian
The Bank of New York Europe Limited*
One Canada Square
London E14 5AL

Registrar
Computershare Investor Services PLC*
PO Box 435, Owen House
8 Bankhead Crossway North
Edinburgh EH11 4BR
Telephone: 0870 702 0131

Independent Auditor
Ernst & Young LLP
Rolls House
7 Rolls Buildings
Fetter Lane
London EC4A 1NH

*Authorised and regulated by the Financial Services Authority.