The Scottish Investment Trust PLC

Annual Results for the year to 31 October 2018.

***The Scottish Investment Trust PLC** invests internationally and is independently managed. Its objective is to provide investors, over the longer term, with above-average returns through a diversified portfolio of international equities and to achieve dividend growth ahead of UK inflation. Today it announces its results for the year to 31 October 2018.*

Highlights

- Regular dividend increased by 6% to 21.2p
- 35th consecutive year of regular dividend increase
- Additional special dividend of 4p
- Share price total return +1.9% and NAV total return +1.1%

Chairman's Statement

Performance

I am pleased to report that the Company delivered another year of positive total returns during the twelve months to 31 October 2018. The share price total return was +1.9% and the net asset value per share (NAV) total return (with borrowings at market value) was +1.1%.

The Company does not have a formal benchmark but, by way of comparison, the sterling total return of the international MSCI All Country World Index (ACWI) was +3.4% while the UK based MSCI UK All Cap Index total return was -1.3%.

As noted in previous communications, we do not expect the Company's portfolio to match any particular index return over any defined period due to the contrarian nature of the portfolio's composition. Our contrarian approach aims to achieve above-average returns over the longer term.

Investment approach

The investment management industry continues to undergo rapid change. A clearer distinction is now made between passive and active investment management. Increasingly, investors wish to either track a stockmarket index or, instead, seek a genuinely active and differentiated approach.

Passive products, by design, take no account of valuations or future prospects. We think this creates an opportunity for an active, long-term investor.

The high conviction, global contrarian investment approach adopted by Alasdair McKinnon and his team clearly distinguishes the Company from our global investment trust peers and from passive investment products.

The approach aims to profit by investing in carefully selected, but unfashionable, companies which appear undervalued as they are overlooked by other investors who prefer the comfort of investing with the crowd. As an independent investment trust, The Scottish is able to take this differentiated view in the long-term interest of shareholders.

This contrarian philosophy is reflected in the portfolio which is constructed without reference to any benchmark or stockmarket index. We do not expect the portfolio return to be similar to a particular index return in any given year and we expect that the contrarian style will work differently depending on market conditions. For example, the Manager expects that the Company might not participate fully in more speculative market conditions as the investment team seeks to avoid investments that are sustained by overly enthusiastic sentiment.

Growing our following

The Scottish has made many important changes in recent years, which I have discussed in previous Chairman's Statements. The aim of these changes was to continue to provide an attractive, low cost investment vehicle for our shareholders who are mainly individuals. We aim to grow our loyal following as the merits of our approach are increasingly recognised. In this regard, it is pleasing to note that we were voted Best Investment Trust in the 2018 Shares Awards, received the award for Best PR Campaign from The Association of Investment Companies and were awarded Best Investment Trust for Income at the Online Personal Wealth Awards.

A very visible change has been our reinvigorated approach to marketing and investor communications. By communicating our distinct investment style in an engaging manner, we aim to stimulate additional demand for the Company's shares to seek to ensure that the discount to NAV remains at or below 9% with a reduced recourse to share buybacks. The team has produced a wealth of thought-provoking content which is shared on our website and social media. I would encourage you to follow us on Twitter and LinkedIn. News and articles can be found on our website and you can also subscribe to our monthly email.

Dividend policy
The year to 31 October 2018 was the first year of our higher and more frequent dividend. A full rationale for these changes was outlined in last year's annual report but, as a reminder, the key elements are summarised below.

Last year there was a step change increase in the regular dividend, lifting it by nearly half, as well as a shift to quarterly dividend payments. The contrarian style does not explicitly target higher yielding investments but is expected to generate a higher than average level of income through an investment cycle. If there are occasions when the portfolio does not generate a sufficient level of income to cover the requirements of the regular dividend, the Board considers that it would be appropriate to utilise the Company's healthy revenue reserve.

Shareholders now have a clearer indication of the income that they can expect to receive from their investment while gaining a more regular income stream. Following this step change increase, the Company has one of the highest stated dividend yields among its global investment trust peers.

Income and dividend
Over the past year, earnings per share rose by 12.8% to 26.0p (2017: 23.1p).

The Board recommends a final dividend of 6.2p which, if approved, will mean that the total regular dividend for the year will increase by 6.0% to 21.2p and will be the 35th consecutive year of regular dividend increase.

The Board's target is to declare three quarterly interim dividends of 5.3p for the year to 31 October 2019 and recommend a final dividend of at least 5.3p for approval by shareholders at the Annual General Meeting in 2020. The final dividend will be reviewed in accordance with the Board's desire to continue the long track record of annual dividend increases and the aim of the Company to provide dividend growth ahead of UK inflation over the longer term.

As outlined in my statement last year, the Company is less likely to pay discretionary special dividends in future years but, as the income generated for the year to 31 October 2018 is substantial, the Board recommends a special dividend of 4.0p.

Amendments to the Articles of Association
As part of the business to be proposed at the Annual General Meeting, the Board is seeking shareholder approval for the adoption of new Articles of Association, primarily to take account of legislative changes and developments in market practice. Certain statutory rules governing investment trusts and companies were amended in 2012. In particular, the rule which prohibited an investment trust from distributing any surplus arising from the realisation of its investments was repealed. In compliance with the previous statutory regime, the Company has a provision in its current Articles which expressly prohibits the distribution of any surplus arising from the realisation of any investment. In the light of the amended statutory rules, the Board no longer considers it appropriate for the Articles to contain such a prohibition and therefore proposes that it is removed. The Board believes that the removal of this restriction will give the Company greater flexibility in the long-term as it will enable the Company to make distributions from any surplus arising from the realisation of any investment. However, the Board has no intention of exercising this authority at the current time.

The Board is also taking the opportunity to propose some additional amendments to the Articles to increase the aggregate limit of Directors' remuneration in each year from £250,000 to £300,000 and to reflect other recent regulatory changes including, for example, in relation to the Company's international tax reporting obligations and the Alternative Investment Fund Managers Directive. The increase in the aggregate limit of Directors' remuneration provides additional flexibility over the number of Directors on the Board and ensures that the Company continues to have the ability to pay Directors' fees in line with the market in the future.

Discount, share buybacks and ongoing charges
The Company follows a policy that aims, in normal market conditions, to maintain the discount to NAV (with borrowings at market value) at or below 9%. The average discount over the year was 8.6%.

During the year, 2.3m shares were purchased for cancellation at an average discount of 9.3% and a cost of £19.5m. In the previous year, 16.9m shares were purchased, although this included the exit of Aviva from the share register who were generally selling investment trust holdings inherited through its purchase of Friends Life. Excluding the Aviva transaction, 5.5m shares were purchased in the previous year.

The ongoing charges figure (OCF) for the year under review of 0.52% (2017: 0.49%) remains favourable compared with other actively-managed investment vehicles. All else being equal, a lower share count from buying back shares increases the OCF. As a self-managed investment trust, the OCF represents the ongoing costs of running the Company as a proportion of net assets. We have substantially reduced our costs in recent years.

Gearing
After a period of strong performance from markets, when combined with a seemingly greater than usual number of potentially destabilising events, the Company reduced gearing to 0% in August. Prior to this, gearing had been maintained at around 5% for a number of years. This proved a timely change in light of the subsequent correction in markets, but we continue to review opportunities to deploy gearing for the long-term benefit of shareholders.

Outlook
Politics has changed in recent years. The consensual politician, driven by focus groups, is a species on the wane. Meanwhile, politicians with a greater tendency to shoot from the hip and to challenge established norms have been in the ascendancy.

The drivers of this trend are complicated but very important must be the fact that, economically, it has been a poor decade for large sections of the population in a number of countries. Politicians now seem to have adopted a mantra that the benefits of economic growth must be spread more equally within their own borders whilst eroding their commitments to balance budgets.

Central banks continue a creep towards the ‘normalisation’ of monetary policy following a long period of crisis measures. The US Federal Reserve is most advanced in this strategy, but the difficulty of this challenge when debt levels are high is best highlighted by the fact that President Trump has launched hostile tweets criticising its endeavours.

Brexit negotiations remain what best can be described as complex. We expect any perceived progress to be reflected in the value of sterling.

There are a number of other geopolitical issues that could move markets in either direction, depending on how they develop. The most obvious concerns are the apparent slowdown in the Chinese economy, the state of relations between the US and China, a debt crisis in Turkey, the actions of the new Italian government and US relations with Iran.

The larger than usual number of risks, combined with the strong performance of equities in recent years, mean that the Company currently has a cautious view about the short-term outlook for markets.

The Board is pleased with the progress made to transform the investment approach, the increase in the regular dividend and the improvement in the profile of the Company. It believes that the Company is differentiated, cost competitive and an attractive investment vehicle focused on delivering above-average returns and dividend growth over the longer term.

James Will
Chairman
7 December 2018

Manager's Review

It's too early to tell

In a conversation with US President Richard Nixon in 1972, the Chinese Prime Minister, Zhou Enlai, reputedly quipped that it was 'too early to tell' when asked about the impact of the French Revolution on Western civilisation. After listening to the translated reply, President Nixon was delighted by this profound example of far-sighted wisdom with reference, he presumed, to the seismic events of 1789. Disappointingly, witnesses to the conversation have subsequently insisted that the Prime Minister was, in fact, referring to the Paris student riots of 1968. However, the misunderstanding was allowed to stand, possibly because it suited all concerned.

Whatever actually happened in the above exchange, the episode does suggest two things that have relevance for today. Firstly, it is reasonable to expect major events in human history to cause reverberations for surprisingly long periods of time and, secondly, reality can be distorted to suit the interests of those involved.

The financial world has recently marked the tenth anniversary of the defining moment of the financial crisis of 2008/9, namely the collapse of Lehman Brothers. The occasion prompted more than a dollop of self-satisfied backslapping from the economics profession, politicians and officials about the inspired actions taken to avert a meltdown. The various measures employed were presented as calmly rationalised options that were deployed with known outcomes. The truth, of course, was far less edifying. In reality, increasingly panicked measures were thrown like mud at a wall in the hope that one of them would stick. Major industries were bailed out, toxic asset purchases arranged, sales taxes cut, accounting rules suspended, interest rates slashed to near zero and 'quantitative easing' (a clever way of printing money) was introduced. Eventually the rot was stopped.

Of course, something had to be done. But it is worth bearing in mind that some of the policies employed would have been considered downright heretical by mainstream economists even a few weeks before they were deployed. Further, despite a short history of usage, zero (or even negative) interest rates and quantitative easing are today treated as legitimate and controllable policy options that can be tweaked as required. From this, we can only surmise that, like the conversation in 1972, reality has been 'revised' to suit all concerned.

Despite this desire to paint a picture of certainty and control, the various crisis rescue measures have already introduced a raft of unintended consequences. Perhaps the biggest of these has been the increase in wealth inequality, particularly across generations. There are now fewer people with a meaningful stake in the system and, as they tend to be younger, the full implications of this will take some time to become clear.

If excessive debt was one of the main contributing factors to the financial crisis, the measures taken over the past ten years have not addressed this. In fact, they have arguably made it worse.

It seems unlikely that an entire generation will commit itself to a life of indentured servitude to repay debt that they had no choice but to accumulate. History would instead suggest that the rules of the system will be changed. It is, of course, 'too early to tell' how the rules will change but the time-tested solution is currency debasement, in other words inflation.

Our Approach

In previous Manager's Reviews, I have outlined the simple philosophy that underpins our contrarian approach to investment. At the core of this philosophy is a recognition that investors are not, in aggregate, dispassionate calculating machines but, instead, make decisions based heavily on emotion.

While this may not seem a surprising observation, it nonetheless conflicts with the conclusions of substantial bodies of research in finance and economics. Conventional theory essentially expounds that 'the wisdom of the crowd' ensures that the irrational decisions of individuals are cancelled out and a rational decision is reached.

There is, of course, a sound logic to this theoretical point of view. Our very civilisation has been created by the ability of the crowd to achieve great things. Living standards are far higher because we work as a group allowing division of labour, specialisation and economies of scale. In short, 'many hands make light work'.

A second trait that we possess is a desire to imitate the successful actions of others as a way to quickly acquire accumulated knowledge. There might be many ways to skin a cat, but it makes sense to replicate the most efficient method while bypassing a period of trial and error.

So, in the 'real' world, sticking with the crowd and copying success are both useful human characteristics.

However, we believe that these useful instincts do not translate well into the 'virtual' world of financial markets.

The trouble is that, unlike a physical task, copying others in investment markets does not necessarily yield the same result. There are too many dynamic factors at work and the starting point is not static.

There is an assumption that, if an investment appears well positioned the price will go up, whereas if an investment appears poorly positioned the price will go down. But this is not necessarily the case. If expectations are high, favourable trends can continue but the price can go down if expectations are not met. Likewise, unfavourable trends can continue but if they are better than expected, the price can go up.

Overall, by the time an investment has performed sufficiently well (or badly) for it to become an accepted wisdom, conditions are ripe for the trend to change. It is this momentum mentality which creates the business cycle and the numerous bubbles (and subsequent busts) which have always bedevilled investment markets.

We do not attempt to follow investment fashions and instead seek investments in which we can foresee long term upside. We actively seek unpopular areas because this is where the balance between risk and reward can be most favourable. Rather than perpetual trends, we believe in cycles, and we use this thought process to maximise the odds in our favour.

To apply our approach, we divide the stocks in which we invest into three categories.

First, we have those that we describe as ugly ducklings – unloved shares that most investors shun. These companies have endured an extended period of poor operating performance and, for the majority, the near-term outlook continues to appear uninspiring. However, we see their out-of-favour status as an opportunity and can foresee the circumstances in which these investments will surprise on the upside.

The second category consists of companies where change is afoot. These companies have also endured a long period of poor operating performance but have recently demonstrated that their prospects have significantly improved. However, other investors continue to overlook this change for historical reasons.

In our third category, more to come, we have investments that are more generally recognised as good businesses with decent prospects. However, we see an opportunity as we believe there is scope for further improvement that is not yet fully recognised.

The Portfolio

We have a number of holdings in retailers and these produced some of our largest gains during the year. Each was different but, generally, we thought pessimism surrounding long-established retailers had reached a crescendo, creating 'ugly duckling' opportunities. US department store operator Macy's (+£12.1m) produced better than expected results, aided by a revitalised approach and an improved consumer environment. US retailer Target (+£4.9m) benefited from the same themes and the introduction of a more convenient store format. UK supermarket retailer Tesco (+£4.8m) is making good progress towards rebuilding the profitability of its domestic business after well documented problems. The combination with Booker should deliver superior purchasing power. US retailer GAP (+£2.2m) has continued to see strong results from the Old Navy and Athleta brands, albeit this has been largely overshadowed by a lack of progress at the namesake brand. UK retailer Marks & Spencer (-£2.2m) is undergoing a far-reaching transformation overseen by turnaround expert Chairman Archie Norman. We continue to believe that the company, which remains very profitable, has a great brand which can be revived.

NAV Absolute Performance Attribution
Year to 31 October 2018

	Contribution %
Equity portfolio (ungeared)	+0.6
Gearing	+0.5
Total equities	**+1.1**
Other income and currency	+0.2
Buybacks	+0.2
Expenses	-0.6
Interest charges	-0.5
Change in market value of borrowings	+0.7
Change in pension liability	0.0
NAV with borrowings at market value total return	**+1.1**

Top Ten Gains and Losses
Year to 31 October 2018

	Performance† %	Gains £m		Performance† %	Losses £m
Macy's	99.0	12.1	ING	-30.0	-8.7
Pfizer	30.4	6.5	Standard Chartered	-25.4	-7.0
Target	25.7	4.9	BNP Paribas	-26.5	-4.9
Tesco	19.4	4.8	General Electric*	-51.2	-4.0
GlaxoSmithKline	17.3	4.3	Cemex*	-27.7	-3.8
Sony	46.1	4.3	Newmont Mining	-17.1	-3.4
BHP Billiton	21.3	3.9	Newcrest Mining	-10.8	-3.2
Verizon Communications	28.7	2.9	Adecco	-33.7	-3.1
Royal Dutch Shell	12.0	2.9	BASF	-24.1	-2.9
TGS Nopec Geophysical	56.1	2.7	Marks & Spencer	-8.5	-2.2

* Sold during the year.
† Total return on investment, taking into account both capital returns and entitlement to dividends declared, for the period the investment was held during the year.

US pharmaceutical company Pfizer (+£6.5m) gained as the company's lowly valuation was re-evaluated in light of a promising pipeline of new products. UK company GlaxoSmithKline (+£4.3m) reassured investors about the sustainability of the dividend after sensibly opting to buy Novartis's share of their consumer healthcare joint venture rather than pursuing a more ambitious acquisition. The new CEO is determined to better commercialise the company's gargantuan R&D efforts.

Energy stocks were volatile but generally performed well over the year as resurgent oil prices and efforts to reduce costs boosted cash flows. Our largest gain in this sector came from UK listed oil major Royal Dutch Shell (+£2.9m) which has done an excellent job of transforming its portfolio and managing costs, driving a rebound in cash flow. We also saw gains from TGS Nopec Geophysical (+£2.7m), Hess (+£2.5m) and Total (+£2.1m).

UK listed miner BHP Billiton (+£3.9m) gained as the more favourable commodity price environment, alongside productivity improvements, helped drive solid cash flow and dividend growth. Our investments in unloved gold miners, including Newcrest Mining (-£3.2m) and Newmont Mining (-£3.4m), delivered negative returns. Gold has been out of favour in recent years, but we think it looks well placed for a recovery. We see gold as both a potential safe haven and a potential beneficiary if the inflationary environment picks up.

European banks have recovered well in recent years, benefiting from attractive valuations and a more settled regulatory environment. However, this year was tougher as uncertain European politics and concerns regarding emerging markets weighed on sentiment. We made losses in our holdings in ING (-£8.7m) and BNP Paribas (-£4.9m). UK listed but emerging market exposed bank Standard Chartered (-£7.0m) was impacted by the slowdown in these markets. We increased our holding in Sumitomo Mitsui Financial Group (+£1.0m) as we considered it likely to be a beneficiary of any rise in bond yields in Japan.

Mexican cement producer Cemex (-£3.8m) was hampered by a combination of headwinds and we sold our holding due to the changing political climate in Mexico. We also sold our holding in US industrial conglomerate General Electric (-£4.0m) as a quick succession of leadership changes led to a reset of expectations for earnings and the dividend. BASF (-£2.9m) declined as trade tensions weighed on stocks sensitive to economic growth. Swiss based recruiter Adecco (-£3.1m) performed poorly as the outlook for European economic growth remained muted.

Japanese electronics and entertainment group Sony (+£4.3m) gained as an extensive restructuring delivered growing profits following years of losses. Our investment in US telecommunications provider Verizon Communications (+£2.9m) rose as it focused on upgrading its network to win customers in a mature market and its lowly valuation was reconsidered.

Honourable mentions must also be made for two stocks we sold completely during the year. Rentokil Initial, which was an unloved and underperforming conglomerate and is now a business focused chiefly on pest control, produced a total return for us of +£24m over the period we held the shares. Australian based global wine producer, Treasury Wine Estates, which was for a long time our largest holding, has been an exceptional investment, providing a total return of +£39m over the three years we held the shares. These companies have transformed and their progress is now more widely recognised. While their prospects remain promising, we believe they are now reflected in the share prices and consider that the balance of risk and reward is no longer as favourable.

Outlook

In my youth, I read The Ragged Trousered Philanthropists by Robert Tressell. Looking back, the book presented socialist ideas in a more digestible form and the title was meant to illustrate the irony of poverty stricken ‘philanthropists’ performing gruelling work for inadequate pay on behalf of avaricious masters.

I always considered the title very clever, as it summed up the thrust of the book, and as I look at today’s stockmarket, I wonder if the author would have managed a wry smile at the gigantic malinvestment in the ecommerce area. Today, investors are acting as philanthropists as they subsidise unprofitable user growth by ‘disruptive’ entrants in a variety of areas. Investments connected with internet shopping, food delivery, ride hailing services, scooter rentals, music streaming and video streaming, to name just some, are strongly favoured by investors despite their continued propensity to burn cash. That the consumer appreciates a service sold below the cost of production is not a surprise. The challenge is converting a subsidised, or free service, to a sustainably profitable business model. The lack of scepticism about the difficulty of achieving this is a symptom of ten years of cheap money.

In recent reviews, I have noted some concern with regard to investor attitudes to risk driven by a fear of missing out. The mania for cryptocurrency get-rich-quick schemes proved to be brief but was concerning as it represented a proxy for both the ease and speculative nature of financial conditions. The investor infatuation with all things technological was also highlighted as a concern as the area appeared to be awash with both cash and excessive optimism. The premium smartphone boom has peaked, social media is now subject to increasing regulatory pressure and the ecommerce business model will have to evolve further. We have minimal exposure to these areas as we see elevated expectations and thus scope for disappointment.

It is now increasingly popular for politicians to pledge tax cuts and increased spending in anticipation of these actions generating improved future growth (and hence tax revenues). This may well prove correct but, equally, once politicians get a taste for this type of strategy, it is the first step on the road to currency debasement via inflation. That said, this is likely to be a lengthy journey, as a large number of stakeholders favour the status quo.

Generally speaking, the spread of valuations across the market is wide and we continue to identify opportunities that we believe will generate good long-term returns for shareholders.

As I have previously noted, as contrarian investors we actively seek unfashionable and unpopular investments that we believe can recover. This is where we find the best balance between risk (expectations are low) and reward (things can get better). Our investment approach is designed to anticipate and benefit from change and we will continue to seek out opportunities with potential to profit the long-term investor.

Alasdair McKinnon
Manager
7 December 2018

For further information, please contact: info@thescottish.co.uk or 0131 225 7781.

Financial Summary

	2018	2017	Change %	Total Return %
NAV with borrowings at market value	900.1p	924.4p	(2.6)	+1.1
NAV with borrowings at amortised cost	926.8p	956.8p	(3.1)	+0.4
Ex-income NAV with borrowings at market value	888.9p	904.8p	(1.8)	
Ex-income NAV with borrowings at amortised cost	915.5p	937.2p	(2.3)	
Share price	825.0p	843.0p	(2.1)	+1.9
Discount to NAV with borrowings at market value	8.3%	8.8%		
MSCI ACWI			+1.4	+3.4
MSCI UK All Cap Index			(5.1)	(1.3)
	£'000	£'000		
Equity investments	717,547	801,302		
Net current assets	82,931	43,897		
Total assets	800,478	845,199		
Long-term borrowings at amortised cost	(83,829)	(83,737)		
Pension liability	(1,337)	(1,091)		
Shareholders' funds	715,312	760,371		
Earnings per share	26.02p	23.06p	+12.8	
Regular dividend per share (2018: proposed final 6.20p)	21.20p	20.00p	+6.0	
Special dividend per share	4.00p	5.00p		
Total dividend per share	25.20p	25.00p	+0.8	
UK Consumer Prices Index – annual inflation			+2.4	

Year's High & Low

	Year to 31 October 2018		Year to 31 October 2017	
	High	Low	High	Low
NAV with borrowings at market value	991.8p	844.9p	938.2p	817.1p
Closing share price	902.0p	771.0p	850.0p	739.0p
Discount to NAV with borrowings at market value	10.7%	6.2%	12.2%	7.1%

List of Investments
As at 31 October 2018

Listed Equities

Holding	Country	Market value £'000	Cumulative weight %
Tesco	UK	32,230	
Sumitomo Mitsui Financial	Japan	29,130	
GlaxoSmithKline	UK	29,087	
Pfizer	US	27,325	
Target	US	26,686	
Royal Dutch Shell	UK	25,891	
Newcrest Mining	Australia	25,718	
Macy's	US	25,146	
Gap	US	25,084	
Suncor Energy	Canada	24,212	37.7
Marks & Spencer	UK	21,935	
BHP Billiton	UK	21,248	
Newmont Mining	US	20,497	
Standard Chartered	UK	20,348	
ING	Netherlands	19,795	
Exxon Mobil	US	19,704	
PepsiCo	US	17,327	
Roche	Switzerland	16,143	
Total	France	15,565	
Citigroup	US	15,344	63.9
China Mobile	Hong Kong	15,009	
Mitsubishi UFJ Financial	Japan	14,115	
Chevron	US	13,979	
United Utilities	UK	13,838	
Sony	Japan	13,525	
BNP	France	13,143	
National Oilwell Varco	US	12,987	
Verizon Communications	US	12,752	
British Land	UK	12,497	
Vinci	France	11,668	82.5
Royal Bank of Scotland	UK	9,452	
Hess	US	8,979	
BASF	Germany	8,969	
East Japan Railway	Japan	8,899	
Citizens Financial	US	8,156	
Carrefour	France	8,144	
Bank of Kyoto	Japan	7,730	
Nintendo	Japan	7,645	
TGS Nopec Geophysical	Norway	7,497	
BT	UK	6,926	94.8
Adecco	Switzerland	6,044	
Intesa Sanpaolo	Italy	5,784	
Bank of Ireland	Ireland	5,654	
Baker Hughes	US	5,302	
KDDI	Japan	5,013	
Diamond Offshore Drilling	US	4,769	
BorgWarner	US	3,608	
Tourmaline Oil	Canada	2,563	
Freehold Royalties	Canada	1,871	
Greggs	UK	1,114	
Total listed equities		**716,047**	**99.8**

Unlisted

Holding	Country	Market value £'000	Cumulative weight %
Heritable property and subsidiary	UK	1,500	
Total unlisted		**1,500**	**0.2**
Total equities		**717,547**	**100.0**

Distribution of Total Assets

By Sector	31 October 2018 %	31 October 2017 %
Energy	17.9	15.2
Materials	9.5	8.4
Industrials	3.3	10.0
Consumer Discretionary	14.6	8.6
Consumer Staples	7.2	11.8
Health Care	9.1	8.5
Financials	18.8	19.2
Information Technology	-	4.5
Communication Services	5.9	5.2
Utilities	1.7	1.9
Real Estate	1.6	1.5
Net current assets	10.4	5.2
Total assets	**100.0**	**100.0**

By Region	31 October 2018 %	31 October 2017 %
UK	24.5	28.6
Europe (ex UK)	14.8	17.9
North America	34.5	26.5
Latin America	-	3.0
Japan	10.7	8.2
Asia Pacific (ex Japan)	5.1	10.6
Net current assets	10.4	5.2
Total assets	**100.0**	**100.0**

Allocation of Shareholders' Funds

	31 October 2018 %
Total equities	**100.3**
Net current assets	11.6
Borrowings at amortised cost	-11.7
Pension liability	-0.2
Shareholders' funds	**100.0**

Changes in Asset Distribution

	31 October 2017 £m	Net purchases (sales) £m	Appreciation (depreciation) £m	31 October 2018 £m
Energy	128.5	8.1	6.7	143.3
Materials	70.9	16.9	(11.4)	76.4
Industrials	84.2	(47.8)	(9.8)	26.6
Consumer Discretionary	73.1	27.0	17.0	117.1
Consumer Staples	99.4	(49.0)	7.3	57.7
Health Care	72.1	(8.9)	9.4	72.6
Financials	162.5	18.1	(30.4)	150.2
Information Technology	37.7	(36.7)	(1.0)	-
Communication Services	44.3	3.1	(0.1)	47.3
Utilities	15.9	-	(2.1)	13.8
Real Estate	12.7	-	(0.2)	12.5
Total equities	**801.3**	**(69.2)**	**(14.6)**	**717.5**

Changes in Shareholders' Funds

	31 October 2017 £m	Net purchases (sales) £m	31 October 2018 £m	Appreciation (depreciation) £m	Dividend income £m	Total return £m
Total equities	**801.3**	**(69.2)**	**717.5**	**(14.6)**	**23.7**	**9.1**
Net current assets	43.9	39.0	82.9			
Total assets	845.2	(30.2)	800.4			
Borrowings at amortised cost	(83.7)	(0.1)	(83.8)			
Pension liability	(1.1)	-	(1.3)			
Shareholders' funds	**760.4**	**(30.3)**	**715.3**			

Income Statement
For the year to 31 October 2018

	2018 Revenue £'000	2018 Capital £'000	2018 Total £'000	2017 Revenue £'000	2017 Capital £'000	2017 Total £'000
Net (losses)/gains on investments held at fair value through profit and loss	-	(14,566)	(14,566)	-	50,816	50,816
Net gains/(losses) on currencies	-	819	819	-	(1,185)	(1,185)
Income	25,854	-	25,854	25,898	-	25,898
Expenses	(2,045)	(1,209)	(3,254)*	(2,075)	(1,442)	(3,517)
Net Return before Finance Costs and Taxation	23,809	(14,956)	8,853	23,823	48,189	72,012
Interest payable	(1,732)	(3,217)	(4,949)	(2,474)	(2,475)	(4,949)
Return on Ordinary Activities before Tax	22,077	(18,173)	3,904	21,349	45,714	67,063
Tax on ordinary activities	(1,697)	-	(1,697)	(1,252)	-	(1,252)
Return attributable to Shareholders	**20,380**	**(18,173)**	**2,207**	**20,097**	**45,714**	**65,811**
Return per share (basic and fully diluted)	**26.02p**	**(23.20)p**	**2.82p**	**23.06p**	**52.46p**	**75.52p**
Weighted average number of shares in issue during the year		**78,338,201**			**87,144,760**	

	2018 £'000	2017 £'000
Dividends paid and proposed		
First interim 2018 - 5.0p (2017: 5.5p)	3,931	4,543
Second interim 2018 - 5.0p (2017: Nil)	3,906	-
Third interim 2018 - 5.0p (2017: Nil)	3,880	-
Final 2018 – 6.2p (2017: 14.5p)	4,786	11,400
Special 2018 – 4.0p (2017: 5.0p)	3,087	3,930
Total 2018 – 25.2p (2017: 25.0p)	**19,590**	**19,873**

* Includes a refund of previously paid expenses

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

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

Balance Sheet
As at 31 October 2018

	£'000	2018 £'000	£'000	2017 £'000
Fixed Assets				
Investments		717,547		801,302
Current Assets				
Debtors	12,733		2,113	
Cash and cash equivalents	83,236		42,936	
	95,969		45,049	
Creditors: liabilities falling due within one year	(13,038)		(1,152)	
Net Current Assets		**82,931**		**43,897**
Total Assets less Current Liabilities		**800,478**		**845,199**
Creditors: liabilities falling due after more than one year				
Long-term borrowings at amortised cost		(83,829)		(83,737)
Provisions for Liabilities				
Pension liability		(1,337)		(1,091)
Net Assets		**715,312**		**760,371**
Capital and Reserves				
Called-up share capital		19,296		19,867
Share premium account		39,922		39,922
Other reserves:				
Capital redemption reserve		51,565		50,994
Capital reserve		555,308		593,484
Revenue reserve		49,221		56,104
Shareholders' Funds		**715,312**		**760,371**
Net Asset Value per share with borrowings at amortised cost (basic and fully diluted)		**926.8p**		**956.8p**
Number of shares in issue at year end		**77,184,578**		**79,468,458**

Statement of Comprehensive Income
For the year to 31 October 2018

	2018 Revenue £'000	2018 Capital £'000	2018 Total £'000	2017 Revenue £'000	2017 Capital £'000	2017 Total £'000
Return attributable to shareholders	20,380	(18,173)	2,207	20,097	45,714	65,811
Actuarial (losses)/gains relating to pension scheme	(216)	(400)	(616)	1,077	749	1,826
Total comprehensive income for the year	20,164	(18,573)	1,591	21,174	46,463	67,637
Total comprehensive income per share	25.74p	(23.71)p	2.03p	24.30p	53.31p	77.61p

Statement of Changes in Equity
For the year to 31 October 2018

	2018 £'000	2017 £'000
Opening balance	760,371	849,017
Total comprehensive income	1,591	67,637
Dividend payments	(27,047)	(21,095)
Aviva share buyback	-	(90,255)
Regular share buybacks	(19,603)	(44,933)
Closing balance	**715,312**	**760,371**

Cash Flow Statement
For the year to 31 October 2018

	2018 £'000	2017 £'000
Operating activities		
Net revenue before finance costs and taxation	23,809	23,823
Expenses charged to capital	(1,209)	(1,442)
(Decrease)/increase in accrued income	(72)	226
Increase in other payables	264	47
Increase/(decrease) in other receivables	9	(3)
Adjustment for pension funding	(370)	(355)
Tax on investment income	(1,809)	(1,327)
Cash flows from operating activities	**20,622**	**20,969**
Investing activities		
Purchases of investments	**(105,183)**	**(131,714)**
Disposals of investments	**175,216**	**273,474**
Cash flows from investing activities	**70,033**	**141,760**
Cash flows before financing activities	**90,655**	**162,729**
Financing activities		
Dividends paid	(27,047)	(21,095)
Aviva share buyback	-	(90,255)
Regular share buybacks	(18,451)	(44,490)
Interest paid	(4,857)	(4,857)
Cash flows from financing activities	**(50,355)**	**(160,697)**
Net movement in cash and cash equivalents	**40,300**	**2,032**
Cash and cash equivalents at the beginning of year	**42,936**	**40,904**
Cash and cash equivalents at the end of year *	**83,236**	**42,936**

* Cash and cash equivalents represent cash at bank and short-term money market deposits repayable on demand.

Responsibility Statement

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

Company law requires the Directors to prepare Financial Statements for each financial year. Under that law the Directors have elected to prepare the Financial Statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland". Under company law the Directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these Financial Statements, the Directors are required to:

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

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

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

The Board of Directors confirms that to the best of its knowledge:

a) the Financial Statements, prepared in accordance with United Kingdom Generally Accepted Accounting Practice, give a true and fair view of the assets, liabilities, financial position and return of the Company;
b) the Strategic Report includes a fair review of the development and performance of the business and the position of the Company together with a description of the principal risks and uncertainties the Company faces; and
c) the Annual Report and Financial Statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position, performance, business model and strategy.

The Responsibility Statement was approved by the Board of Directors and signed on its behalf by:

James Will
Chairman
7 December 2018

Notes

1. Basis of accounting

The Financial Statements have been prepared in accordance with Financial Reporting Standard 102 and with the AIC 's Statement of Recommended Practice "Financial Statements of Investment Trust Companies and Venture Capital Trusts" (SORP). They are also prepared on a going concern basis under the historical cost convention, modified to include the revaluation of investments at fair value. The functional and presentation currency is pounds sterling, which is the currency of the environment in which the Company operates.

2. Return per ordinary share

The revenue return per share is calculated on net revenue on ordinary activities after taxation for the year of £20,380,000 (2017: £20,097,000) and on 78,338,201 (2017: 87,144,760) shares, being the weighted average number of shares in issue during the year.

The capital return per share is calculated on net capital loss for the year of £18,173,000 (2017: net capital gain of £45,714,000) and on 78,338,201 (2017: 87,144,760) shares, being the weighted average number of shares in issue during the year.

The total return per share is calculated on total return for the year of £2,207,000 (2017: £65,811,000) and on 78,338,201 (2017: 87,144,760) shares, being the weighted average number of shares in issue during the year.

3. Net asset value per share

The net asset value per share with borrowings at amortised cost is based on net assets of £715,312,000 (2017: £760,371,000) and on 77,184,578 (2017: 79,468,458) shares, being the number of shares in issue at the year end.

4. Dividends

A final dividend in respect of the year ended 31 October 2018 of 6.2p (2017 - 14.5p) per share will be paid on 15 February 2019 to shareholders on the register on 18 January 2019.

A special dividend in respect of the year ended 31 October 2018 of 4.0p (2017 - 5.0p) per share will be paid on 15 February 2019 to shareholders on the register on 18 January 2019.

5. Related parties

The Directors of the Company receive fees for their services.

The financial information set out above does not constitute the Company's statutory Financial Statements for the year ended 31 October 2018 but is derived from those Financial Statements. Statutory Financial Statements for the year ended 31 October 2018 will be delivered to the Registrar of Companies in due course. The Auditor has reported on those Financial Statements; its report was (i) unqualified, (ii) did not include a reference to any matters to which the Auditor drew attention by way of emphasis without qualifying the report and (iii) did not contain a statement under Section 498 (2) or (3) of the Companies Act 2006. The text of the Auditor's Report will be found in the Company's full Annual Report and Financial Statements on the Company's website: **www.thescottish.co.uk** Copies may also be obtained from the Company Secretary: Maitland Administration Services (Scotland) Limited, 20 Forth Street, Edinburgh EH1 3LH.

Risk management policies and procedures

As an investment trust, the Company invests in equities and other investments for the long-term so as to secure its investment objective stated below (note f). In pursuing its investment objective, the Company is exposed to a variety of risks that could result in a reduction in the Company's net assets and a reduction in the profits available for dividend.

The main risks include investment and market price risk (comprising foreign currency risk and interest rate risk), liquidity risk and credit risk. The Directors' approach to the management of these risks is set out below. The Directors of the Company and of S.I.T. Savings Limited coordinate the Company's risk management.

The Company's policies and processes for managing the risks, and the methods used to measure the risks, which are set out below, have not changed from those applied in the previous year.

a. Investment and market price risk

The holding of securities and investing activities involve certain inherent risks, principally in relation to market risk. A contrarian investment approach is a distinctive style that may deviate from comparator indices and peer group performance over discrete periods. Whilst performance is compared against major global and UK indices, the composition of indices has no influence on investment decisions or the construction of the portfolio. As a result, it is expected that the Company's investment portfolio and performance may deviate from the comparator indices. Events may occur which affect the value of investments. From time to time, the Company may wish to use derivatives in order to protect against a specific risk or to facilitate a change in investment strategy such as the movement of funds from one area to another. No such transaction may take place without the prior authorisation of the Board.

Management of the risk

Company performance is monitored at each Board meeting, including investment performance. The Company holds a portfolio which is well diversified across industrial and geographical areas to help minimise these risks. The contrarian investment approach is explained in our shareholder communications and through meetings with media and the investor community. The levels of gearing and gross gearing are monitored closely by the Board and the Manager. The Board currently limits gearing to 20%. While gearing will be employed in a typical range of 0% to 20%, the Company retains the ability to lower equity exposure to a net cash position if deemed appropriate.

b. Foreign currency risk

Approximately 73% of the Company's assets are invested overseas which gives rise to a currency risk. From time to time, specific hedging transactions may be undertaken. The Company's overseas income is subject to currency movements.

Management of the risk

Management monitors the Company's exposure to foreign currencies on a daily basis, and reports to the Board at regular intervals. Management measures the risk to the Company of the foreign currency exposure by considering the effect on the Company's net asset value and income of a movement in the rates of exchange to which the Company's assets, liabilities, income and expenses are exposed.

Foreign currency borrowings and forward currency contracts may be used to limit the Company's exposure to anticipated future changes in exchange rates which might otherwise adversely affect the value of the portfolio of investments or the income received from them. These borrowings and contracts are limited to currencies and amounts commensurate with the asset exposure to those currencies.

Income denominated in foreign currencies is converted to sterling on receipt. The Company does not use financial instruments to mitigate the currency exposure in the period between the time that income is receivable and its receipt.

c. Interest rate risk

The Company finances its operations through a combination of investment realisations, retained revenue reserves, debenture stocks and secured bonds. All debenture stocks and secured bonds are at fixed rates.

Management of the risk

The Company finances part of its activities through borrowings at levels which have been approved and are monitored by the Board.

d. Liquidity risk

Almost all of the Company's assets comprise listed securities which represent a ready source of funds.

Management of the risk

Liquidity risk is not as significant as the other risks as most of the Company's assets are investments in quoted equities and are readily realisable. Management reviews the liquidity of the portfolio when making investment decisions.

e. Credit risk

The failure of the counterparty to a transaction to discharge its obligations under that transaction could result in the Company suffering a loss.

Management of the risk

This risk is managed as follows:

- by dealing only with brokers and banks which have been approved by the Audit Committee and which have credit ratings assigned by international credit rating agencies; and
- by setting limits on the maximum exposure to any one counterparty at any time, which are reviewed semi-annually at meetings of the Audit Committee.

f. Capital management policies and procedures

The Company carries on its business as a global growth investment trust. Its objective is to provide investors, over the longer term, with above-average returns through a diversified portfolio of international equities and to achieve dividend growth ahead of UK inflation.

The levels of gearing and gross gearing are monitored closely by the Board and management. The Board currently limits gearing to 20%. While gearing will be employed in a typical range of 0% to 20%, the Company retains the ability to lower equity exposure to a net cash position if deemed appropriate.

The Board, with the assistance of management, monitors and reviews the structure of the Company's capital on an ongoing basis. This review includes the planned level of gearing which will take into account management's view on the market, the need to buy back shares for cancellation and the level of dividends.

The Company's policies and processes for managing capital are unchanged from the previous year.