

ABERDEEN AUSTRALIA EQUITY FUND INC
Form N-CSR
January 04, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM N-CSR

CERTIFIED SHAREHOLDER REPORT OF REGISTERED MANAGEMENT

INVESTMENT COMPANIES

| | |
|---|---|
| Investment Company Act file number: | 811-04438 |
| Exact name of registrant as specified in charter: | Aberdeen Australia Equity Fund, Inc. |
| Address of principal executive offices: | 800 Scudders Mill Road, Plainsboro, New Jersey 08536 |
| Name and address of agent for service: | Mr Beverly Hendry, 300 S.E. 2 nd Street, Suite #820, Fort Lauderdale, Florida 33301 |
| Registrant's telephone number, including area code: | 212-968-8800 |
| Date of fiscal year end: | 10/31/04 |
| Date of reporting period: | 10/31/04 |

Item 1 Reports to Stockholders [INSERT REPORT]

Annual Report

October 31, 2004

Letter to Shareholders

December 20, 2004

Dear Shareholder,

We present this Annual Report which covers the activities of Aberdeen Australia Equity Fund, Inc. (the Fund) for the year ended October 31, 2004. The Fund's principal investment objective is long-term capital appreciation through investment primarily in equity securities of Australian companies listed on The Australian Stock Exchange. The Fund's secondary investment objective is current income.

Change of Fund Address

On November 1, 2004, the Fund's address was changed to 800 Scudders Mill Road, Plainsboro, New Jersey 08536.

New Fund Administrator

Effective November 1, 2004, Aberdeen Asset Management Inc. became the Fund's administrator.

Managed Distribution Policy

The Fund has a managed distribution policy of paying quarterly distributions at an annual rate, set once a year, that is a percentage of the rolling average of the Fund's prior four quarter-end net asset values. The Board of Directors has determined the initial rolling distribution rate to be 10%. This policy will be subject to regular review by the Fund's Board of Directors. The distributions will be made from current income, supplemented by realized capital gains and, to the extent necessary, paid-in capital.

On December 20, 2004, the Board of Directors declared a quarterly distribution of 25 cents per share, payable on January 14, 2005 to all shareholders of record as of December 31, 2004.

Net Asset Value Performance

For the twelve months ended October 31, 2004, the Fund's total return based on NAV was 23.2% after expenses (assuming reinvestment of distributions) compared with 26.9%, in U.S. dollar terms, for the S&P/ASX 200 Accumulation Index.

Share Price Performance

The Fund's share price rose 22.0% over the year, from \$8.40 on October 31, 2003 to \$10.25 on October 31, 2004. The Fund's share price on October 31, 2004 represented a discount of 3.7% to the NAV per share of \$10.64 on that date, compared with a discount of 10.4% to the NAV per share of \$9.38 on October 31, 2003. At the date of this letter, the share price was \$11.30, representing a discount of 1.8% to the NAV per

share of \$11.51.

Aberdeen Australia Equity Fund, Inc.

Letter to Shareholders (continued)

Portfolio Holdings Disclosure

The Fund files its complete schedule of portfolio holdings with the SEC for the first and third quarters of each fiscal year on Form N-Q. The Fund's Forms N-Q are available on the SEC's website at <http://www.sec.gov> and may be reviewed and copied at the SEC's Public Reference Room in Washington D.C. Information about the operation of the Public Reference Room may be obtained by calling 1-800-SEC-0330. The Fund's schedule of portfolio holdings are part of the fund's quarterly reports to shareholders, which are available on the Fund's website or upon request and without charge by calling Investor Relations toll-free at 1-866-839-5205.

Proxy Voting

A description of the policies and procedures that the Fund uses to determine how to vote proxies relating to portfolio securities, and information regarding how the Fund voted proxies relating to portfolio securities during the twelve months ended June 30, 2004, is available: (i) upon request and without charge by calling Investor Relations toll-free at 1-866-839-5205; and (ii) on the SEC's website at <http://www.sec.gov>.

For information about the Fund, including a market review and outlook, weekly updates of share prices, NAV and details of recent distributions, please contact Aberdeen Asset Management Inc. by:

Calling toll free on 1-866-839-5205 or 1-954-767-9900 in the United States,

E-mailing to InvestorRelations@aberdeen-asset.com, or

Visiting the website at www.aberdeen-asset.us.

For information about the Aberdeen Group, visit the Aberdeen website at www.aberdeen-asset.com.

Yours sincerely,

Martin Gilbert

President

All amounts are U.S. dollars unless otherwise stated.

Aberdeen Australia Equity Fund, Inc.

Your Board's policy is to provide investors with a stable distribution rate. Each quarterly distribution will be paid out of current income, supplemented by realized capital gains and, to the extent necessary, paid-in capital.

The Fund is subject to U.S. corporate, tax and securities laws. Under U.S. tax accounting rules, the amount of distributable income for each fiscal period depends on the actual exchange rates during the entire year between the U.S. dollar and the currencies in which Fund assets are denominated and on the aggregate gains and losses realized by the Fund during the entire year.

Therefore, the exact amount of distributable income for each fiscal year can only be determined as of the end of the Fund's fiscal year, October 31. However, under the U.S. Investment Company Act of 1940, the Fund is required to indicate the source of each distribution to shareholders. This estimated distribution composition may vary from quarter to quarter because it may be materially impacted by future realized gains and losses on securities and fluctuations in the value of the currencies in which Fund assets are denominated.

The distributions for the fiscal year ended October 31, 2004 were comprised of 39% net investment income, 47% realized capital gains and 14% return of paid-in capital.

In January 2005, a Form 1099 DIV will be sent to shareholders, which will state the amount and composition of distributions and provide information with respect to their appropriate tax treatment for the 2004 calendar year.

Aberdeen Australia Equity Fund, Inc.

Dividend Reinvestment and Cash Purchase Plan

We invite you to participate in the Fund's Dividend Reinvestment and Cash Purchase Plan (the "Plan"), which allows you to automatically reinvest your distributions in shares of the Fund's common stock at favorable commission rates. Distributions made under the Plan are taxable to the same extent as are cash distributions. The Plan also enables you to make additional cash investments in shares of at least \$100, with a maximum of \$10,000 per month, with an aggregate annual limit of \$120,000. Under this arrangement, the Plan Agent will purchase shares for you on the American or Pacific Stock Exchanges or otherwise on the open market on or before the 15th day of each month.

Effective July 26, 2004, The Bank of New York became the Plan Agent, replacing EquiServe Trust Company, N.A. as Plan Agent. As a result of this transfer of services, certain fees associated with the Plan may have changed. Fees payable by Plan participants are more fully described under the heading "Other Information (Unaudited)" following the notes to the financial statements included in this report.

As a Participant in the Plan, you will have the convenience of:

Automatic reinvestment - the Plan Agent will automatically reinvest your distributions, allowing you to gradually grow your holdings in the Fund;

Lower cost - shares are purchased on your behalf under the Plan at low brokerage rates. Brokerage on share purchases is currently 2 cents per share;

Convenience - the Plan Agent will hold your shares in non-certificated form and will provide a detailed plan account statement of your holdings at the end of each distribution period.

To request a brochure containing information on the Plan, together with an enrollment form, please contact the Plan Agent, The Bank of New York, Shareholder Relations Department, P.O. Box 11258, Church Street Station, New York, NY 10286 or call toll free on 1-800-432-8224.

Aberdeen Australia Equity Fund, Inc.

Report of the Investment Manager

Portfolio Composition

The following chart summarizes the composition of the Fund's portfolio, in industry classification standard sectors, expressed as a percentage of net assets. An industry sector can include more than one industry group. On October 31, 2004, the Fund held 97.2% of its net assets in equities and 2.8% in other assets in excess of liabilities.

Aberdeen Australia Equity Fund, Inc.

Selected Equity Holdings

The following were the Fund's top ten holdings at October 31, 2004.

| <u>Name of Security</u> | <u>Percentage of Net Assets</u> |
|---|---------------------------------|
| Australia & New Zealand Banking Group Limited | 8.2% |
| QBE Insurance Group Limited | 7.5% |
| Westpac Banking Corporation Limited | 6.9% |
| BHP Billiton Limited | 5.9% |
| Telecom Corporation of New Zealand Limited | 5.7% |
| Foster's Group Limited | 5.7% |
| TABCORP Holdings Limited | 4.6% |
| Leighton Holdings Limited | 4.6% |
| Woolworths Limited | 4.5% |
| Rio Tinto Limited | 4.3% |

The Fund may invest between 25% and 35% of its total assets in the securities of any one industry group if, at the time of investment, that industry group represents 20% or more of the S&P/ASX 200 Accumulation Index. As of October 31, 2004, the Fund did not have more than 25% of its assets invested in any industry group.

An industry classification standard sector, as referred to on the previous page, can include more than one industry group.

Aberdeen Asset Management Asia Limited, December 2004.

Aberdeen Australia Equity Fund, Inc.

Portfolio of Investments

October 31, 2004

| Shares | Description | Value (US\$) |
|--|---|-------------------|
| LONG-TERM INVESTMENTS 97.2% | | |
| Common Stocks 97.2% | | |
| Consumer Discretionary 12.5% | | |
| 1,360,000 | APN News & Media Corporation Limited | \$ 4,845,613 |
| 494,000 | Billabong International Limited | 3,874,429 |
| 1,906,000 | Pacifica Group Limited | 5,239,166 |
| 740,000 | TABCORP Holdings Limited | 8,291,143 |
| | | 22,250,351 |
| Consumer Staples 15.8% | | |
| 2,680,000 | Foster s Group Limited | 10,109,219 |
| 811,000 | Lion Nathan Limited | 4,773,517 |
| 1,390,000 | McGuigan Simeon Wines Limited | 5,295,127 |
| 797,000 | Woolworths Limited | 7,965,369 |
| | | 28,143,232 |
| Energy 1.5% | | |
| 188,000 | Woodside Petroleum Limited | 2,734,105 |
| Financials 34.2% | | |
| 960,000 | Australia & New Zealand Banking Group Limited | 14,628,266 |
| 294,000 | Australian Stock Exchange Limited | 4,064,856 |
| 125,632 | Bendigo Bank Limited | 943,099 |
| 238,000 | Commonwealth Bank of Australia | 5,706,547 |
| 187,000 | National Australia Bank Limited | 3,948,743 |
| 1,303,000 | QBE Insurance Group Limited* | 13,363,075 |
| 470,000 | Suncorp-Metway Limited | 6,010,257 |
| 873,000 | Westpac Banking Corporation Limited | 12,311,406 |
| | | 60,976,249 |
| Shares | | |
| Industrials 6.1% | | |
| 981,000 | Leighton Holdings Limited* | \$ 8,192,232 |
| 1,089,000 | Qantas Airway Limited | 2,700,582 |
| | | 10,892,814 |
| Materials 10.3% | | |
| 1,026,000 | BHP Billiton Limited | 10,614,232 |
| 283,000 | Rio Tinto Limited | 7,736,757 |
| | | 18,350,989 |
| Property 4.2% | | |
| 675,999 | Westfield Group Limited | 7,574,060 |
| Telecommunication Services 9.5% | | |

Edgar Filing: ABERDEEN AUSTRALIA EQUITY FUND INC - Form N-CSR

| | | | |
|---|-----------|--|----------------------|
| | 2,580,000 | Telecom Corporation of New Zealand Limited | 10,194,521 |
| | 1,932,000 | Telstra Corporation Limited | 6,739,310 |
| | | | 16,933,831 |
| Utilities 3.1% | | | |
| | 506,000 | Australian Gas Light Company Limited | 4,951,232 |
| | 381,446 | GasNet Australia Group | 652,469 |
| | | | 5,603,701 |
| Total long-term investments (cost \$113,337,085) | | | 173,459,332 |
| Total Investments 97.2% (cost \$113,337,085) | | | 173,459,332 |
| Other assets in excess of liabilities 2.8% | | | 5,091,303 |
| Net assets 100% | | | \$178,550,635 |

* Portion of security is on loan, see Note 3.

See Notes to Financial Statements.

Aberdeen Australia Equity Fund, Inc.

Statement of Assets and Liabilities

October 31, 2004

| | |
|---|-----------------------|
| Assets | |
| Investments, at value (including \$449,476 of securities on loan) (cost \$113,337,085) (Note 3) | \$ 173,459,332 |
| Foreign currency, at value (cost \$4,808,806) | 4,962,732 |
| Dividends and interest receivable | 216,679 |
| Receivables for investments sold | 115,659 |
| Other assets | 139,334 |
| | <hr/> |
| Total assets | 178,893,736 |
| | <hr/> |
| Liabilities | |
| Accrued expenses and other liabilities | 325,830 |
| Payable to custodian | 17,271 |
| | <hr/> |
| Total liabilities | 343,101 |
| | <hr/> |
| Net Assets | \$ 178,550,635 |
| | <hr/> |
| Net assets were comprised of: | |
| Common stock, \$.01 par value | \$ 167,773 |
| Paid-in capital in excess of par | 134,082,419 |
| | <hr/> |
| | 134,250,192 |
| Distributions in excess of net investment income | (1,476) |
| Accumulated net realized loss on investments | (53,362) |
| Net unrealized appreciation on investments | 36,442,623 |
| Accumulated net realized foreign exchange losses | (15,922,772) |
| Net unrealized foreign exchange gains | 23,835,430 |
| | <hr/> |
| Net assets | \$ 178,550,635 |
| | <hr/> |
| Net asset value per share: (\$178,550,635 ÷ 16,777,298 shares of common stock issued and outstanding) | \$10.64 |
| | <hr/> |

See Notes to Financial Statements.

Aberdeen Australia Equity Fund, Inc.

Statement of Operations

Year Ended October 31, 2004

| | |
|---|----------------------|
| Net Investment Income | |
| Income | |
| Dividends (net of foreign withholding taxes of \$259,441) | \$ 7,343,711 |
| Interest | 276,203 |
| Income from securities loaned, net | 25,838 |
| | <u>7,645,752</u> |
| Total income | |
| Expenses | |
| Investment management fee | 1,468,789 |
| Legal fees and expenses | 437,000 |
| Directors' fees and expenses | 215,000 |
| Insurance expense | 212,000 |
| Custodian's fees and expenses | 132,000 |
| Reports to shareholders | 130,000 |
| Administration fee | 83,367 |
| Independent auditors' fees and expenses | 83,000 |
| Investor relations fees and expenses | 77,000 |
| Transfer agent's fees and expenses | 43,000 |
| Litigation Settlement (Note 7) | 8,100 |
| Miscellaneous | 13,384 |
| | <u>2,902,640</u> |
| Total operating expenses | 2,902,640 |
| | <u>4,743,112</u> |
| Net investment income | |
| Realized and Unrealized Gains (Losses) on Investments and Foreign Currencies | |
| Net realized gain on investment transactions | 5,906,261 |
| Net realized foreign exchange gains | 7,443,611 |
| | <u>13,349,872</u> |
| | <u>16,279,442</u> |
| Net change in unrealized appreciation on investments | 16,279,442 |
| Net change in unrealized foreign exchange losses | (154,910) |
| | <u>16,124,532</u> |
| | <u>29,474,404</u> |
| Net gain on investments and foreign currencies | 29,474,404 |
| | <u>\$ 34,217,516</u> |
| Net Increase In Net Assets Resulting From Operations | |

See Notes to Financial Statements.

Aberdeen Australia Equity Fund, Inc.

Statement of Changes in Net Assets

| | Year Ended October 31, | |
|---|------------------------|-------------------|
| | 2004 | 2003 |
| Increase in Net Assets | | |
| Operations | | |
| Net investment income | \$ 4,743,112 | \$ 2,135,073 |
| Net realized gains on investment transactions | 5,906,261 | 646,739 |
| Net realized foreign exchange gains | 7,443,611 | 6,831,734 |
| Net increase in unrealized appreciation on investments | 16,279,442 | 12,891,635 |
| Net change in unrealized foreign exchange gains (losses) | (154,910) | 22,964,386 |
| Net increase in Net Assets resulting from operations | 34,217,516 | 45,469,567 |
| Dividends to shareholders from net investment income | (5,068,817) | (1,677,682) |
| Distributions to shareholders from long-term capital gains | (6,088,832) | (1,174,365) |
| Tax return of capital | (1,928,603) | |
| Cost of Fund shares reacquired in repurchase program (0 and 116,200 shares, respectively) (Note 5) | | (687,920) |
| Total increase | 21,131,264 | 41,929,600 |
| Net Assets | | |
| Beginning of year | 157,419,371 | 115,489,771 |
| End of year(a) | \$ 178,550,635 | \$ 157,419,371 |
| (a) Includes distributions in excess of net investment income and undistributed net investment income of: | \$ (1,476) | \$ 307,900 |

See Notes to Financial Statements.

Aberdeen Australia Equity Fund, Inc.

Notes to Financial Statements

Aberdeen Australia Equity Fund, Inc. (the Fund) is a closed-end, non-diversified management investment company incorporated in Maryland on September 30, 1985. The Fund's principal investment objective is long-term capital appreciation through investment primarily in equity securities of Australian companies listed on The Australian Stock Exchange. The Fund's secondary investment objective is current income. In order to comply with a rule adopted by the Securities and Exchange Commission under the Investment Company Act of 1940 regarding fund names, the Board of Directors has adopted an investment policy that, for as long as the name of the Fund remains Aberdeen Australia Equity Fund, Inc., it shall be the policy of the Fund normally to invest at least 80% of its net assets plus the amount of any borrowings for investment purposes, in equity securities, consisting of common stock, preferred stock and convertible stock, listed on The Australian Stock Exchange. This 80% investment policy is a non-fundamental policy of the Fund and may be changed by the Board of Directors upon 60 days prior written notice to shareholders.

Note 1. Accounting Policies

The following is a summary of significant accounting policies followed by the Fund in the preparation of its financial statements.

Basis of Presentation:

The financial statements of the Fund are prepared in accordance with accounting principles generally accepted in the United States of America, using the United States dollar as both the functional and reporting currency. However, the Australian dollar is the functional currency for Federal tax purposes (see Taxes below).

Securities Valuation:

The Fund's Board of Directors has adopted Pricing and Valuation Procedures (the Procedures) to be used in determining the value of the assets held by the Fund. In accordance with the Procedures, investments are stated at value. Investments for which market quotations are readily available are valued at the last trade price on the date of determination as obtained from a pricing source. If no such trade price is available, such investments are valued at the quoted bid price or the mean between the quoted bid and asked price on the date of determination as obtained from a pricing source.

Short-term securities which mature in more than 60 days are valued at current market quotations. Short-term securities which mature in 60 days or less are valued at amortized cost, which approximates market value.

Securities for which market quotations are not readily available (including investments which are subject to limitations as to their sale) are to be valued at fair value. As a general rule, whether or not the Fund is required to fair value price an asset is dependent on the ready availability of current market quotes or, even if readily available, the reliability of such quotes. Any assets for which market quotations are not readily available or for which

Aberdeen Australia Equity Fund, Inc.

Notes to Financial Statements (continued)

available prices are not reliable, shall be determined in a manner that most fairly reflects the asset's (or group of assets) fair value (*i.e.*, the amount that the Fund might reasonably expect to receive for the asset upon its current sale) on the valuation date, based on a consideration of all available information.

The Procedures provide that in certain instances, including without limitation, if there is a stale price for a portfolio security, in an emergency situation, or if a significant event occurs after the close of trading of a portfolio security, but before the calculation of the Fund's net asset value, the security may be valued at its fair value.

Repurchase Agreements:

In connection with transactions in repurchase agreements with United States financial institutions, it is the Fund's policy that its custodian or designated subcustodians under triparty repurchase agreements, as the case may be, take possession of the underlying collateral securities, the value of which exceeds the principal amount of the repurchase transaction, including accrued interest. To the extent that any repurchase transaction exceeds one business day, the value of the collateral is marked-to-market on a daily basis to ensure the adequacy of the collateral. If the seller defaults and the value of the collateral declines or if bankruptcy proceedings are commenced with respect to the seller of the security, realization of the collateral by the Fund may be delayed or limited.

Foreign Currency Translation:

Australian dollar (A\$) amounts are translated into United States dollars (US\$) on the following basis:

(i) market value of investment securities, other assets and liabilities at the exchange rates at the end of the reporting period; and

(ii) purchases and sales of investment securities, income and expenses at the rate of exchange prevailing on the respective dates of such transactions.

The Fund isolates that portion of the results of operations arising as a result of changes in the foreign exchange rates from the fluctuations arising from changes in the market prices of securities held at fiscal year end. Similarly, the Fund isolates the effect of changes in foreign exchange rates from the fluctuations arising from changes in the market prices of portfolio securities sold during the reporting period.

Net realized and unrealized foreign exchange gains (losses) include realized foreign exchange gains (losses) from sales and maturities of portfolio securities, sales of foreign currencies, currency gains (losses) realized between the trade and settlement dates on securities transactions, the difference between the amounts of dividends, interest and foreign withholding taxes recorded on the Fund's books and the US\$ equivalent amounts actually received or paid and changes in unrealized foreign exchange gains (losses) in the value of portfolio securities and other assets and liabilities arising as a result of changes in the

Aberdeen Australia Equity Fund, Inc.

Notes to Financial Statements (continued)

exchange rate. Accumulated net realized and unrealized foreign exchange gains (losses) shown in the composition of net assets at October 31, 2004 represent foreign exchange gains (losses) for book purposes that may not have been recognized for tax purposes.

Foreign security and currency transactions may involve certain considerations and risks not typically associated with those of domestic origin, including unanticipated movements in the value of the foreign currency relative to the US\$.

The exchange rate at October 31, 2004 was US\$0.75 to A\$1.00.

Securities Transactions and Net Investment Income:

Securities transactions are recorded on the trade date. Realized and unrealized gains (losses) from security and currency transactions are calculated on the identified cost basis. Dividend income is recorded on the ex-dividend date and interest income is recorded on an accrual basis. Expenses are recorded on an accrual basis.

Dividends and Distributions:

The Fund has a managed distribution policy of paying quarterly distributions at an annual rate, set once a year, that is a percentage of the rolling average of the Fund's prior four quarter-end net asset values. The Board of Directors has determined the initial rolling distribution rate to be 10%. This policy will be subject to regular review by the Fund's Board of Directors. The distributions will be made from current income, supplemented by realized capital gains and, to the extent necessary, paid-in capital.

On an annual basis, the Fund intends to distribute its net realized capital gains, if any, by way of a final distribution to be declared during the calendar quarter ending December 31. Dividends and distributions to shareholders are recorded on the ex-dividend date.

Income distributions and capital and currency gains distributions are determined in accordance with income tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences are primarily due to differing treatments for foreign currencies.

Taxes:

For federal income and excise tax purposes, substantially all of the Fund's transactions are accounted for using the Australian dollar as the functional currency. Accordingly, only realized currency gains (losses) resulting from the repatriation of Australian dollars into United States dollars are recognized for U.S. tax purposes.

It is the Fund's policy to continue to meet the requirements of the United States Internal Revenue Code applicable to regulated investment companies and to distribute substantially all of its taxable net income and capital gains, if any, to shareholders. Therefore, no provision for

Edgar Filing: ABERDEEN AUSTRALIA EQUITY FUND INC - Form N-CSR

United States income taxes is required. Australia imposes a withholding tax of 15% on certain dividends and 10% on certain interest.

Aberdeen Australia Equity Fund, Inc.

Notes to Financial Statements (continued)

Securities Lending:

The Fund's investment policies permit the Fund to lend to banks and broker-dealers, portfolio securities with an aggregate market value of up to one-third of the Fund's total assets when it deems advisable. Pursuant to a securities lending agreement (Agreement) between the Fund and State Street Bank and Trust Company (State Street), any loans made under the Agreement must be secured by collateral (consisting of any combination of U.S. currency and securities issued or guaranteed by the U.S. government or its agencies, or irrevocable bank letters of credit) in an amount at least equal, on a daily marked-to-market basis, to 100% of the current market value of the securities loaned.

The Agreement also provides that the Fund may terminate the loans at any time and demand the return of the securities, and that the Fund will continue to receive all interest, dividends and other distributions obtained on any of the loaned securities and will continue to have voting rights with respect to the securities.

In the event the Fund lends its portfolio securities, the Fund may be exposed to counterparty risk, which may result in the delay in recovery of the loaned securities or possible loss of right in the collateral should the borrower become insolvent.

Use of Estimates:

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from those estimates.

Note 2. Agreements

In December 2003, the Fund's Board of Directors approved the transfer by Aberdeen Asset Managers (C.I.) Limited (AAMCIL) to Aberdeen Asset Management Asia Limited (AAMAL) of the rights and obligations of AAMCIL under the management agreement and the advisory agreement with the Fund. Effective March 8, 2004, AAMAL became the investment manager of the Fund (the Investment Manager). Aberdeen Asset Management Limited (the Investment Adviser) serves as the investment adviser to the Fund pursuant to an advisory agreement. The Investment Manager and the Investment Adviser are direct or indirect wholly-owned subsidiaries, respectively, of Aberdeen Asset Management PLC.

The Investment Manager makes investment decisions on behalf of the Fund on the basis of recommendations and information furnished to it by the Investment Adviser, including the selection of and the placement of orders with brokers and dealers to execute portfolio transactions on behalf of the Fund.

The management agreement provides the Investment Manager with a fee, computed weekly and payable monthly, at the following annual rates: 1.10% of the Fund's average weekly Managed Assets up to \$50 million, 0.90% of Managed Assets between \$50 million and \$100 million and 0.70% of Managed Assets in excess of \$100 million. Managed Assets are defined in the management agreement as net assets plus the amount of any borrowings for investment purposes.

Aberdeen Australia Equity Fund, Inc.

Notes to Financial Statements (continued)

The Investment Manager pays fees to the Investment Adviser for its services rendered. AAMCIL, the Fund's investment manager through March 7, 2004 and AAMAL, the Fund's current investment manager, informed the Fund that it paid \$374,426 to the Investment Adviser during the year ended October 31, 2004.

During the year ended October 31, 2004, Prudential Investments LLC (Prudential) served as administrator to the Fund pursuant to an agreement which provided Prudential with a fee at the annual rate of the greater of \$25,000 or 0.05% of the Fund's average weekly net assets. Effective November 1, 2004, Aberdeen Asset Management Inc. (AAMI), an affiliate of the Fund's Investment Manager and Investment Adviser, became the Fund's administrator, pursuant to an agreement under which AAMI receives a fee at an annual rate equal to 0.04% of the Fund's average weekly net assets.

Under terms of an Investor Relations Services Agreement, AAMI serves as the Fund's investor relations services provider. This agreement provides AAMI with a monthly retainer fee of \$5,000 plus out-of-pocket expenses. During the year ended October 31, 2004, the Fund incurred fees of approximately \$60,000 for the services of AAMI. As of October 31, 2004, \$5,000 was due to AAMI. Investor relations fees and expenses in the Statement of Operations include certain out-of-pocket expenses.

Note 3. Portfolio Securities

Purchases and sales of investment securities, other than short-term investments, for the year ended October 31, 2004 aggregated \$37,279,094 and \$43,360,352, respectively.

As of October 31, 2004, the Fund had securities on loan with an aggregate market value of \$449,476. The Fund received \$507,725 in securities as collateral for securities on loan in accordance with the Fund's securities lending procedures. The collateral consisted of United States Treasury bonds and notes.

Note 4. Distributions and Tax Information

Distributions to shareholders, which are determined in accordance with federal income tax regulations and which may differ from generally accepted accounting principles, are recorded on the ex-dividend date. In order to present undistributed net investment income (loss) and accumulated net realized gains (losses) on the Statement of Assets and Liabilities in a way that more closely represents their tax character, certain adjustments have been made to paid-in capital in excess of par, undistributed net investment income (loss) and accumulated net realized gains (losses) on investments.

For the year ended October 31, 2004, the Fund decreased distributions in excess of net investment income by \$16,329, decreased accumulated net realized loss on investments by \$22,517 and increased accumulated realized foreign exchange losses by \$38,846. Net investment income, net realized gains and net assets were not affected by this change. These differences are primarily due to differing treatments for foreign currencies.

Edgar Filing: ABERDEEN AUSTRALIA EQUITY FUND INC - Form N-CSR

As of October 31, 2004, there were no distributable earnings.

For the year ended October 31, 2004, the tax character of total distributions paid was \$5,068,817 of ordinary income, \$6,088,832 of long-term capital gains and \$1,928,603 of

Aberdeen Australia Equity Fund, Inc.

Notes to Financial Statements (concluded)

return of paid-in capital. For the year ended October 31, 2003, the tax character of total dividends paid was \$1,677,682 of ordinary income and \$1,174,365 of long-term capital gains.

The United States federal income tax basis of the Fund's investments and the net unrealized appreciation as of October 31, 2004 were as follows:

| Tax | | | | Net |
|----------------|---------------|----------------|-----------------------------------|---------------|
| Cost | Appreciation | (Depreciation) | Other Cost Basis Adjustment | Unrealized |
| Basis | Basis | Basis | Basis | Appreciation |
| \$ 137,016,709 | \$ 39,066,612 | \$ (2,623,989) | \$ (53,362) | \$ 36,389,261 |

The difference between book and tax basis is primarily attributable to deferred losses on foreign currency transactions and tax straddles.

Note 5. Capital

There are 20 million shares of \$0.01 par value common stock authorized. At October 31, 2004 there were 16,777,298 shares issued and outstanding.

On March 1, 2001, the Board of Directors approved a stock repurchase program. The stock repurchase program allows the Fund to repurchase up to 10% of its outstanding common stock in the open market during any 12 month period if and when the discount to net asset value is at least 10%. For fiscal years ended October 31, 2004 and October 31, 2003, the Fund repurchased and cancelled under this program 0 and 116,200 shares, respectively.

Based on filings with the Securities and Exchange Commission, on February 26, 2004, Bankgesellschaft Berlin (A.G.) was the beneficial owner of 5,374,949 shares of common stock. This number of shares represented approximately 32% of the outstanding shares of the Fund as of the date of this report.

Note 6. Distributions

The Board of Directors of the Fund declared on December 20, 2004 a quarterly distribution of \$0.25 per share, payable on January 14, 2005 to shareholders of record on December 31, 2004.

Note 7. Litigation

As previously reported to shareholders, Full Value Partners, L.P. (Full Value) filed a purported class action on behalf of the Fund's shareholders, in Newark, New Jersey federal court in March 2003 against both the Fund and its Board of Directors. Full Value sought injunctive relief enjoining (i) the effectuation of a then proposed tender offer, (ii) the enforcement of certain bylaw amendments, and (iii) the overturning of any wrongful election of directors of the Fund. The Fund and its Directors believed, and continue to believe, that the claims were without merit. On March 31, 2004, as part of a settlement agreement, Full Value's claims were dismissed with prejudice. Full Value determined that it would not proceed with the suit if the Fund agreed to pay Full Value's legal fees of approximately \$81,000. The Fund has paid such amount to Full Value, without any admission of liability, in order to avoid additional litigation expense. The Fund has been reimbursed by its insurance carrier for 90% of the amount it paid in this settlement. Thus, the amount of the litigation settlement in the Statement of Operations is \$8,100.

Aberdeen Australia Equity Fund, Inc.

This page intentionally left blank

Financial Highlights

| | Year Ended October 31, 2004 |
|--|--------------------------------|
| PER SHARE OPERATING PERFORMANCE: | |
| Net asset value, beginning of year | \$ 9.38 |
| Net investment income | .28 |
| Net realized and unrealized gains (losses) on investments and foreign currencies | 1.76 |
| Total from investment operations | 2.04 |
| Dividends from net investment income | (.30) |
| Distributions from net capital and currency gains | (.36) |
| Tax return of capital | (.12) |
| Total dividends and distributions | (.78) |
| Capital reduction with respect to issuance of Fund shares Increase resulting from Fund share repurchase | |
| Net asset value, end of year | \$ 10.64 |
| Market price per share, end of year | \$ 10.25 |
| TOTAL INVESTMENT RETURN BASED ON#: | |
| Market value | 32.53% |
| Net asset value | 23.19% |
| RATIOS/SUPPLEMENTAL DATA: | |
| Ratio of expenses to average net assets | 1.75% |
| Ratio of net investment income to average net assets | 2.85% |
| Portfolio turnover rate | 23% |
| Net assets, end of year (000 omitted) | \$ 178,551 |
| Average net assets (000 omitted) | \$ 166,284 |

Total investment return is calculated assuming a purchase of common stock on the first day and a sale on the last day of each period reported. Dividends and distributions are assumed, for purposes of this calculation, to be reinvested at prices obtained under the Fund's dividend reinvestment plan. Total investment return does not reflect brokerage commissions. Less than \$0.005 per share.

NOTE: Contained above is operating performance for a share of common stock outstanding, total investment return, ratios to average net assets and other supplemental data for each of the periods indicated. This information has been determined based upon financial information provided in the financial statements and market value data for the Fund's shares.

See Notes to Financial Statements.

Aberdeen Australia Equity Fund, Inc.

Financial Highlights (concluded)

| Year Ended October 31, | | | | |
|------------------------|---------|---------|---------|--|
| 2003 | 2002 | 2001 | 2000 | |
| \$ 6.84 | \$ 5.97 | \$ 6.86 | \$ 8.78 | |
| .12 | .15 | .12 | .14 | |
| 2.58 | .93 | (.33) | (1.25) | |
| 2.70 | 1.08 | (.21) | (1.11) | |
| (.10) | (.15) | | (.12) | |
| (.07) | (.07) | | (.69) | |
| | | (.68) | | |
| (.17) | (.22) | (.68) | (.81) | |
| .01 | .01 | | | |