

SCUDDER MUNICIPAL INCOME TRUST  
Form N-CSRS  
August 06, 2004

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D. C. 20549

FORM N-CSRS

Investment Company Act file number 811-05655

SCUDDER MUNICIPAL INCOME TRUST

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(Exact Name of Registrant as Specified in Charter)

222 South Riverside Plaza, Chicago, IL 60606

-----  
(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, including Area Code: (617) 295-2663

-----  
Salvatore Schiavone  
Two International Place  
Boston, Massachusetts 02110

-----  
(Name and Address of Agent for Service)

Date of fiscal year end: 11/30

Date of reporting period: 5/31/2004

[Scudder Investments logo]

**Scudder Municipal  
Income Trust**  
**Semiannual Report to  
Shareholders**  
**May 31, 2004**

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Statement

*Investments in funds involve risk. Certain investors' income may be subject to the federal Alternative Minimum Tax (AMT), and state and local taxes may also apply. Shares of closed-end funds frequently trade at a discount to net asset value. The price of the fund's shares is determined by a number of factors, several of which are beyond the control of the fund. Therefore, the fund cannot predict whether its shares will trade at, below or above net asset value.*

*Scudder Investments is part of Deutsche Asset Management, which is the marketing name in the US for the asset management activities of Deutsche Bank AG, Deutsche Investment Management Americas Inc., Deutsche Asset Management Inc., Deutsche Asset Management Investment Services Ltd., Deutsche Bank Trust Company Americas and Scudder Trust Company.*

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*Fund shares are not FDIC-insured and are not deposits or other obligations of, or guaranteed by, any bank. Fund shares involve investment risk, including possible loss of principal.*

### Performance Summary May 31, 2004

Performance is historical, assumes reinvestment of all dividends and capital gains, and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when sold, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please visit [scudder.com](http://scudder.com) for the product's most recent month-end performance.

| Average Annual Total Returns as of 5/31/04        |                       |        |        |        |         |
|---|-----------------------|--------|--------|--------|---------|
| Scudder Municipal Income Trust                    | 6-Month <sup>++</sup> | 1-Year | 3-Year | 5-Year | 10-Year |
| Based on Net Asset Value <sup>(a)</sup>           | -.27%                 | .38%   | 8.24%  | 7.23%  | 7.19%   |
| Based on Market Price                             | -4.36%                | -4.33% | 6.63%  | 4.12%  | 6.25%   |
| Lehman Brothers Municipal Bond Index <sup>+</sup> | -.22%                 | -.03%  | 5.52%  | 5.49%  | 6.33%   |

<sup>++</sup> Total returns shown for periods less than one year are not annualized.

| Net Asset Value and Market Price |               |                |
|----------------------------------|---------------|----------------|
|                                  | As of 5/31/04 | As of 11/30/03 |
| Net Asset Value                  | \$ 12.14      | \$ 12.59       |
| Market Price                     | \$ 11.06      | \$ 11.96       |

| Distribution Information  |          |
|---|----------|
| Six Months:   |          |
| Income Dividends (common shareholders) as of 5/31/04  | \$ .41   |
| May Income Dividend (common shareholders)   | \$ .0675 |
| Current Annualized Distribution Rate (based on Net Asset Value) as of 5/31/04 <sup>++</sup> | 6.67%    |
| Current Annualized Distribution Rate (based on Market Price) as of 5/31/04 <sup>++</sup>    | 7.32%    |
| Tax Equivalent Distribution Rate (based on Net Asset Value) as of 5/31/04 <sup>++</sup>     | 10.26%   |
| Tax Equivalent Distribution Rate (based on Market Price) as of 5/31/04 <sup>++</sup>        | 11.26%   |

<sup>a</sup> Total investment returns reflect changes in net asset value per share during each period and assume that dividends and capital gains distributions, if any, were reinvested. These percentages are not an indication of the performance of a shareholder's investment in the Fund based on market price.

<sup>+</sup> The unmanaged Lehman Brothers Municipal Bond Index is a market-value-weighted measure of municipal bonds issued across the United States. Index issues have a credit rating of at least Baa and a maturity of at least two years. Index returns assume reinvestment of dividends and, unlike Fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.

<sup>++</sup> Current annualized distribution rate is the latest monthly dividend shown as an annualized percentage of net asset value/market price on May 31, 2004. Distribution rate simply measures the level of dividends and is not a complete measure of performance. Tax equivalent distribution rate is based on the Fund's distribution rate and a marginal income tax rate of 35%. Distribution rates are historical and will fluctuate.

### Portfolio Management Review

Philip G. Condon and Eleanor R. Brennan serve as co-lead portfolio managers of Scudder Municipal Income Trust. In the following interview, Scudder's municipal bond team discusses the Trust's performance for the period and the market environment for municipal bonds.

**Q: Will you describe the general market environment during the semiannual period ended May 31, 2004?**

**A:** The semiannual period was somewhat lackluster for municipal bonds. While the broad bond market showed a slight gain, municipal bonds logged a slight decline for the six-month period ended May 31, 2004. The municipal bond market, as measured by the Lehman Brothers Municipal Bond Index, fell -0.22% for the semiannual period. The broad bond market, as measured by the Lehman Brothers Aggregate Bond Index, gained 0.60% for the same period.<sup>1</sup>

<sup>1</sup> The Lehman Brothers Aggregate Bond Index is an unmanaged index representing domestic taxable investment-grade bonds, with index components for government and corporate securities, mortgage pass-through securities and asset-backed securities with average maturities of one year or more.

Municipal bond yields rose over the period, and 10-year municipal bonds slightly underperformed 10-year US Treasury bonds. For the period, 10-year Treasury bond yields moved from 4.33% to 4.66%, a rise of 0.33 percentage points.<sup>2</sup> Ten-year municipal bond yields rose 0.38 percentage points from 3.55% to 3.93%.<sup>3</sup> The municipal bond yield curve between maturities of two years to 30 years flattened. A flattening yield curve means that the difference in yields between longer-term and shorter-term maturities is becoming smaller, and investors generally have less incentive to buy bonds with longer maturities. The following graph shows municipal bond yield changes from the beginning to the end of the period. The yield curve illustrates the relationship among the yields on bonds of the same credit quality but different maturities.

<sup>2</sup> Source: Municipal Market Data

<sup>3</sup> Source: Municipal Market Data

**AAA Municipal bond yield curve (as of 11/28/03 and 5/28/04)**

Source: Municipal Market Data

This chart is not intended to represent the yield of any Scudder fund.

The Federal Reserve Board made no changes to the federal funds rate during the period, but over the course of the period indicated that it was more likely that a rate increase was probable. On the economic front, the economy continued to make headway as reports on manufacturing, housing and economic growth strengthened. Still, in the early months of the period doubts remained as to whether the economy was in a full recovery, as employment figures remained less robust. In the final months of the period, the Fed began to send signals that the economy was in full recovery and inflation was becoming a greater concern, and that "measured" increases in the federal funds rate were more imminent.

**Q: Will you discuss municipal bond supply and demand in the period and its importance in the bond market?**

**A:** Throughout much of 2003, states deluged the market with record levels of new issues, which were brought to market to help make up for revenue shortfalls and refinance old debt at lower rates, which resulted in record supply levels. However, as states completed much of the refinancing and new issuance that they needed, supply became somewhat less abundant toward the final months of 2003. Overall, issuance levels heightened again in 2004, boosted by issuance of \$7.9 billion California Economic Recovery Bonds - the largest municipal bond issuance in history. In addition, demand was solid at the end of 2003, but lessened in the first quarter of 2004.

Supply and demand factors are important because they are one way a bond's price can be driven higher or lower. High demand or low supply can cause a bond's price to rise, while lessened demand or a flood of supply can cause a bond's price to decline. A bond's yield moves in the opposite direction of its price.

**Q: How did Scudder Municipal Income Trust perform for the semiannual period ended May 31, 2004?**

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**A:** Scudder Municipal Income Trust delivered a total return at net asset value of -0.27%. The Trust posted a market value of -4.36%. Its average peer in the Lipper General Municipal Debt Funds category for closed-end funds delivered -0.56% in the period.<sup>4</sup> The Trust's benchmark, the unmanaged Lehman Brothers Municipal Bond Index, posted a -0.22% loss. (Please see page 4 for more complete performance information.)

<sup>4</sup> The Lipper General Municipal Debt Funds category includes closed-end funds that invest in general municipal debt issues in the top-four credit grades.

**Q: How was the Trust positioned, and how did this positioning contribute to its performance for the semiannual period ended May 31, 2004?**

**A:** Throughout the period we positioned the portfolio for a flattening of the yield curve, which began to occur at the end of 2003. In addition, our overall selection of premium callable bonds helped boost returns.<sup>5</sup> Premium callable bonds outperformed noncallable bonds. For the same maturity, premium callable bonds offered similar yields as noncallable bonds, but with a shorter duration.<sup>6</sup> For example, a 20-year premium callable bond would be priced to a 10-year call with a yield equivalent of a 20-year security.

<sup>5</sup> A callable bond can be redeemed by the issuer prior to its maturity.

<sup>6</sup> Duration is a measure of bond price volatility. Duration can be defined as the approximate percentage change in price for a one-percentage-point change in market interest rate levels. A duration of 5, for example, means that if interest rates fall one percentage point, the price of a bond should rise by approximately 5%, and the price should fall by 5% for a one-percentage-point rise in interest rates. Bonds with a shorter duration are typically not as sensitive to interest rate movements as are bonds with a longer duration. They will, therefore, experience less price erosion in a rising-interest-rate environment.

The Trust's results benefited from the use of leverage. Overall interest rates, despite the fluctuations discussed earlier, remained at historical lows. In addition, the municipal bond yield curve, despite flattening somewhat, remained at a historical steep level. As a result, we were able to use outstanding shares to borrow money at attractive rates, which could fund additional investments.

Overall, we believe municipal bond valuations relative to Treasuries and agencies are attractive throughout the yield curve.

*The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.*

### Portfolio Summary May 31, 2004

| Portfolio Composition    | 5/31/04 | 11/30/03 |
|--------------------------|---------|----------|
| Revenue Bonds            | 66%     | 67%      |
| US Government Secured    | 17%     | 15%      |
| General Obligation Bonds | 12%     | 12%      |
| Lease Obligations        | 5%      | 6%       |
|                          | 100%    | 100%     |

| Quality | 5/31/04 | 11/30/03 |
|---------|---------|----------|
| AAA     | 72%     | 72%      |
| AA      | 5%      | 4%       |

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|           |      |      |
|-----------|------|------|
| A         | 9%   | 9%   |
| BBB       | 11%  | 12%  |
| BB        | 2%   | 1%   |
| Not Rated | 1%   | 2%   |
|           | 100% | 100% |

| Interest Rate Sensitivity | 5/31/04   | 11/30/03  |
|---------------------------|-----------|-----------|
| Average Maturity          | 8.4 years | 8.3 years |
| Duration                  | 5.5 years | 5.6 years |

| Top Five State Allocations at May 31, 2004 (42.0% of Investment Portfolio) |     |
|--|-----|
| Texas  | 14% |
| Illinois   | 7%  |
| New Jersey   | 7%  |
| California   | 7%  |
| New York   | 7%  |

Portfolio composition, quality, interest rate sensitivity and top five state allocations are subject to change.

For more complete details about the Fund's investment portfolio, see page 10. A quarterly Fact Sheet is available upon request. Information concerning portfolio holdings of the Fund as of month end is available upon request on the 16th of the following month. Please see the Account Management Resources section for contact information.

**Investment Portfolio as of May 31, 2004 (Unaudited)**

|   | Principal Amount (\$) | Value (\$)        |
|---|-----------------------|-------------------|
| <b>Municipal Investments 155.4%</b>   |                       |                   |
| <b>Alabama 5.3%</b>   |                       |                   |
| Alabama, Port Authority Revenue, Docks Department, AMT, 6.3%, 10/1/2021 (b)   | 8,250,000             | 9,015,270         |
| Camden, AL, Industrial Development Board Revenue, AMT, Series B, 6.375%, 12/1/2024  | 1,000,000             | 1,044,540         |
| Huntsville, AL, Hospital & Healthcare Revenue, Health Care Authority, Series A, 5.75%, 6/1/2031                           | 5,500,000             | 5,607,690         |
| Huntsville, AL, Water & Sewer Revenue, AMT, 5.75%, 10/1/2011 (b)  | 8,560,000             | 9,391,262         |
|   |                       | <b>25,058,762</b> |
| <b>Arizona 1.6%</b>   |                       |                   |
| Arizona, Hospital & Healthcare Revenue, Health Facilities Authority, Catholic Healthcare West, Series A, 6.625%, 7/1/2020 | 7,000,000             | <b>7,617,470</b>  |

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| <b>California 10.2%</b>  |            |                   |
|--|------------|-------------------|
| California, Electric Revenue, Department of Water Resources and Power Supply, Series A, 5.375%, 5/1/2022                                     | 7,350,000  | 7,524,930         |
| California, General Obligation, 5.125%, 4/1/2024   | 4,400,000  | 4,388,824         |
| California, General Obligation, Economic Recovery, Series A, 5.0%, 7/1/2015 (b)  | 8,500,000  | 9,072,390         |
| California, Hospital & Healthcare Revenue, Health Facilities Funding Authority, Adventist Health Systems, Series A, 5.0%, 3/1/2028           | 1,000,000  | 928,430           |
| California, Special Assessment Revenue, Golden State Tobacco Securitization Corp.:   |            |                   |
| Series B, 5.625%, 6/1/2038   | 7,080,000  | 7,037,449         |
| Series 2003-A-1, 6.75%, 6/1/2039   | 11,730,000 | 10,340,934        |
| California, State (REV) Lease, Public Works Board, Department of Corrections, Series C, 5.5%, 6/1/2021                                       | 2,500,000  | 2,569,850         |
| California, State GO, 5.25%, 2/1/2021  | 1,000,000  | 1,021,470         |
| Sacramento County, CA, Airport Revenue, AMT, Series A, 5.9%, 7/1/2024 (b)  | 5,000,000  | 5,325,050         |
|  |            | <b>48,209,327</b> |
| <b>Colorado 8.4%</b>   |            |                   |
| Adams County, CO, Multi-Family Housing Revenue, Oasis Park Apartments Project, Series A, 6.15%, 1/1/2026 (b)                                 | 6,000,000  | 6,194,340         |
| Colorado, Hospital & Healthcare Revenue, Portercare Adventist Health Project, 6.5%, 11/15/2031   | 1,000,000  | 1,078,960         |
| Colorado, Hospital & Healthcare Revenue, Poudre Valley Health Facilities:  |            |                   |
| Series A, 5.5%, 12/1/2017 (b)  | 6,145,000  | 6,537,235         |
| Series A, 6.0%, 12/1/2015 (b)  | 5,705,000  | 6,305,451         |
| Series A, 6.0%, 12/1/2016 (b)  | 2,000,000  | 2,204,460         |
| Colorado, Single Family Housing Revenue, AMT, Series B2, 7.25%, 10/1/2031  | 445,000    | 452,414           |
| Colorado, Transportation/Tolls Revenue, Anticipation Note, Prerefunded, 6.0%, 6/15/2011 (b)  | 10,000,000 | 11,480,500        |
| Denver, CO, Airport Revenue, AMT, Series A, 6.0%, 11/15/2014 (b)   | 5,000,000  | 5,495,000         |
|  |            | <b>39,748,360</b> |
| <b>District of Columbia 10.5%</b>  |            |                   |
| District of Columbia, Core City GO, Series B, 5.5%, 6/1/2011 (b)   | 20,000,000 | 22,242,400        |
| District of Columbia, ETM, Series A, 5.5%, 6/1/2014 (b)  | 640,000    | 700,262           |
| District Columbia, State GO:   |            |                   |
| Series A, 5.25%, 6/1/2027 (b)  | 10,830,000 | 10,950,538        |
| Series A, 5.5%, 6/1/2014 (b)   | 1,860,000  | 2,018,100         |
| Metropolitan Washington, DC, Airport Authority, General Airport Revenue, AMT, Series A, 5.75%, 10/1/2020 (b)                                 | 13,100,000 | 13,481,865        |
|  |            | <b>49,393,165</b> |
| <b>Florida 6.6%</b>  |            |                   |
| Alachua County, FL, Hospital & Healthcare Revenue, Health Facilities Authority, Shands Teaching Hospital, Series A, 1.08%, 12/1/2012 (c) (d) | 700,000    | 700,000           |
| Dade County, FL, Airport Revenue, AMT, Series A, 5.75%, 10/1/2026 (b)  | 13,000,000 | 13,492,310        |
| Dade County, FL, Special Assessment Revenue, Zero Coupon:  |            |                   |
| Series B, Prerefunded, 10/1/2022 (b)   | 7,735,000  | 2,868,834         |
| Series B, Prerefunded, 10/1/2024 (b)   | 16,955,000 | 5,538,690         |
| Hillsborough County, FL, Industrial Development Revenue, University Community Hospital Project, Series A, 5.625%, 8/15/2023                  | 1,000,000  | 953,640           |
| Miami-Dade County, FL, Transportation/Tolls Revenue, Expressway Authority:   |            |                   |
| 6.0%, 7/1/2013 (b)   | 1,665,000  | 1,892,722         |

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|  |            |                   |
|--|------------|-------------------|
| 6.0%, 7/1/2014 (b)   | 1,000,000  | 1,136,770         |
| Orange County, FL, Hospital & Healthcare Revenue, Health Facilities Authority, Orlando Regional Healthcare, 5.75%, 12/1/2032 | 1,000,000  | 1,015,100         |
| Palm Beach County, FL, School District (REV) Lease, Series A, Prerefunded, 5.75%, 8/1/2017 (b)                               | 2,850,000  | 3,248,003         |
|  |            | <b>30,846,069</b> |
| <b>Georgia 0.6%</b>  |            |                   |
| Burke County, GA, Development Authority Pollution Control Revenue, Oglethorpe Power Corp. Project:                           |            |                   |
| Series A, 1.08%, 1/1/2020 (b) (c)  | 1,000,000  | 1,000,000         |
| Series C, 1.08%, 1/1/2018 (b) (c)  | 1,700,000  | 1,700,000         |
|  |            | <b>2,700,000</b>  |
| <b>Hawaii 7.6%</b>   |            |                   |
| Hawaii, Airport Revenue, AMT, Series B, 6.5%, 7/1/2013 (b)   | 8,800,000  | 9,999,176         |
| Hawaii, Electric Revenue, Department of Budget & Finance, AMT:   |            |                   |
| Series D, 6.15%, 1/1/2020 (b)  | 2,195,000  | 2,407,059         |
| Series A, 6.2%, 5/1/2026 (b)   | 13,200,000 | 14,082,948        |
| Hawaii, Port Authority Revenue, AMT:   |            |                   |
| Series A, 6.0%, 7/1/2011 (b)   | 2,950,000  | 3,291,787         |
| Series A, 6.0%, 7/1/2012 (b)   | 3,135,000  | 3,442,198         |
| Hawaii, State GO, Series CT, Prerefunded, 5.75%, 9/1/2014 (b)  | 2,310,000  | 2,612,541         |
|  |            | <b>35,835,709</b> |
| <b>Idaho 0.1%</b>  |            |                   |
| Idaho, Single Family Housing Revenue, AMT, Series C2, 6.9%, 7/1/2025 (b)   | 585,000    | <b>585,164</b>    |
| <b>Illinois 10.8%</b>  |            |                   |
| Chicago, IL, Airport Revenue, O'Hare International Airport, AMT, 5.5%, 1/1/2014 (b)  | 10,000,000 | 10,582,300        |
| Chicago, IL, Core City GO:   |            |                   |
| Series A, Prerefunded, 6.0%, 1/1/2014 (b)  | 2,085,000  | 2,403,505         |
| Series A, Prerefunded, 6.125%, 1/1/2015 (b)  | 2,000,000  | 2,319,200         |
| Series A, 6.125%, 1/1/2016 (b)   | 2,000,000  | 2,257,140         |
| Chicago, IL, Other GO, Neighborhoods Alive 21 Project:   |            |                   |
| Series A, Prerefunded, 6.0%, 1/1/2015 (b)  | 1,000,000  | 1,152,760         |
| Series A, 6.0%, 1/1/2017 (b)   | 1,000,000  | 1,120,930         |
| Illinois, Higher Education Revenue, DePaul University, Educational Facilities Authority:                                     |            |                   |
| 5.625%, Prerefunded, 10/1/2013 (b)   | 2,695,000  | 3,055,294         |
| 5.625%, Prerefunded, 10/1/2015 (b)   | 1,710,000  | 1,938,610         |
| Illinois, Higher Education Revenue, MJH Educational Assistance Authority, Series D, 5.45%, 9/1/2014 (b)                      | 8,000,000  | 8,626,480         |
| Illinois, Hospital & Healthcare Revenue, Adventist Health System, 5.5%, 11/15/2020   | 2,500,000  | 2,534,275         |
| Illinois, Hospital & Healthcare Revenue, Children's Memorial Hospital, Series A, Prerefunded, 5.625%, 8/15/2019 (b)          | 4,000,000  | 4,490,160         |
| Illinois, Pollution Control Revenue, Commonwealth Edison Co. Project, Series D, 6.75%, 3/1/2015 (b)                          | 4,220,000  | 4,445,221         |
| Illinois, Sales & Special Tax Revenue, Metropolitan Pier & Exposition Authority:   |            |                   |
| Series A, ETM, 5.5%, 6/15/2017 (b)   | 1,955,000  | 2,186,316         |
| Series A, 5.5%, 6/15/2017 (b)  | 1,555,000  | 1,716,067         |
| Will County, IL, Industrial Development Revenue, Mobil Oil Refining Corp. Project, AMT, 6.0%, 2/1/2027                       | 2,000,000  | 2,067,840         |



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|   |            |                   |
|---|------------|-------------------|
|   |            | <b>50,896,098</b> |
| <b>Indiana 4.1%</b>   |            |                   |
| Indiana, Hospital & Healthcare Revenue, Health Facilities Authority, 5.5%, 11/1/2031                          | 5,000,000  | 5,018,150         |
| Indianapolis, IN, Electric Revenue, Series A, Prerefunded, 5.875%, 6/1/2024 (b)                               | 14,000,000 | 14,285,460        |
|   |            | <b>19,303,610</b> |
| <b>Kansas 0.6%</b>  |            |                   |
| Overland Park, KS, Industrial Development Revenue, Development Corp., Series A, 7.375%, 1/1/2032              | 3,000,000  | <b>2,994,420</b>  |
| <b>Kentucky 1.3%</b>  |            |                   |
| Kentucky, Hospital & Healthcare Revenue, Economic Development Finance Authority, Norton Healthcare, Inc.:     |            |                   |
| Series A, 6.5%, 10/1/2020   | 2,000,000  | 2,084,360         |
| Series A, 6.625%, 10/1/2028   | 4,000,000  | 4,152,280         |
|   |            | <b>6,236,640</b>  |
| <b>Louisiana 0.5%</b>   |            |                   |
| Louisiana, Electric Revenue, 5.75%, 1/1/2013 (b)  | 2,000,000  | <b>2,270,180</b>  |
| <b>Maine 3.4%</b>   |            |                   |
| Maine, Hospital & Healthcare Revenue:   |            |                   |
| Series D, 5.7%, 7/1/2013 (b)  | 5,000,000  | 5,117,000         |
| Series B, Prerefunded, 7.0%, 7/1/2024 (b)   | 4,320,000  | 4,428,907         |
| Maine, Transportation/Tolls Revenue, 5.0%, 7/1/2017 (b)   | 6,165,000  | 6,354,882         |
|   |            | <b>15,900,789</b> |
| <b>Maryland 2.0%</b>  |            |                   |
| Howard County, MD, Multi-Family Housing Revenue, Braeland Commons Project, Series B, 6.2%, 6/15/2023          | 2,500,000  | 2,530,625         |
| Howard County, MD, Multi-Family Housing Revenue, Eden Commons Project, Series A, 6.2%, 6/15/2023              | 4,250,000  | 4,302,063         |
| Maryland, Hospital & Healthcare Revenue, University of Maryland Medical System, 6.75%, 7/1/2030               | 2,500,000  | 2,814,325         |
|   |            | <b>9,647,013</b>  |
| <b>Massachusetts 3.6%</b>   |            |                   |
| Massachusetts, Airport Revenue, AMT, Series B, 5.5%, 7/1/2009 (b)   | 8,000,000  | 8,722,480         |
| Massachusetts, Airport Revenue, U.S. Airways, Inc. Project, AMT, Series A, 5.875%, 9/1/2023 (b)               | 5,000,000  | 5,208,650         |
| Massachusetts, Port Authority Revenue, AMT, Series B, 5.5%, 7/1/2015 (b)                                      | 3,000,000  | 3,192,330         |
|   |            | <b>17,123,460</b> |
| <b>Michigan 2.2%</b>  |            |                   |
| Chippewa County, MI, Hospital & Healthcare Revenue, Chippewa County War Memorial, Series B, 5.625%, 11/1/2014 | 1,500,000  | 1,483,290         |
| Michigan, Industrial Development Revenue:   |            |                   |
| 5.5%, 6/1/2018 (b)  | 3,425,000  | 3,691,294         |
| 5.75%, 6/1/2016 (b)   | 4,640,000  | 5,075,046         |
|   |            | <b>10,249,630</b> |
| <b>Minnesota 1.6%</b>   |            |                   |
| Minneapolis and St. Paul, MN, Airport Revenue, AMT, Series B, 6.0%, 1/1/2012 (b)                              | 4,395,000  | 4,809,888         |
| Minneapolis and St. Paul, MN, Port Authority Revenue, AMT, Series B, 5.625%, 1/1/2015 (b)                     | 2,500,000  | 2,682,425         |
|   |            | <b>7,492,313</b>  |
| <b>Missouri 1.3%</b>  |            |                   |

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|  |            |                   |
|--|------------|-------------------|
| Missouri, Hospital & Healthcare Revenue, Lake of the Ozarks General Hospital:  |            |                   |
| Prerefunded, 6.5%, 2/15/2021   | 760,000    | 829,821           |
| 6.5%, 2/15/2021  | 365,000    | 376,147           |
| St. Louis, MO, County GO, Industrial Development Authority Revenue, St. Louis Convention Center, AMT, Series A, 7.2%, 12/15/2028           | 4,000,000  | 3,699,880         |
| St. Louis, MO, Industrial Development Revenue, St. Louis Convention Center, AMT, Series A, 6.875%, 12/15/2020                              | 1,500,000  | 1,375,815         |
|  |            | <b>6,281,663</b>  |
| <b>Nevada 2.6%</b>   |            |                   |
| Clark County, NV, Airport Revenue, AMT, Series A, 1.1%, 7/1/2036 (b) (c)   | 250,000    | 250,000           |
| Las Vegas, NV, Core City GO, Water & Sewer Revenue, 5.375%, 4/1/2014 (b)   | 2,705,000  | 2,944,122         |
| Nevada, State GO, Capital Improvement and Cultural Affairs Project, Series A, 5.5%, 2/1/2014   | 2,575,000  | 2,823,848         |
| Washoe County, NV, School District GO, Prerefunded, 5.75%, 6/1/2014 (b)  | 5,450,000  | 6,128,579         |
|  |            | <b>12,146,549</b> |
| <b>New Jersey 10.5%</b>  |            |                   |
| New Jersey, Hospital & Healthcare Revenue, General Hospital Center at Passaic, ETM, 6.75%, 7/1/2019 (b)                                    | 5,000,000  | 6,115,300         |
| New Jersey, Industrial Development Revenue, American Water Co., Inc. Project, AMT, Series A, 6.875%, 11/1/2034 (b)                         | 10,775,000 | 11,197,919        |
| New Jersey, Industrial Development Revenue, Economic Development Authority, Harrogate, Inc., Series A, 5.875%, 12/1/2026                   | 1,400,000  | 1,362,536         |
| New Jersey, Resource Recovery Revenue, Tobacco Settlement Financing Corp., 5.75%, 6/1/2032   | 4,465,000  | 3,790,919         |
| New Jersey, State Agency (GO) Lease, Transportation Trust Fund Authority, Series A, Prerefunded, 5.75%, 6/15/2017                          | 10,000,000 | 11,303,700        |
| New Jersey, Transportation/Tolls Revenue, Economic Development Authority, Series A, Prerefunded, 5.75%, 5/1/2013 (b)                       | 6,000,000  | 6,709,860         |
| New Jersey, Transportation/Tolls Revenue, Garden State Parkway Project, Prerefunded, 5.6%, 1/1/2017 (b)                                    | 8,000,000  | 9,001,040         |
|  |            | <b>49,481,274</b> |
| <b>New York 10.1%</b>  |            |                   |
| Nassau County, NY, Hospital & Healthcare, 6.0%, 8/1/2015 (b)   | 3,390,000  | 3,794,495         |
| New York, State Agency (GO) Lease, Higher Education Revenue, Dormitory Authority, Bronx-Lebanon Hospital Center, Series E, 5.2%, 2/15/2016 | 1,770,000  | 1,832,694         |
| New York, State Agency (GO) Lease, Higher Education Revenue, Dormitory Authority, City University, Series A, 5.625%, 7/1/2016              | 1,500,000  | 1,662,630         |
| New York, State Agency (GO) Lease, Higher Education Revenue, Dormitory Authority, Jamaica Hospital, Series F, 5.2%, 2/15/2016              | 1,000,000  | 1,035,420         |
| New York, State GO, Tobacco Settlement Funding Corp., Series A-1, 5.5%, 6/1/2019   | 7,400,000  | 7,833,492         |
| New York, Transportation/Tolls Revenue:  |            |                   |
| Prerefunded, 5.625%, 4/1/2013 (b)  | 5,000,000  | 5,600,400         |
| Prerefunded, 5.75%, 4/1/2014 (b)   | 2,000,000  | 2,251,320         |
| New York, NY, Core City GO:  |            |                   |
| Series F, 5.25%, 8/1/2015 (b)  | 10,380,000 | 10,991,070        |
| Series F, 5.25%, 8/1/2015  | 5,000,000  | 5,229,200         |
| New York, NY, Sales & Special Tax Revenue, Transitional Finance Authority:   |            |                   |
| Prerefunded, Series B, 6.125%, 11/15/2014  | 1,645,000  | 1,904,351         |
| Series B, 6.125%, 11/15/2014   | 355,000    | 404,707           |
| Series B, Prerefunded, 6.125%, 11/15/2015  | 3,000,000  | 3,472,980         |
| New York, NY, State GO, Series D-2002, 7.5%, 8/1/2004  | 160,000    | 161,666           |
| Niagara Falls, NY, School District GO, 5.6%, 6/15/2014 (b)   | 1,180,000  | 1,307,003         |

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|  |           |                   |
|--|-----------|-------------------|
|  |           | <b>47,481,428</b> |
| <b>North Carolina 1.8%</b>   |           |                   |
| Charlotte, NC, Airport Revenue, AMT:   |           |                   |
| Series B, 5.75%, 7/1/2013 (b)  | 2,480,000 | 2,693,181         |
| Series B, 5.875%, 7/1/2014 (b)   | 1,140,000 | 1,238,131         |
| North Carolina, Electric Revenue, Municipal Power Agency:  |           |                   |
| Series C, 5.375%, 1/1/2017   | 1,000,000 | 1,031,170         |
| Series B, 6.375%, 1/1/2013   | 3,000,000 | 3,343,440         |
|  |           | <b>8,305,922</b>  |
| <b>North Dakota 0.8%</b>   |           |                   |
| Grand Forks, ND, Hospital & Healthcare Revenue, Altru Health Care System, 7.125%, 8/15/2024  | 3,400,000 | <b>3,658,434</b>  |
| <b>Ohio 2.4%</b>   |           |                   |
| Cuyahoga County, OH, Hospital Revenue, Meridia Health Systems, Prerefunded, 6.25%, 8/15/2024   | 2,350,000 | 2,528,553         |
| Green Springs, OH, Senior Care Revenue, St. Francis Health Care Center Project, Series A, 7.125%, 5/15/2025  | 6,000,000 | 5,126,220         |
| Ohio, Higher Education Revenue, University of Findlay Project:   |           |                   |
| 6.125%, 9/1/2016   | 2,000,000 | 1,998,060         |
| 6.15%, 9/1/2011  | 1,635,000 | 1,668,436         |
|  |           | <b>11,321,269</b> |
| <b>Oklahoma 0.1%</b>   |           |                   |
| Oklahoma, Industrial Authority Revenue, Integris Baptist Project, Series B, 1.08%, 8/15/2029 (b) (c)   | 300,000   | <b>300,000</b>    |
| <b>Oregon 3.4%</b>   |           |                   |
| Oregon, Other (REV) Lease, Department of Administrative Services:  |           |                   |
| Series A, 5.5%, 5/1/2010 (b)   | 2,245,000 | 2,434,680         |
| Series A, 5.6%, 5/1/2011 (b)   | 2,120,000 | 2,306,899         |
| Oregon, State (GO) Lease, Department of Administrative Services, Series A, Prerefunded, 6.25%, 5/1/2017 (b)  | 1,000,000 | 1,163,740         |
| Oregon, State (REV) Lease, Department of Administrative Services, Series A, Prerefunded, 6.25%, 5/1/2018 (b)                                       | 1,000,000 | 1,163,740         |
| Portland, OR, Special Assessment Revenue, Downtown Waterfront:   |           |                   |
| Series A, 5.625%, 6/15/2015 (b)  | 3,100,000 | 3,390,811         |
| Series A, 5.75%, 6/15/2018 (b)   | 2,225,000 | 2,454,442         |
| Series A, 5.75%, 6/15/2019 (b)   | 2,820,000 | 3,101,549         |
|  |           | <b>16,015,861</b> |
| <b>Pennsylvania 1.1%</b>   |           |                   |
| Pennsylvania, Hospital & Healthcare Revenue, Economic Development Financing Authority, UPMC Health System, Series A, 6.0%, 1/15/2031               | 2,570,000 | 2,670,898         |
| Philadelphia, PA, Municipal Authority Revenue, Series B, 5.25%, 11/15/2018 (b)   | 2,500,000 | 2,632,325         |
|  |           | <b>5,303,223</b>  |
| <b>Rhode Island 0.7%</b>   |           |                   |
| Rhode Island, Special Assessment Revenue, Series A, 6.125%, 6/1/2032   | 4,000,000 | <b>3,432,040</b>  |
| <b>South Carolina 3.5%</b>   |           |                   |
| Greenwood County, SC, Hospital & Healthcare Revenue, South Carolina Memorial Hospital, 5.5%, 10/1/2031   | 1,500,000 | 1,506,615         |
| South Carolina, Hospital & Healthcare Revenue, Jobs Economic Development Authority, Bon Secours Health Systems, Inc., Series A, 5.625%, 11/15/2030 | 7,000,000 | 6,793,710         |

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|  |            |                   |
|--|------------|-------------------|
| South Carolina, Hospital & Healthcare Revenue, Jobs Economic Development Authority, Palmetto Health Alliance:                                  |            |                   |
| Series C, 7.0%, 8/1/2030   | 5,420,000  | 5,815,335         |
| Series A, Prerefunded, 7.375%, 12/15/2021  | 2,000,000  | 2,455,580         |
|  |            | <b>16,571,240</b> |
| <b>Tennessee 2.7%</b>  |            |                   |
| Memphis-Shelby County, TN, Airport Revenue, AMT, Series D, 6.25%, 3/1/2017 (b)   | 4,690,000  | 5,188,453         |
| Shelby County, TN, Hospital & Healthcare Revenue, Health Education & Housing Facilities Board, 6.5%, 9/1/2026                                  | 7,000,000  | 7,499,660         |
|  |            | <b>12,688,113</b> |
| <b>Texas 20.8%</b>   |            |                   |
| Austin, TX, Sales & Special Tax Revenue, Hotel Occupancy Tax:  |            |                   |
| 6.0%, 11/15/2013 (b)   | 3,190,000  | 3,569,132         |
| 6.0%, 11/15/2015 (b)   | 3,480,000  | 3,865,375         |
| 6.0%, 11/15/2016 (b)   | 3,625,000  | 4,026,432         |
| Brazos River, TX, Pollution Control Revenue, Brazos River Authority, Texas Utilities Electric Co. Project, AMT, Series C, 5.75%, 5/1/2036 (c)  | 5,000,000  | 5,246,750         |
| Dallas-Fort Worth, TX, Airport Revenue, International Airport, AMT, Series A, 5.875%, 11/1/2016 (b)  | 6,500,000  | 7,131,215         |
| El Paso, TX, State GO:   |            |                   |
| 5.875%, 8/15/2012 (b)  | 1,000,000  | 1,091,770         |
| 5.875%, 8/15/2013 (b)  | 1,570,000  | 1,714,079         |
| 5.875%, 8/15/2014 (b)  | 1,665,000  | 1,817,797         |
| Harris County, TX, Health Facilities Development Corp., Hospital Revenue, Memorial Hermann Healthcare Systems, Series A, 5.125%, 12/1/2022     | 1,000,000  | 973,190           |
| Harris County, TX, Hospital & Healthcare Revenue, Health Facilities Development Corp., YMCA Greater Houston Area, 1.08%, 7/1/2037 (c) (d)      | 500,000    | 500,000           |
| Harris County, TX, Hospital & Healthcare Revenue, Health Facilities Development Corp., Memorial Hermann Healthcare, Series A, 6.375%, 6/1/2029 | 5,500,000  | 5,978,005         |
| Houston, TX, Airport Revenue, People Mover Project, AMT, Series A, 5.5%, 7/15/2017 (b)   | 3,300,000  | 3,452,724         |
| Houston, TX, Port Authority Revenue, Airport Revenue, AMT, Series A, 5.875%, 7/1/2014 (b)  | 3,960,000  | 4,301,550         |
| Lower Neches Valley, TX, Industrial Development Revenue, Mobil Oil Refining Corp. Project, AMT, 6.4%, 3/1/2030                                 | 17,000,000 | 17,513,230        |
| Red River, TX, School District (REV) Lease, St. Marks School Project, 6.0%, 8/15/2019  | 5,390,000  | 5,893,372         |
| Richardson, TX, Hospital & Healthcare Revenue, Hospital Authority, 5.625%, 12/1/2028   | 5,000,000  | 4,690,850         |
| Tarrant County, TX, Hospital & Healthcare Revenue, Health Facilities Development Corp., 6.7%, 11/15/2030                                       | 4,500,000  | 4,840,020         |
| Texas, Industrial Development Revenue, Waste Disposal Authority, AMT, Series A, 6.1%, 8/1/2024   | 2,000,000  | 2,025,440         |
| Texas, State GO, College Student Loans, AMT, 5.0%, 8/1/2021  | 4,015,000  | 3,948,833         |
| Texas, State Turnpike Authority, Dallas Northway Revenue, 5.5%, 1/1/2015 (b)   | 14,605,000 | 15,649,550        |
|  |            | <b>98,229,314</b> |
| <b>Utah 0.0%</b>   |            |                   |
| Utah, Single Family Housing Revenue, Housing Finance Agency, AMT, Series B2, 6.65%, 7/1/2026 (b)   | 65,000     | <b>65,250</b>     |
| <b>Washington 5.9%</b>   |            |                   |
| Seattle, WA, Airport Revenue, AMT, Series B, 6.0%, 2/1/2013 (b)  | 7,355,000  | 8,207,297         |
| Seattle, WA, Special Assessment Revenue, AMT:  |            |                   |
| Series B, 5.5%, 9/1/2011 (b)   | 1,085,000  | 1,168,296         |
| Series B, 5.75%, 9/1/2013 (b)  | 1,045,000  | 1,135,800         |

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|  |           |                    |
|--|-----------|--------------------|
| Skagit County, WA, School District GO, School District No. 1, Burlington Edison, 5.625%, 12/1/2014 (b)                                   | 1,570,000 | 1,747,284          |
| Snohomish County, WA, Electric Revenue, Public Utility District No. 1, 5.375%, 12/1/2024 (b)   | 3,000,000 | 3,088,170          |
| Washington, Electric Revenue, Energy Northwest Columbia Generating, Series B, 6.0%, 7/1/2018 (b)   | 3,000,000 | 3,363,360          |
| Washington, Hospital & Healthcare Revenue, Group Health Coop of Puget Sound, 5.375%, 12/1/2017 (b)                                       | 1,500,000 | 1,583,790          |
| Washington, State GO:  |           |                    |
| Series A, 5.5%, 7/1/2013   | 2,000,000 | 2,181,100          |
| Series A, 5.5%, 7/1/2016   | 4,835,000 | 5,198,205          |
|  |           | <b>27,673,302</b>  |
| <b>West Virginia 4.6%</b>  |           |                    |
| West Virginia, Hospital Finance Authority, Charleston Medical Center:  |           |                    |
| Prerefunded, 6.75%, 9/1/2022   | 9,645,000 | 11,512,658         |
| Prerefunded, 6.75%, 9/1/2030   | 3,605,000 | 4,303,072          |
| West Virginia, Hospital & Healthcare Revenue, Hospital Finance Authority, Charleston Medical Center:                                     |           |                    |
| Series A, 6.75%, 9/1/2022  | 2,355,000 | 2,575,922          |
| 6.75%, 9/1/2030  | 395,000   | 426,553            |
| West Virginia, Water & Sewer Revenue, Water Development Authority, Series B, 5.25%, 11/1/2023 (b)  | 2,740,000 | 2,838,969          |
|  |           | <b>21,657,174</b>  |
| <b>Wisconsin 2.1%</b>  |           |                    |
| Wisconsin, Hospital & Healthcare Revenue, Health & Educational Facilities Authority, Aurora Health Care, Inc., Series A, 5.6%, 2/15/2029 | 6,000,000 | 5,718,120          |
| Wisconsin, Special Assessment Revenue, 6.125%, 6/1/2027  | 4,695,000 | 4,211,368          |
|  |           | <b>9,929,488</b>   |
| <b>Total Municipal Investments</b>   |           | <b>732,649,723</b> |

|  | % of Net Assets | Value (\$)           |
|--|-----------------|----------------------|
| <b>Total Investment Portfolio</b> (Cost \$682,173,562) (a) | 155.4           | <b>732,649,723</b>   |
| <b>Other Assets and Liabilities, Net</b>                   | .8              | <b>3,679,147</b>     |
| <b>Preferred Stock, at Redemption Value</b>                | (56.2)          | <b>(265,000,000)</b> |
| <b>Net Assets Applicable to Common Shareholders</b>        | 100.0           | <b>471,328,870</b>   |

(a) The cost for federal income tax purposes was \$681,914,668. At May 31, 2004, net unrealized appreciation for all securities based on tax cost was \$50,735,055. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of \$53,997,523 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of \$3,262,468.

(b) Bond is insured by one of these companies:

| Insurance Coverage |                                       | As a % of Total Investment Portfolio |
|--------------------|---------------------------------------|--------------------------------------|
| AMBAC              | AMBAC Assurance Corp.                 | 17.1                                 |
| FGIC               | Financial Guaranty Insurance Company  | 11.3                                 |
| FSA                | Financial Security Assurance          | 16.0                                 |
| MBIA               | Municipal Bond Investors Assurance    | 18.0                                 |
| FNMA               | Federal National Mortgage Association | .8                                   |

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|     |                                |    |
|-----|--------------------------------|----|
| FHA | Federal Housing Administration | .1 |
|-----|--------------------------------|----|

(c) Variable rate demand notes are securities whose interest rates are reset periodically at market levels. These securities are often payable on demand and are shown at their current rates as of May 31, 2004.

(d) Security incorporates a letter of credit from a major bank.

AMT: Subject to alternative minimum tax

ETM: Bonds bearing the description ETM (escrowed to maturity) are collateralized by US Treasury securities which are held in escrow and used to pay principal and interest on bonds so designated.

Prerefunded: Bonds which are prerefunded are collateralized by US Treasury securities which are held in escrow and are used to pay principal and interest on tax-exempt issues and to retire the bonds in full at the earliest refunding date.

The accompanying notes are an integral part of the financial statements.

## Financial Statements

| <b>Statement of Assets and Liabilities as of May 31, 2004 (Unaudited)</b>  |                       |
|--|-----------------------|
| <b>Assets</b>  |                       |
| Investments in securities, at value (cost \$682,173,562)   | \$ 732,649,723        |
| Cash   | 94,938                |
| Receivable for investments sold  | 440,000               |
| Interest receivable  | 13,003,431            |
| Other assets   | 12,087                |
| <b>Total assets</b>  | <b>746,200,179</b>    |
| <b>Liabilities</b>   |                       |
| Payable for investments purchased  | 9,022,306             |
| Dividends payable  | 178,249               |
| Accrued management fee   | 335,096               |
| Other accrued expenses and payables  | 335,658               |
| <b>Total liabilities</b>   | <b>9,871,309</b>      |
| <b>Remarketed preferred shares, at redemption value</b>  | <b>265,000,000</b>    |
| <b>Net assets applicable to common shareholders</b>  | <b>\$ 471,328,870</b> |
| <b>Net Assets</b>  |                       |
| Net assets applicable to common shareholders consist of:   |                       |
| Undistributed net investment income  | 4,601,328             |
| Net unrealized appreciation (depreciation) on investments  | 50,476,161            |
| Accumulated net realized gain (loss)   | (10,093,274)          |
| Paid-in capital  | 426,344,655           |
| <b>Net assets applicable to common shareholders</b>  | <b>\$ 471,328,870</b> |
| <b>Net Asset Value</b>   |                       |
| <b>Net Asset Value</b> per common share (\$471,328,870 / 38,832,628 outstanding shares of beneficial interest, \$.01 par value, unlimited number of shares authorized) | <b>\$ 12.14</b>       |

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The accompanying notes are an integral part of the financial statements.

| <b>Statement of Operations</b> for the six months ended May 31, 2004 (Unaudited) |                       |
|--|-----------------------|
| <b>Investment Income</b>   |                       |
| Income:  |                       |
| Interest   | \$ 20,039,563         |
| Expenses:  |                       |
| Management fee   | 2,074,214             |
| Services to shareholders   | 34,463                |
| Custodian fees   | 13,065                |
| Auditing   | 19,435                |
| Legal  | 7,320                 |
| Trustees' fees and expenses  | 14,810                |
| Reports to shareholders  | 17,560                |
| Remarketing agent fee  | 268,750               |
| Stock exchange listing fees  | 12,361                |
| Other  | 30,652                |
| Total expenses, before expense reductions  | 2,492,630             |
| Expense reductions   | (210)                 |
| Total expenses, after expense reductions   | 2,492,420             |
| <b>Net investment income</b>   | <b>17,547,143</b>     |
| <b>Realized and Unrealized Gain (Loss) on Investment Transactions</b>            |                       |
| Net realized gain (loss) from investments  | 487,778               |
| Net unrealized appreciation (depreciation) during the period on investments      | (18,546,678)          |
| <b>Net gain (loss) on investment transactions</b>                                | <b>(18,058,900)</b>   |
| <b>Dividends on remarketed preferred shares</b>                                  | <b>(1,324,290)</b>    |
| <b>Net increase (decrease) in net assets resulting from operations</b>           | <b>\$ (1,836,047)</b> |

The accompanying notes are an integral part of the financial statements.

| <b>Statement of Changes in Net Assets</b>           |  |                                    |
|---|--|------------------------------------|
|   | <b>Six Months Ended<br/>May 31,<br/>2004</b> | <b>Year Ended November<br/>30,</b> |
| <b>Increase (Decrease) in Net Assets</b>            | <b>(Unaudited)</b>                           | <b>2003</b>                        |
| Operations:   |  |                                    |
| Net investment income                               | \$ 17,547,143                                | \$ 35,554,384                      |
| Net realized gain (loss) on investment transactions | 487,778                                      | (1,562,075)                        |

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|  |                       |                       |
|--|-----------------------|-----------------------|
| Net unrealized appreciation (depreciation) on investment transactions during the period                                  | (18,546,678)          | 15,500,754            |
| Dividends on remarketed preferred shares   | (1,324,290)           | (2,886,268)           |
| Net increase (decrease) in net assets resulting from operations  | (1,836,047)           | 46,606,795            |
| Distributions to common shareholders from:   |                       |                       |
| Net investment income  | (15,763,069)          | (30,568,443)          |
| Net realized gains   | -                     | (194,163)             |
| <b>Increase (decrease) in net assets</b>   | (17,599,116)          | 15,844,189            |
| Net assets at beginning of period  | 488,927,986           | 473,083,797           |
| Net assets at end of period (including undistributed net investment income of \$4,601,328 and \$4,141,544, respectively) | <b>\$ 471,328,870</b> | <b>\$ 488,927,986</b> |
| <b>Other Information</b>   |                       |                       |
| Shares outstanding at beginning of period  | 38,832,628            | 38,832,628            |
| Shares outstanding at end of period  | 38,832,628            | 38,832,628            |

The accompanying notes are an integral part of the financial statements.

## Financial Highlights

| Years Ended November 30,   | 2004 <sup>a</sup> | 2003     | 2002 <sup>b</sup> | 2001 <sup>c</sup> | 2000 <sup>c</sup> | 1999 <sup>c</sup> |
|--|-------------------|----------|-------------------|-------------------|-------------------|-------------------|
| <b>Selected Per Share Data</b>   |                   |          |                   |                   |                   |                   |
| Net asset value, beginning of period                                       | \$ 12.59          | \$ 12.18 | \$ 11.87          | \$ 11.30          | \$ 11.03          | \$ 12.41          |
| <i>Income (loss) from investment operations:</i>                           |                   |          |                   |                   |                   |                   |
| Net investment income <sup>d</sup>   | .45               | .92      | .91               | .91               | .93               | .92               |
| Net realized and unrealized gain (loss) on investment transactions         | (.46)             | .36      | .22               | .59               | .42               | (1.28)            |
| <i>Dividends on remarketed preferred shares (common share equivalent):</i> |                   |          |                   |                   |                   |                   |
| From net investment income   | (.03)             | (.07)    | (.10)             | (.21)             | (.28)             | (.18)             |
| <b>Total from investment operations</b>                                    | (.04)             | 1.21     | 1.03              | 1.29              | 1.07              | (.54)             |
| <i>Less distributions from:</i>  |                   |          |                   |                   |                   |                   |
| Net investment income to common shareholders                               | (.41)             | (.79)    | (.72)             | (.72)             | (.80)             | (.83)             |
| Net realized gains on investment transactions to common shareholders       | -                 | (.01)    | -                 | -                 | -                 | -                 |
| Dilution resulting from remarketed preferred shares <sup>e</sup>           | -                 | -        | -                 | -                 | -                 | (.01)             |
| <b>Total distributions</b>   | (.41)             | (.80)    | (.72)             | (.72)             | (.80)             | (.84)             |
| Net asset value, end of period   | \$ 12.14          | \$ 12.59 | \$ 12.18          | \$ 11.87          | \$ 11.30          | \$ 11.03          |
| Market value, end of period  | \$ 11.06          | \$ 11.96 | \$ 11.06          | \$ 11.37          | \$ 10.25          | \$ 10.31          |
| <b>Total Return</b>  |                   |          |                   |                   |                   |                   |
| Based on net asset value (%) <sup>f</sup>                                  | (.27)**           | 10.53    | 9.36              | 11.93             | 10.40             | (4.69)            |
| Based on market value (%) <sup>f</sup>                                     | (4.36)**          | 15.63    | 3.76              | 18.10             | 7.11              | (24.40)           |

Years Ended November 30, (continued)

2004<sup>a</sup> 2003 2002<sup>b</sup> 2001<sup>c</sup> 2000<sup>c</sup> 1999<sup>c</sup>

May 31, 2004

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| <b>Ratios to Average Net Assets and Supplemental Data</b>  |        |        |        |        |        |        |
|--|--------|--------|--------|--------|--------|--------|
| Net assets, end of period (\$ millions)  | 471    | 489    | 473    | 461    | 439    | 428    |
| Ratio of expenses (%) (based on net assets of common shares)   | 1.02*  | 1.05   | 1.07   | 1.09   | 1.24   | 1.13   |
| Ratio of expenses (%) (based on net assets of common and remarketed preferred shares)  | .66*   | .68    | .69    | .69    | .77    | .77    |
| Ratio of net investment income (%) (based on net assets of common shares)  | 7.18*  | 7.35   | 7.51   | 7.72   | 8.48   | 7.76   |
| Ratio of net investment income (%) (based on net assets of common and remarketed preferred shares)   | 4.66*  | 4.75   | 4.80   | 4.90   | 5.23   | 5.27   |
| Portfolio turnover rate (%)  | 13*    | 7      | 7      | 10     | 38     | 38     |
| Remarketed preferred shares information at end of period:  |        |        |        |        |        |        |
| Aggregate amount outstanding (\$ millions)   | 265    | 265    | 265    | 265    | 265    | 265    |
| Asset coverage per share (\$)***   | 13,893 | 14,225 | 13,900 | 13,700 | 13,300 | 13,100 |
| Liquidation and market value per share (\$)  | 5,000  | 5,000  | 5,000  | 5,000  | 5,000  | 5,000  |
| <p><sup>a</sup> For the six months ended May 31, 2004 (Unaudited).</p> <p><sup>b</sup> As required, effective December 1, 2001, the Fund has adopted the provisions of the AICPA Audit and Accounting Guide for Investment Companies and began accreting market discount on debt securities. The effect of this change for the six months ended May 31, 2004 was to increase net investment income by an amount less than \$.005 and decrease net realized and unrealized gain (loss) per share by an amount less than \$.005. Per share data and ratios for periods prior to December 1, 2001 have not been restated to reflect this change in presentation.</p> <p><sup>c</sup> In 2001 the Fund changed its method of classifying remarketed preferred shares.</p> <p><sup>d</sup> Based on average common shares outstanding during the period.</p> <p><sup>e</sup> On November 24, 1999, the Fund issued 10,000 remarketed preferred shares.</p> <p><sup>f</sup> Total return based on net asset value reflects changes in the Fund's net asset value during the period. Total return based on market value reflects changes in market value. Each figure includes reinvestment of dividends. These figures will differ depending upon the level of any discount from or premium to net asset value at which the Fund's shares trade during the period.</p> <p>* Annualized</p> <p>** Not annualized</p> <p>*** Asset coverage per share equals net assets of common shares plus the redemption value of the remarketed preferred shares divided by the total number of remarketed preferred shares outstanding at the end of the period.</p> |        |        |        |        |        |        |

## Notes to Financial Statements (Unaudited)

### A. Significant Accounting Policies

Scudder Municipal Income Trust (the "Fund") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as a closed-end, diversified management investment company organized as a Massachusetts business trust.

The Fund's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Fund in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading. Debt securities are valued by independent pricing services approved by the Trustees of the Fund, whose valuations are intended to reflect the mean between the bid and asked prices. If the pricing services are unable to provide valuations, the securities are valued at the most recent bid quotation or evaluated price, as applicable, obtained from a broker dealer. Such services may use various pricing techniques which take into account appropriate factors such as yield, quality, coupon rate, maturity, type of issue,

trading characteristics and other data, as well as broker quotes.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Trustees.

**Federal Income Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies, and to distribute all of its taxable and tax-exempt income to its shareholders. Accordingly, the Fund paid no federal income taxes and no federal income tax provision was required.

At November 30, 2003 the Fund had a net tax basis capital loss carryforward of approximately \$10,421,000 which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until November 30, 2007 (\$5,496,000), November 30, 2008 (\$3,602,000) and November 30, 2011 (\$1,323,000), the respective expiration dates, whichever occurs first.

**Distribution of Income and Gains.** Net investment income of the Fund is declared and distributed to shareholders monthly. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed, and, therefore, will be distributed to shareholders at least annually.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

The tax character of current year distributions will be determined at the end of the current fiscal year.

**Remarketed Preferred Shares.** The Fund has issued and outstanding 10,800 Series A, 10,700 Series B, 10,800 Series C, 10,700 Series D and 10,000 Series E remarketed preferred shares, each at a liquidation value of \$5,000 per share. The preferred shares are senior to and have certain class specific preferences over the common shares. The dividend rate on each series is set by the remarketing agent, and the dividends are generally paid every 28 days. The remarketing agent will pay each broker-dealer a service charge from funds provided by the Fund (remarketing agent fee). The 1940 Act requires that the preferred shareholders of the Fund, voting as a separate class, have the right to: a) elect at least two trustees at all times, and b) elect a majority of the trustees at any time when dividends on the preferred shares are unpaid for two full years. Unless otherwise required by law or under the terms of the preferred shares designation statement, each preferred share is entitled to one vote and preferred shareholders will vote together with common shareholders as a single class and have the same voting rights.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Realized gains and losses from investment transactions are recorded on an identified cost basis. All premiums and discounts are amortized/accreted for financial reporting purposes.

## **B. Purchases and Sales of Securities**

During the six months ended May 31, 2004, purchases and sales of investment securities (excluding short-term investments) aggregated \$48,778,558 and \$45,501,500, respectively.

### **C. Related Parties**

**Management Agreement.** Under the Management Agreement with Deutsche Investment Management Americas Inc. ("DeIM" or the "Advisor"), the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund. In addition to portfolio management services, the Advisor provides certain administrative services in accordance with the Management Agreement. The Fund pays a monthly investment management fee of 1/2 of the annual rate of 0.55% of the Fund's average weekly net assets, of common shares plus the value of remarketed preferred shares, at redemption value, computed and accrued daily and payable monthly.

**Service Provider Fees.** Scudder Investments Service Company ("SISC"), an affiliate of the Advisor, is the transfer, dividend-paying and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between SISC and DST systems, Inc. ("DST"), SISC has delegated certain transfer agent and dividend paying agent functions to DST. SISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the six months ended May 31, 2004, the amount charged to the Fund by SISC aggregated \$20,760, of which \$3,333 is unpaid.

**Trustees' Fees and Expenses.** The Fund pays each Trustee not affiliated with the Advisor retainer fees plus specified amounts for attended board and committee meetings.

### **D. Expense Off-Set Arrangement**

The Fund has entered into an arrangement with its custodian whereby credits realized as a result of uninvested cash balances were used to reduce a portion of the Fund's expenses. During the six months ended May 31, 2004, the Fund's custodian fees were reduced by \$210 under this arrangement.

### **E. Line of Credit**

The Fund and several other affiliated funds (the "Participants") share in a \$1.25 billion revolving credit facility administered by J.P. Morgan Chase Bank for temporary or emergency purposes. The Participants are charged an annual commitment fee which is allocated, based upon net assets, among each of the Participants. Interest is calculated at the Federal Funds Rate plus 0.5 percent. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

## **Dividend Reinvestment Plan**

### **A. Participation**

We invite you to review the description of the Dividend Reinvestment Plan (the "Plan") which is available to you as a shareholder of Scudder Municipal Income Trust (the "Fund"). If you wish to participate and your shares are held in your own name, simply contact Scudder Investments Service Company, whose address and phone number are provided in Paragraph E for the appropriate form. If your shares are held in the name of a brokerage firm, bank, or other nominee, you must instruct that nominee to re-register your shares in your name so that you may participate in the Plan, unless your nominee has made the Plan available on shares held by them. Shareholders who so elect will be

deemed to have appointed UMB Bank, N.A. ("United Missouri Bank" or "UMB") as their agent and as agent for the Fund under the Plan.

### **B. Dividend Investment Account**

The Fund's transfer agent and dividend disbursing agent or its delegate (the "Transfer Agent") will establish a Dividend Investment Account (the "Account") for each shareholder participating in the Plan. The Transfer Agent will credit to the Account of each participant funds it receives from the following sources: (a) cash dividends and capital gains distributions paid on shares of beneficial interest (the "Shares") of the Fund registered in the participant's name on the books of the Fund; and (b) cash dividends and capital gains distributions paid on Shares registered in the name of the Transfer Agent but credited to the participant's Account. Sources described in clauses (a) and (b) of the preceding sentence are hereinafter called "Distributions."

### **C. Investment of Distribution Funds held in each account**

If on the record date for a Distribution (the "Record Date"), Shares are trading at a discount from net asset value per Share (according to the evaluation most recently made on Shares of the Fund), funds credited to a participant's Account will be used to purchase Shares (the "Purchase"). UMB will attempt, commencing five days prior to the Payment Date and ending at the close of business on the Payment Date ("Payment Date" as used herein shall mean the last business day of the month in which such Record Date occurs), to acquire Shares in the open market. If and to the extent that UMB is unable to acquire sufficient Shares to satisfy the Distribution by the close of business on the Payment Date, the Fund will issue to UMB Shares valued at net asset value per Share (according to the evaluation most recently made on Shares of the Fund) in the aggregate amount of the remaining value of the Distribution. If, on the Record Date, Shares are trading at a premium over net asset value per Share, the Fund will issue on the Payment Date, Shares valued at net asset value per Share on the Record Date to the Transfer Agent in the aggregate amount of the funds credited to the participants' accounts.

### **D. Voluntary Cash Contributions**

A participant may from time to time make voluntary cash contributions to his Account by sending to Transfer Agent a check or money order, payable to Transfer Agent, in a minimum amount of \$100 with appropriate accompanying instructions. (No more than \$500 may be contributed per month.) Transfer Agent will inform UMB of the total funds available for the purchase of Shares and UMB will use the funds to purchase additional Shares for the participant's Account the earlier of: (a) when it next purchases Shares as a result of a Distribution or (b) on or shortly after the first day of each month and in no event more than 30 days after such date except when temporary curtailment or suspension of purchases is necessary to comply with applicable provisions of federal securities laws. Cash contributions received more than fifteen calendar days or less than five calendar days prior to a Payment Date will be returned uninvested. Interest will not be paid on any uninvested cash contributions. Participants making voluntary cash investments will be charged a \$.75 service fee for each such investment and will be responsible for their pro rata share of brokerage commissions.

### **E. Additional Information**

Address all notices, correspondence, questions, or other communication regarding the Plan, or if you would like a copy of the Plan, to:

Scudder Investments Service Company  
P.O. Box 219066  
Kansas City, Missouri 64121-9066  
1-800-294-4366

#### **F. Adjustment of Purchase Price**

The Fund will increase the price at which Shares may be issued under the Plan to 95% of the fair market value of the shares on the Record Date if the net asset value per Share of the Shares on the Record Date is less than 95% of the fair market value of the Shares on the Record Date.

#### **G. Determination of Purchase Price**

The cost of Shares and fractional Shares acquired for each participant's Account in connection with a Purchase shall be determined by the average cost per Share, including brokerage commissions as described in Paragraph G hereof, of the Shares acquired by UMB in connection with that Purchase. Shareholders will receive a confirmation showing the average cost and number of Shares acquired as soon as practicable after the Transfer Agent has received or UMB has purchased Shares. The Transfer Agent may mingle the cash in a participant's account with similar funds of other participants of the Fund for whom UMB acts as agent under the Plan.

#### **H. Brokerage Charges**

There will be no brokerage charges with respect to Shares issued directly by the Fund as a result of Distributions. However, each participant will pay a pro rata share of brokerage commissions incurred with respect to UMB's open market purchases in connection with the reinvestment of Distributions. Brokerage charges for purchasing small amounts of Shares for individual Accounts through the Plan can be expected to be less than the usual brokerage charges for such transactions, as UMB will be purchasing Shares for all participants in blocks and prorating the lower commission thus attainable.

#### **I. Service Charges**

There is no service charge by the Transfer Agent or UMB to shareholders who participate in the Plan other than service charges specified in Paragraphs D and M hereof. However, the Fund reserves the right to amend the Plan in the future to include a service charge.

#### **J. Transfer of Shares Held by Agent**

The Transfer Agent will maintain the participant's Account, hold the additional Shares acquired through the Plan in safekeeping and furnish the participant with written confirmation of all transactions in the Account. Shares in the Account are transferable upon proper written instructions to the Transfer Agent. Upon request to the Transfer Agent, a certificate for any or all full Shares in a participant's Account will be sent to the participant.

#### **K. Shares Not Held in Shareholder's Name**

Beneficial owners of Shares which are held in the name of a broker or nominee will not be automatically included in the Plan and will receive all distributions in cash. Such shareholders should contact the broker or nominee in whose name their Shares are held to determine whether and how they may participate in the Plan.

#### **L. Amendments**

Experience under the Plan may indicate that changes are desirable. Accordingly, the Fund reserves the right to amend or terminate the Plan, including provisions with respect to any Distribution paid, subsequent to notice thereof sent to participants in the Plan at least ninety days before the record date for such Distribution, except when such amendment is necessary or appropriate to comply with applicable law or the rules or policies of the Securities and Exchange Commission or any other regulatory authority, in which case such amendment shall be effective as soon as practicable. The amendment shall be deemed to be accepted by each participant unless, prior to the effective date

thereof, the Transfer Agent receives notice of the termination of such participant's account under the Plan in accordance with the terms hereof. The Plan may be terminated by the Fund.

**M. Withdrawal from Plan**

Shareholders may withdraw from the Plan at any time by giving the Transfer Agent a written notice. If the proceeds are \$100,000 or less and the proceeds are to be payable to the shareholder of record and mailed to the address of record, a signature guarantee normally will not be required for notices by individual account owners (including joint account owners), otherwise a signature guarantee will be required. In addition, if the certificate is to be sent to anyone other than the registered owner(s) at the address of record, a signature guarantee will be required on the notice. A notice of withdrawal will be effective for the next Distribution following receipt of the notice by the Transfer Agent provided the notice is received by the Transfer Agent at least ten days prior to the Record Date for the Distribution. When a participant withdraws from the Plan, or when the Plan is terminated in accordance with Paragraph L hereof, the participant will receive a certificate for full Shares in the Account, plus a check for any fractional Shares based on market price; or if a Participant so desires, the Transfer Agent will notify UMB to sell his Shares in the Plan and send the proceeds to the participant, less brokerage commissions and a \$2.50 service fee.

**N. Tax Implications**

Shareholders will receive tax information annually for personal records and to assist in preparation of their Federal income tax returns. If Shares are purchased at a discount, the amount of the discount is considered taxable income and is added to the cost basis of the purchased shares.

**Shareholder Meeting Results**

The Annual Meeting of Shareholders of Scudder Municipal Income Trust (the "fund") was held on June 29, 2004 at the office of Deutsche Investment Management Americas Inc., Two International Place, Boston, Massachusetts. At the meeting, the following matters were voted upon by the shareholders:

- 1. To elect nine Trustees to the Board of Trustees of the fund.

|                     | Number of Votes: |           |
|---------------------|------------------|-----------|
|                     | For              | Withheld  |
| John W. Ballantine  | 23,871,433       | 1,150,076 |
| Lewis A. Burnham    | 23,903,157       | 1,188,352 |
| Donald L. Dunaway   | 23,923,804       | 1,097,705 |
| James R. Edgar      | 23,916,916       | 1,104,593 |
| Paul K. Freeman     | 23,912,478       | 1,109,031 |
| Robert B. Hoffman   | 23,901,696       | 1,119,813 |
| Shirley D. Peterson | 23,900,914       | 1,120,595 |
| William N. Shiebler | 39,644           | 20        |
| John G. Weithers    | 39,644           | 20        |

2. To ratify the selection of Ernst & Young LLP as the fund's independent auditors for the current fiscal year.

| Affirmative | Against | Abstain |
|-------------|---------|---------|
| 24,019,917  | 421,825 | 579,766 |

3. To approve the modification or elimination of certain investment policies and the elimination of the shareholder approval requirement as to certain other matters.

|  | Affirmative | Against   | Abstain   |
|--|-------------|-----------|-----------|
| Investment Objectives  | 17,731,957  | 1,825,212 | 1,016,224 |
| Investment Policies  | 18,128,460  | 1,406,382 | 1,016,915 |
| Diversification  | 18,046,448  | 1,497,943 | 1,029,004 |
| Borrowing  | 17,789,440  | 1,687,632 | 1,096,322 |
| Senior Securities  | 17,900,277  | 1,603,750 | 1,069,367 |
| Concentration  | 17,983,532  | 1,444,715 | 1,145,149 |
| Underwriting of Securities   | 18,110,739  | 1,406,449 | 1,056,206 |
| Investment in Real Estate  | 17,993,638  | 1,502,492 | 1,077,265 |
| Purchase of Commodities  | 17,768,142  | 1,704,823 | 1,100,428 |
| Lending  | 17,820,229  | 1,670,720 | 1,082,444 |
| Margin Purchases and Short Sales                                       | 17,546,235  | 1,892,116 | 1,135,045 |
| Restricted and Illiquid Securities                                     | 17,491,789  | 1,926,773 | 1,154,832 |
| Investment other than in Municipal Securities and Temporary Investment | 17,701,318  | 1,794,082 | 1,077,997 |

The following were the number of broker non-votes for proposal 3: Investment Objectives (4,448,116), Investment Policies (4,469,752), Diversification (4,448,114), Borrowing (4,448,115), Senior Securities (4,448,115), Concentration (4,448,113), Underwriting of Securities (4,448,115), Investment in Real Estate (4,448,114), Purchase of Commodities (4,448,116), Lending (4,448,116), Margin Purchases and Short Sales (4,448,113), Restricted and Illiquid Securities (4,448,115), and Investment other than in Municipal Securities and Temporary Investment (4,448,112).

### Policies and Objective

At the 2004 Annual Shareholder Meeting, the fund's shareholders approved the elimination of the shareholder approval requirement for amending (a) the "investment objective" and (b) the "investment policies" which are not otherwise specifically identified as fundamental.

Based on the approval of all of the 2004 Annual Shareholder Meeting proposals, the following are the fund's fundamental investment policies, effective June 29, 2004.

As a matter of fundamental policy, the fund may not:

1. borrow money, except as permitted under the Investment Company Act of 1940 (the "1940 Act"), as amended, and as interpreted or modified by regulatory authority having jurisdiction, from time to time;
2. issue senior securities, except as permitted under the 1940 Act, as amended, and as interpreted or modified by regulatory authority having jurisdiction, from time to time;

3. concentrate its investments in a particular industry, as that term is used in the 1940 Act, as amended, and as interpreted or modified by regulatory authority having jurisdiction, from time to time;
4. engage in the business of underwriting securities issued by others, except to the extent that the fund may be deemed to be an underwriter in connection with the disposition of portfolio securities;
5. purchase or sell real estate, which term does not include securities of companies which deal in real estate or mortgages or investments secured by real estate or interests therein, except that the fund reserves freedom of action to hold and to sell real estate acquired as a result of the fund's ownership of securities;
6. purchase physical commodities or contracts relating to physical commodities; or
7. make loans except as permitted under the 1940 Act, as amended, and as interpreted or modified by regulatory authority having jurisdiction, from time to time.

All other investment policies of the fund that are not stated above are classified as nonfundamental, and therefore do not require shareholder approval to be changed. Similarly, the fund's investment objective is classified as nonfundamental.

The fund remains a "diversified" fund under the 1940 Act, but is not subject to additional requirements that are more restrictive than the 1940 Act. Under the 1940 Act, a "diversified" fund may not, with respect to 75% of the value of its total assets, invest more than 5% of the value of its total assets in securities issued by any one issuer or purchase more than 10% of the outstanding voting securities of any one issuer, except in each case in US government securities or securities issued by other investment companies.

As discussed above, the shareholders also have approved the elimination of certain policies as fundamental, and it is anticipated that Deutsche Investment Management Americas Inc. will recommend to the Board that the following policies be eliminated as being unnecessary:

**Margin Purchases and Short Sales** The fund is currently prohibited from making short sales of securities or purchasing any securities on margin (except for such short term credits as are necessary for the clearance of transactions), or writing or purchasing put or call options, except to the extent that the purchase of a stand-by commitment may be considered the purchase of a put, and except for transactions involving options within the limits described in the prospectus.

If the Board approves the elimination of this restriction, the fund's potential use of margin transactions beyond transactions in futures and options and for the clearance of purchases and sales of securities, including the use of margins in ordinary securities transactions, would be generally limited by the current position taken by the staff of the Securities and Exchange Commission that margin transactions with respect to securities are prohibited under Section 18 of the 1940 Act because they create senior securities. "Margin transactions" involve the purchase of securities with money borrowed from a broker, with cash or eligible securities being used as collateral against the loan. The fund's ability to engage in margin transactions is also limited by its borrowing policies, which permit the fund to borrow money only as permitted by applicable law.

**Restricted and Illiquid Securities** The fund is currently prohibited from entering into repurchase agreements or purchasing securities if, as a result: (1) more than 20% of the fund's total assets would be invested in illiquid securities or restricted securities; or (2) more than 10% of total assets would be invested in repurchase agreements maturing in more than seven days.

If the Board approves the elimination of this restriction, the fund would remain subject to any restrictions imposed by applicable law.



**Investments Other than in Municipal Securities and Temporary Investments** The fund is currently prohibited from purchasing securities or from the making of investments other than in municipal securities and temporary investments.

If the Board approves the elimination of this restriction, the fund would remain subject to any restrictions imposed by applicable law.

### Changes in Officers and Directors

Richard Hale resigned as a Trustee, Chairman and Chief Executive Officer of the fund effective with his retirement on June 18, 2004 as a Managing Director of Deutsche Investment Management Americas Inc., the fund's investment manager.

In anticipation of the resulting vacancies, the Board of Trustees elected William N. Shiebler as Trustee and Chairman of the Board. Mr. Shiebler currently serves as CEO in the Americas of the fund's investment manager. In addition, the Board has elected Julian F. Sluyters, a Managing Director of the fund's investment manager, as Chief Executive Officer of the fund. These elections became effective June 18, 2004. As noted (in the section of this report entitled "Shareholder Meeting Results"), Mr. Shiebler was thereafter elected as a Trustee at the fund's 2004 annual meeting on June 29, 2004.

On May 12, 2004, the Board of Trustees appointed Kevin Gay as Assistant Treasurer of the fund, replacing Lucinda Stebbins, who resigned as Assistant Treasurer in connection with her retirement as a Director of the fund's investment manager on June 1, 2004.

## Additional Information

|                                    |  |
|------------------------------------|--|
| <b>Automated Information Lines</b> | <b>Scudder Closed-End Fund Info Line</b><br><br>(800) 349-4281   |
| <b>Web Sites</b>                   | <b>www.scudder.com</b><br><br>or visit our Direct Link:<br><br><b>CEF.Scudder.com</b> (Do not use www.)<br><br>Obtain monthly fact sheets, financial reports, press releases and webcasts when available.  |
| <b>Written Correspondence</b>      | <b>Deutsche Investment Management Americas Inc.</b><br><br>222 South Riverside<br>Chicago, IL 60606  |
| <b>Proxy Voting</b>                | A description of the fund's policies and procedures for voting proxies for portfolio securities can be found on our Web site - scudder.com (type "proxy voting" in the search field) - or on the SEC's Web site - www.sec.gov. To obtain a written copy without charge, call us toll free at (800) 621-1048. |
| <b>Legal Counsel</b>               | <b>Vedder, Price, Kaufman &amp; Kammholz</b><br><br>222 North LaSalle Street<br>Chicago, IL 60601  |
|                                    | <b>UMB Bank</b>  |

|   |  |
|---|--|
| <b>Dividend Reinvestment Plan Agent</b> | P.O. Box 410064<br>Kansas City, MO 64141-0064  |
| <b>Shareholder Service Agent</b>        | <b>Scudder Investments Service Company</b><br><br>P.O. Box 219066<br>Kansas City, MO 64121-9066<br><b>(800) 294-4366</b> |
| <b>Custodian and Transfer Agent</b>     | <b>State Street Bank and Trust Company</b><br><br>225 Franklin Street<br>Boston, MA 02110                                |
| <b>Independent Auditors</b>             | <b>Ernst &amp; Young LLP</b><br><br>200 Clarendon Street<br>Boston, MA 02116   |
| <b>NYSE Symbol</b>                      | KTF  |
| <b>CUSIP Number</b>                     | 81118R604  |

## Privacy Statement

This privacy statement is issued by Deutsche Investment Management Americas Inc., Deutsche Asset Management, Inc., Scudder Distributors, Inc., Scudder Investor Services, Inc., Scudder Trust Company and the Scudder Funds.

We never sell customer lists or individual client information. **We consider privacy fundamental to our client relationships and adhere to the policies and practices described below to protect current and former clients' information.** Internal policies are in place to protect confidentiality, while allowing client needs to be served. Only individuals who need to do so in carrying out their job responsibilities may access client information. We maintain physical, electronic and procedural safeguards that comply with federal standards to protect confidentiality. These safeguards extend to all forms of interaction with us, including the Internet.

In the normal course of business, clients give us nonpublic personal information on applications and other forms, on our websites, and through transactions with us or our affiliates. Examples of the nonpublic personal information collected are name, address, Social Security number and transaction and balance information. To be able to serve our clients, certain of this client information is shared with affiliated and nonaffiliated third party service providers such as transfer agents, custodians, and broker-dealers to assist us in processing transactions and servicing your account with us. In addition, we may disclose all of the information we collect to companies that perform marketing services on our behalf or to other financial institutions with which we have joint marketing agreements. The organizations described above that receive client information may only use it for the purpose designated by the Scudder Companies listed above.

We may also disclose nonpublic personal information about you to other parties as required or permitted by law. For example, we are required or we may provide information to government entities or regulatory bodies in response to requests for information or subpoenas, to private litigants in certain circumstances, to law enforcement authorities, or any time we believe it necessary to protect the firm.

Questions on this policy may be sent to:

Scudder Investments  
Attention: Correspondence - Chicago  
P.O. Box 219415  
Kansas City, MO 64121-9415

August 2003

**Notes**

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ITEM 2. CODE OF ETHICS.

Not applicable.

ITEM 3. AUDIT COMMITTEE FINANCIAL EXPERT.

Not applicable.

ITEM 4. PRINCIPAL ACCOUNTANT FEES AND SERVICES.

Not applicable.

ITEM 5. [RESERVED]

ITEM 6. [RESERVED]

ITEM 7. DISCLOSURE OF PROXY VOTING POLICIES AND PROCEDURES FOR  
CLOSED-END MANAGEMENT INVESTMENT COMPANIES.

Not applicable.

ITEM 8. [RESERVED]

ITEM 9. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

The primary function of the Nominating and Governance Committee is to identify and recommend individuals for membership on the Board and oversee the administration of the Board Governance Procedures and Guidelines. Shareholders may recommend candidates for Board positions by forwarding their correspondence by U.S. mail or courier service to the Fund's Secretary for the attention of the Chairman of the Nominating and Governance Committee, Two International Place, Boston, MA 02110. Suggestions for candidates must include a resume of the candidate.

ITEM 10. CONTROLS AND PROCEDURES.

(a) The Chief Executive and Financial Officers concluded that the Registrant's Disclosure Controls and Procedures are effective based on the evaluation of the Disclosure Controls and Procedures as of a date within 90 days of the filing date of this report.

During the filing period of the report, fund management identified a significant deficiency relating to the overall fund expense payment and accrual process.

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This matter relates primarily to a bill payment processing issue. There was no material impact to shareholders, fund net asset value, fund performance or the accuracy of any fund's financial statements. Fund management discussed this matter with the Registrant's Audit Committee and auditors, instituted additional procedures to enhance its internal controls and will continue to develop additional controls and redesign work flow to strengthen the overall control environment associated with the processing and recording of fund expenses.

(b) There have been no changes in the registrant's internal control over financial reporting that occurred during the registrant's last half-year (the registrant's second fiscal half-year in the case of the annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal controls over financial reporting.

### ITEM 11. EXHIBITS.

- (a)(1) Certification pursuant to Rule 30a-2(a) under the Investment Company Act of 1940 (17 CFR 270.30a-2(a)) is filed and attached hereto as Exhibit 99.CERT.
- (b) Certification pursuant to Rule 30a-2(b) under the Investment Company Act of 1940 (17 CFR 270.30a-2(b)) is furnished and attached hereto as Exhibit 99.906CERT.