MONTANARO

UK Smaller Companies Investment Trust PLC

Annual Reports and Accounts 2013

The Montanaro UK Smaller Companies Investment Trust PLC ("MUSCIT") was launched in March 1995 and is listed on the London Stock Exchange.

Current Investment Objective

MUSCIT's investment objective is capital appreciation through investing in small quoted companies listed on the London Stock Exchange or traded on the Alternative Investment Market ("AIM") and to achieve relative outperformance of its benchmark, the Numis Smaller Companies Index (excluding Investment Companies) ("NSCI")*. No unquoted investments are permitted.

* The benchmark to 31 March 2013 was the FTSE SmallCap (excluding Investment Companies) Index ("SmallCap").

Contents

Highlights
for the year ended 31 March 2013

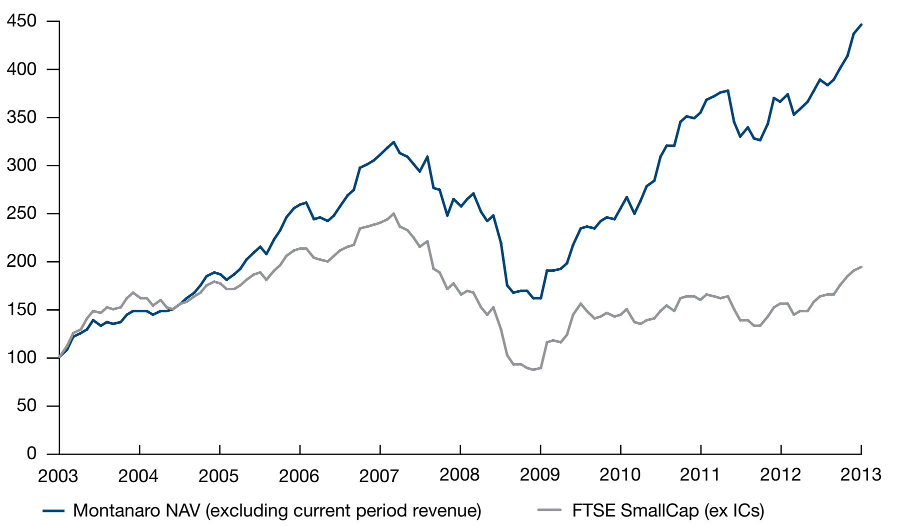
Results

> NAV	+21%	£177m
> NAV (excluding current period revenue)	+22%*	£175m
> Gross assets	+18%	£193m
> Share price	+26%	£146m**
> FTSE SmallCap Index	+24%***	

* Calculated using AIC guidelines.
** Market capitalisation.
*** Excluding Investment Companies.

	Year to 31 March 2013	Year to 31 March 2012
Revenue return on ordinary activities (£000)	2,350	2,480
Movement in capital reserve (£000)	30,916	4,778
Revenue return per Ordinary share	7.02p	7.41p
Dividend per Ordinary share	6.76p	6.76p
Total return per Ordinary share	99.37p	21.68p
	As at 31 March 2013	**As at 31 March 2012**
Ordinary share price	437.00p	348.00p
NAV per Ordinary share	529.19p	436.57p
NAV (excluding current period revenue) per Ordinary share	522.17p	429.17p

NAV Performance vs SmallCap



Source: Montanaro Asset Management Limited/FTSE

Chairman's Statement

Highlights 2013

— In the year to 31 March 2013, the NAV of MUSCIT increased by 21% to 529.19p in comparison with a 24% rise in the SmallCap.

— Since launch, the NAV of MUSCIT has increased by 430% in comparison with a gain of 87% in the SmallCap, outperforming by 343%.

Montanaro's investment focus on companies of the highest quality – "Blue Chip" SmallCap – should reassure investors in these uncertain times.

Background

I am pleased to present the 18th annual report of MUSCIT, which was launched in March 1995. In 1996, the initial investment of £25 million was increased in size through a £30 million "C" share issue. Net assets now stand at £177 million.

An investment trust is an attractive vehicle for shareholders to invest in quoted UK "smaller" companies, which are less well researched and more illiquid than larger, "Blue Chip" companies.

Performance

The NAV (excluding current period revenue) of MUSCIT at 31 March 2013 increased in the year by 21.7% to 522.2p, by 345.1% over ten years and by 429.6% since launch. In comparison, the FTSE SmallCap (excluding Investment Companies ("SmallCap") rose by 24.3% in the year, by 92.9% over ten years and has gained 86.8% since launch.

Since launch, the NAV (excluding current period revenue) of MUSCIT has outperformed the SmallCap by 342.8%.

Discount

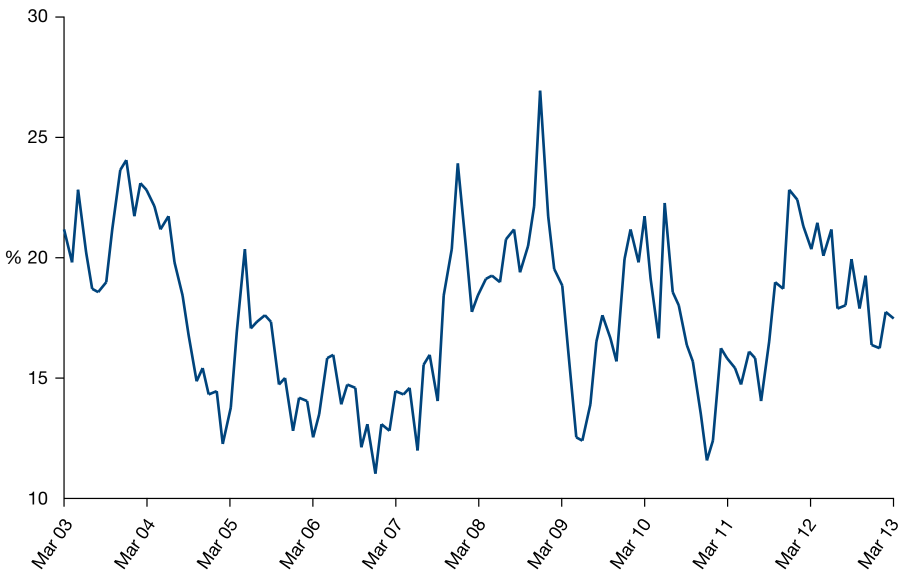
The discount of MUSCIT's share price to NAV (including current period revenue) stood at 17.4% on 31 March 2013 in comparison with a weighted sector average of 12.8%.

Share Buy Backs

The Board is responsible for share buy backs which are undertaken at arm's length by the Manager.

No shares were bought back during the year.

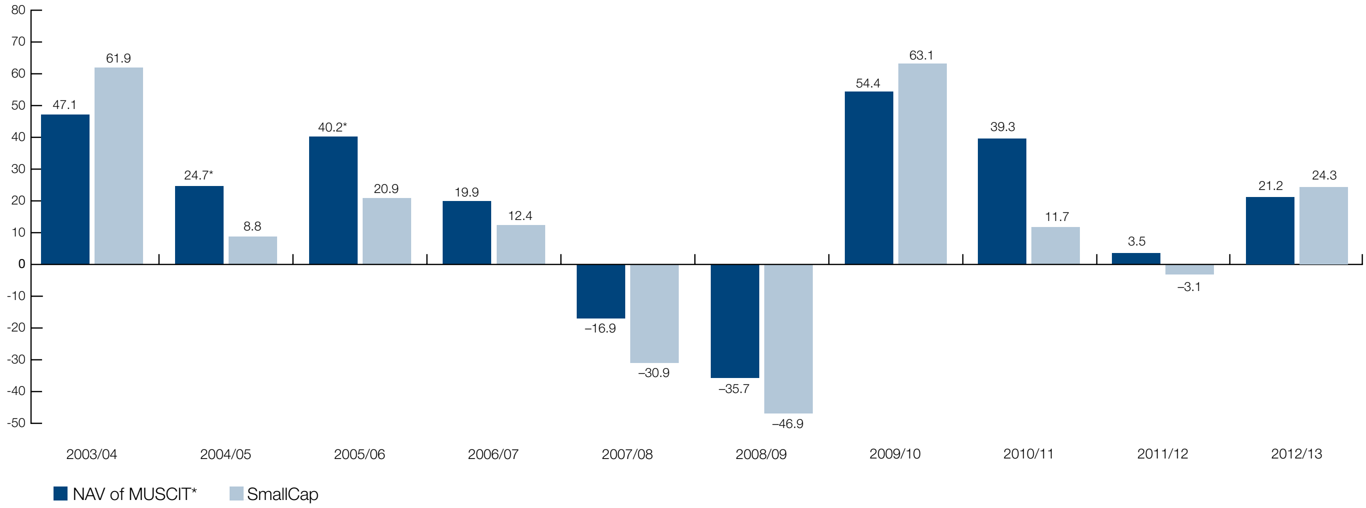
Share Price Discount to NAV



Source: Montanaro Asset Management Limited/Bloomberg

Chairman's Statement continued

Annual NAV Performance vs SmallCap



* Restated for changes to UK GAAP (all other years have not been restated).

Source: Capita Sinclair Henderson Limited/FTSE

Holding Shares in Treasury

Since December 2003, investment trusts have had the right to buy back shares and hold them in Treasury for re-issue at a later date. This has the benefit of improving liquidity as well as retaining the opportunity to enhance the NAV.

The Board has actively and carefully considered the use of Treasury shares and had been among the industry's pioneers. Our policy is to ensure that shareholders receive a tangible benefit above and beyond an enhanced ability to manage the liquidity of the shares of MUSCIT. Shares held in Treasury will only be re-issued at a lower discount than when they were originally purchased and to produce a positive absolute return.

As at 31 March 2013 no shares were held in Treasury.

Gearing

The Board reviews the level of gearing considered appropriate for the Company in discussion with the Manager. One of the benefits of investment trusts is the ability to hold prudent levels of gearing which can enhance investment returns.

The Board has agreed to limit borrowings to 25% of shareholders' funds.

On 19 December 2011 the Company entered into a £15 million revolving credit facility with ING Bank. The facility is available until 19 December 2016. At the same time the Company entered into an interest rate swap effectively fixing the interest rate at 4.29% for the life of the facility. At 31 March 2013, £15 million was drawn down.

During the year, net gearing ranged from 0.3% to 8.3%. At 31 March 2013, net gearing was 1.1% (debt as a % of gross assets) and 1.2% (debt as a % of net assets).

Dividends

MUSCIT's primary focus is on capital growth rather than income. The Board proposes a final dividend of 6.76p per Ordinary share payable on 9 August 2013 to shareholders on the register at the close of business on 28 June 2013. Given the magnitude of the special dividends received last year, the Board has decided to maintain the dividend at the same level.

Directors

There have been no changes to the structure of the Board in the year to 31 March 2013.

Following our internal Board evaluation process and as part of our long-term succession planning we have decided to search for an additional Director with complementary skills to the existing Board members.

Corporate Governance

The Directors have reviewed the recommendations of the AIC Code of Corporate Governance (the "AIC Code") and have implemented procedures where appropriate, such as an annual evaluation of the Board's performance. MUSCIT has complied with the AIC Code throughout the year except where compliance would be inappropriate given the size and nature of the Company. Full disclosure of MUSCIT's compliance with the AIC Code is included in the Directors' Report. The Manager has signed up to the Stewardship Code and has published its voting records on its website.

The use of an internal audit function is not considered necessary given the inherent segregation of duties and internal controls.

Alternative Investment Fund Managers' Directive

The Board has been monitoring the progression of the AIFM Directive and has been actively discussing options with providers. This will ensure that the Company will be able to comply with its requirements when the Directive is fully implemented in July 2014.

Continuation Vote

Under the Articles the Directors will propose a Resolution at this year's Annual General Meeting to remove the obligation that they put a Resolution to Shareholders at the Annual General Meeting in 2014 to wind up the Company. If passed, this will allow the Company to continue as an investment trust for a further five years. This Resolution is similar to the one passed by Shareholders in 2009 and one which the Board recommends all Shareholders vote in favour.

Chairman's Comment

The past year has been particularly good for investors in UK Small and Mid Cap companies, with rises of 24.3% and 20.7% in the SmallCap and FTSE 250 indices. This compares to an increase in the FTSE 100 Index of 11.2%. The second half of the Company's financial year witnessed a marked recovery in lower quality, "value" companies – the opposite of where MUSCIT invests – which largely explains the modest underperformance of MUSCIT against its benchmark (for only the fourth occasion in 18 years). Nonetheless, investors enjoyed NAV returns of 21.2% and saw the MUSCIT share price increase by 25.6%.

In recent years, Montanaro has found fewer stocks meeting their exacting criteria within the SmallCap and Fledgling markets, which represent an ever shrinking proportion of UK stocks. After consulting several of the Company's larger shareholders, the Board considered that the benchmark should be changed from the SmallCap Index to the Numis Smaller Companies Index (excluding Investment Companies) ("NSCI") from 1 April 2013. The goal was to introduce a benchmark that more closely reflected the actual structure of the portfolio, 82% of which falls within the NSCI. This decision was conveyed to shareholders in the half-yearly report. MUSCIT would have outperformed this broader new benchmark last year, which rose by 19.9%.

Despite the change in benchmark, the investment strategy and focus on high quality, growing UK smaller companies remains unchanged. Montanaro firmly believes that thorough research at an individual company level can provide opportunities for long-term outperformance. However, the appetite for passive strategies and Exchange Traded Funds ("ETF") has continued to grow and by the end of 2011, 12% of professionally managed assets around the world were run passively, compared to 7% two years earlier (source: Boston Consulting Group).

Two clear effects of increased indexation have been a fall in average holding periods for equities and a declining interest for individual company fundamentals. The reduction in holding periods is perhaps best exemplified by "SPY", the world's largest ETF, which mirrors the S&P 500 Index and has an average holding period of less than a week. Meanwhile, the decline in interest for company fundamentals is implicit in the rise of passive investments – no-one buys an index tracker because they have analysed every constituent company and found them all to be undervalued. Both of these offer opportunities for active, long-term and bottom up investors.

Montanaro, on the other hand, does analyse every company it holds. In the knowledge that earnings drive the valuations of companies on the stock market, it has assembled a large, multi-national, specialist team based in the United Kingdom to ensure that it understands a company's fundamentals better than others. This is the vital information edge that differentiates bottom-up investment managers. That it can buy or sell stocks to those who have far more transient reasons for investing is an added benefit.

If the trend toward passive investing continues, the opportunity to add value by performing the work that others cannot or do not carry out will increase. Montanaro's focus on companies of the highest quality – "Blue Chip" SmallCap – should reassure investors in these uncertain times. I believe that investors can look forward to the future of MUSCIT with confidence.

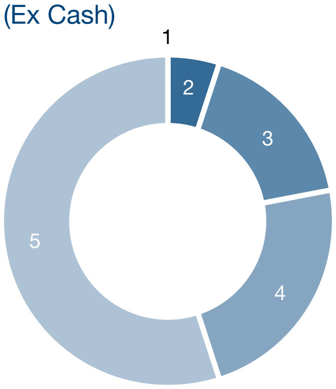
DAVID GAMBLE
Chairman
19 June 2013

Manager's Report

Highlights 2013

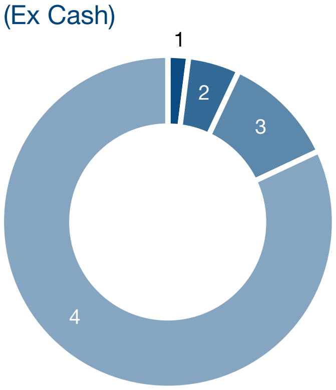
– MUSCIT is well-positioned to benefit from a return of investor appetite for the highest quality quoted small companies. We look forward to the coming year with confidence although we do not expect to see a repeat of the excellent returns of last year.

Breakdown by Market Cap (Ex Cash)



1	£50–£100m	0%
2	£100–£200m	5%
3	£200–£300m	17%
4	£300–£600m	23%
5	>£600m	55%

Breakdown by Index (Ex Cash)



1	FTSE 100	2%
2	UK AIM	5%
3	FTSE 250*	11%
4	Numis Smaller Companies	82%

Manager's Review

The change at the helm of the European Central Bank ("ECB") in November 2011 had a salutary effect on Europe's stock markets. Mario Draghi may one day be remembered for changing the course of history with his statement in July 2012: "Within our mandate, the ECB is ready to do whatever it takes to preserve the Euro, and believe me, it will be enough". This, combined with toned down rhetoric from Germany and the creation of the European Stability Mechansim, reduced the tail risk for the UK's largest export partner, whilst economic recovery in the US provided the impetus required for positive equity markets.

However, the domestic UK economy remained sluggish with little to suggest a resumption of sustainable GDP growth. A lack of fiscal stimulus left the heavy lifting to the Bank of England, which duly kept monetary policy exceptionally loose. The resulting weakness in sterling provided some comfort to exporters.

Fiscal 2012/13 proved to be an excellent year for UK SmallCap: the SmallCap Index rose by 24.3% whereas the FTSE All-Share Index rose by just 12.6%. In comparison, the NAV of MUSCIT rose by 21.2%.

Outlook

As the financial year to 31 March 2013 drew to an end, UK equities had enjoyed ten consecutive months of positive returns. In less than a year, extreme pessimism had been replaced by broad based optimism. All the ingredients are now in place for a recovery in M&A activity. Companies continue to sit on large cash balances which yield negative real returns, capital is cheap for sound borrowers and confidence is improving. We expect there to be increasing pressure to either invest or return some of this cash to investors.

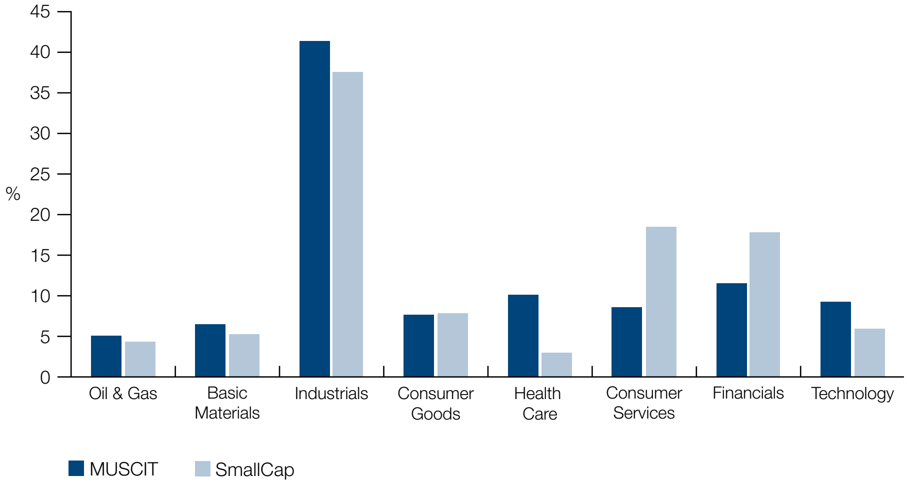
We entered 2013 expecting yet another strong January, reflected in gearing of 8.3% at 31 December 2012. However, in a pattern similar to the previous year, as the quarter has progressed we have adopted an increasingly cautious stance – stock markets simply do not go up in a straight line forever. We would therefore not be surprised to see some profit-taking in the first half of 2013 and would welcome a correction. However, the foundations of the long-term equity bull market are still intact.

* represents those holdings that are in the FTSE 250 and are above the threshold for Numis Smaller Companies holdings.

There are signs that the reign of Value over Growth that began during the summer of 2012 may also be drawing to an end. In a world of low and scarce growth and macro-economic uncertainties, investors are likely to continue to pay a premium for visible and secure growth.

MUSCIT is well positioned to benefit from a return of investor appetite for the highest quality UK quoted small companies. We look forward to the coming year with confidence, although we do not expect to see a repeat of the exceptional returns of last year.

Sector Distribution vs SmallCap



Montanaro Asset Management Limited
19 June 2013

Ten Largest Holdings
as at 31 March 2013

35%
of the portfolio

Dignity PLC
General Retailers

The UK's largest provider of funeral-related services.

£7.10m	4.0%	£814m
Value	Portfolio	Market cap

Dechra Pharmaceuticals PLC
Pharmaceuticals and Biotechnology

An international veterinary pharmaceutical business.

£6.75m	3.8%	£653m
Value	Portfolio	Market cap

Brammer PLC
Support Services

A pan-European distributor of maintenance, repair and overhaul components.

£6.50m	3.6%	£435m
Value	Portfolio	Market cap

Genus PLC
Pharmaceuticals and Biotechnology

A world leader in bovine and porcine genetics.

£6.31m	3.5%	£957m
Value	Portfolio	Market cap

Domino Printing Sciences PLC
Electronic and Electrical Equipment

A provider of total coding and printing solutions.

£6.20m	3.5%	£715m
Value	Portfolio	Market cap

Devro PLC

Food Producers

Producer of manufactured casings for the food industry.

Value	Portfolio	Market cap
£6.14m	3.4%	£582m

Domino's Pizza PLC

Travel and Leisure

The UK's leading franchise pizza delivery company.

Value	Portfolio	Market cap
£6.03m	3.4%	£987m

EnQuest PLC

Oil and Gas Producers

An independent oil and gas development and production company.

Value	Portfolio	Market cap
£5.96m	3.3%	£1,153m

Fidessa Group PLC

Software and Computer Services

Provider of trading, investment and information solutions for the world's financial community.

Value	Portfolio	Market cap
£5.84m	3.2%	£725m

James Fisher PLC

Industrial Transportation

A provider of specialist services to the marine, oil and gas industries worldwide.

Value	Portfolio	Market cap
£5.43m	3.0%	£518m

Investment Portfolio
as at 31 March 2013

Holding	Sector	Value £000	Market cap £m	% of portfolio 31 March 2013	% of portfolio 31 March 2012
Dignity	General Retailers	7,094	814	4.0	2.7
Dechra Pharmaceuticals	Pharmaceuticals and Biotechnology	6,746	653	3.8	2.2
Brammer	Support Services	6,497	435	3.6	3.3
Genus	Pharmaceuticals and Biotechnology	6,312	957	3.5	3.4
Domino Printing Sciences	Electronic and Electrical Equipment	6,198	715	3.5	3.0
Devro	Food Producers	6,143	582	3.4	3.5
Domino's Pizza	Travel and Leisure	6,025	987	3.4	2.5
EnQuest	Oil and Gas Producers	5,959	1,153	3.3	3.0
Fidessa Group	Software and Computer Services	5,835	725	3.2	2.8
James Fisher	Industrial Transportation	5,434	518	3.0	2.8
RPS Group	Support Services	5,346	588	3.0	2.8
Shaftesbury	Real Estate/Real Estate Investment Trusts	5,233	1,464	2.9	2.6
Consort Medical	Health Care Equipment and Services	5,171	227	2.9	2.6
Senior	Aerospace and Defence	5,078	991	2.8	–
Fenner	Industrial Engineering	5,057	754	2.8	2.9
Victrex	Chemicals	4,980	1,406	2.8	3.6
Dialight	Electronic and Electrical Equipment	4,843	416	2.7	3.4
NCC Group	Software and Computer Services	4,738	293	2.6	3.0
Aveva Group	Software and Computer Services	4,641	1,541	2.6	2.0
Renishaw	Electronic and Electrical Equipment	4,607	1,338	2.6	2.2
Twenty largest holdings		**111,937**		**62.4**	
Mears Group	Support Services	4,272	336	2.4	2.2
Brewin Dolphin	General Financials	4,130	523	2.3	2.4
Oxford Instruments	Electronic and Electrical Equipment	3,972	942	2.2	2.9
Ricardo	Support Services	3,964	218	2.2	2.3
Latchways	Support Services	3,789	121	2.1	2.5
Carclo	Chemicals	3,383	259	1.9	1.9
M.P. Evans Group	Food Producers	3,366	280	1.9	1.9
Croda International	Chemicals	3,292	3,724	1.8	2.5
Rotork	Industrial Engineering	3,194	2,521	1.8	–
James Halstead	Construction and Materials	3,121	614	1.7	1.5
Ocean Wilson Holdings	Industrial Transportation	3,120	368	1.7	2.4
Premier Oil	Oil and Gas Producers	3,110	2,057	1.7	1.9
Helical Bar	Real Estate/Real Estate Investment Trusts	2,959	280	1.7	1.6
Rathbone Brothers	General Financials	2,918	672	1.6	–
AG Barr	Beverages	2,861	636	1.6	2.7
Clarkson	Industrial Transportation	2,721	295	1.5	1.5
Brooks Macdonald Group	General Financials	2,476	188	1.4	1.5
Wilmington Group	Media	1,988	137	1.1	0.8
Primary Health Properties	Real Estate/Real Estate Investment Trusts	1,986	252	1.1	1.3
Telecity Group	Software and Computer Services	1,626	1,825	0.9	–
Marshalls	Construction and Materials	1,625	246	0.9	0.9
Halma	Electronic and Electrical Equipment	1,552	1,956	0.9	–
Cranswick	Food Producers	1,282	478	0.7	–
Albemarle & Bond Holdings	General Financials	802	119	0.5	0.9
Total portfolio		**179,446**		**100.0**	

Analysis of Investment Portfolio by Industrial or Commercial Sector

as at 31 March 2013

Sector	% of portfolio	% of FTSE SmallCap
Oil and Gas Producers	5.0	1.6
Oil Equipment, Services and Distribution	–	2.7
Oil and Gas	**5.0**	**4.3**
Chemicals	6.5	1.2
Industrial Metals	–	1.3
Mining	–	2.7
Basic Materials	**6.5**	**5.2**
Construction and Materials	2.6	4.7
Aerospace and Defence	2.8	0.5
General Industrials	–	0.6
Electronic and Electrical Equipment	11.9	4.9
Industrial Engineering	4.6	3.7
Industrial Transportation	6.2	2.9
Support Services	13.3	20.2
Industrials	**41.4**	**37.5**
Automobiles and Parts	–	0.2
Beverages	1.6	–
Food Producers	6.0	4.3
Household Goods	–	2.6
Leisure Goods	–	0.8
Consumer Goods	**7.6**	**7.9**
Health Care Equipment and Services	2.9	1.5
Pharmaceuticals and Biotechnology	7.3	1.4
Health Care	**10.2**	**2.9**
General Retailers	4.0	6.5
Media	1.1	6.4
Travel and Leisure	3.4	5.6
Consumer Services	**8.5**	**18.5**
Life and Non-life Insurance	–	2.5
Real Estate/Real Estate Investment Trusts	5.7	14.0
General Financials	5.8	1.3
Financials	**11.5**	**17.8**
Software and Computer Services	9.3	4.4
Technology Hardware and Equipment	–	1.5
Technology	**9.3**	**5.9**
Total	**100.0**	**100.0**

The investment portfolio comprises 44 listed UK equity holdings including 4 holdings totalling £9,766,000 (representing 5.4% of the portfolio) traded on the Alternative Investment Market ("AIM").

Board of Directors

MUSCIT has a highly experienced Board of Directors with extensive knowledge of investment management and investment trusts

David Gamble – Chairman

David Gamble was appointed a Director on 19 November 2004 and became Chairman of MUSCIT on 28 January 2005. David is also chairman of Dunedin Enterprise Investment Trust PLC, a non-executive director of IBM Pension Trustees Limited, VenCap International plc, Polar Capital Technology Trust plc and a member of the investment committee of the BBC pension Trust. He retired as chief executive of British Airways Pension Investment Management in 2004.

Roger Cuming

Roger Cuming has been in the investment industry for over 35 years. He is Head of Investments for Reliance Mutual Insurance Society Limited. Appointed a Director on 5 June 2009, he is a significant investor in closed and open-ended investments of all types.

Kathryn Matthews

Kathryn Matthews was appointed on 1 April 2010 Kathryn has worked in the investment management industry since 1981. Formerly, she was the chief investment officer of Asia Pacific (ex Japan) for Fidelity International. Prior to that she held senior appointments with William M Mercer, AXA Investment Managers, Santander Global Advisers and Baring Asset Management. She is a non-executive director of Rathbone Brothers plc, Hermes Fund Managers Limited and Fidelity Asian Values Plc. She has also been appointed as a non-executive director for JP Morgan Chinese Investment Trust Plc and Aperam. She is also chairman of the Investment Committee of Royal London Group.

Michael Moule

Michael Moule formerly specialised in managing investment trusts for Henderson and Touche Remnant. Appointed as a Director on 28 January 2005, he has extensive experience of UK and overseas equity markets having worked with investment trusts since 1967. He is also chairman of Polar Capital Technology Trust plc, a non-executive director of The European Investment Trust plc and is a member of the investment committee of the British Heart Foundation and the Open University.

Principal Advisers

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Montanaro UK Smaller Companies Investment Trust PLC
Registered in England and Wales No. 3004101

An investment company as defined under Section 833 of the Companies Act 2006.

Directors' Report

The Chairman's Statement forms part of the Directors' Report

The Directors' present their Annual Report and financial statements for the year ended 31 March 2013.

Business Review

The Business Review has been prepared in accordance with the Companies Act 2006 and should be read in conjunction with the Chairman's Statement on pages 3 to 5 and the Manager's Report on pages 6 and 7.

INTRODUCTION

The purpose of the Business Review is to provide an overview of the business of the Company by:

- Analysing development and performance using appropriate key performance indicators ("KPIs").
- Outlining the principal risks and uncertainties affecting the Company.
- Describing how the Company manages these risks.
- Explaining the future business plans of the Company.
- Setting out the Company's environmental, social and ethical policy.
- Providing information about persons with whom the Company has contractual or other arrangements which are essential to the business of the Company.
- Outlining the main trends and factors likely to affect the future development, performance and position of the Company's business.

REVIEW OF THE DEVELOPMENT AND PERFORMANCE OF THE BUSINESS AND POSITION OF MUSCIT

A description of MUSCIT's activities and a review of the development and performance of the business during the year is given in the Chairman's Statement and in the Manager's Report.

MUSCIT is a closed-ended investment trust listed on the London Stock Exchange with registration number 3004101. It has applied for, and been granted, approval from HM Revenue & Customs as an investment trust under s1158/1159 of the Corporation Tax Act 2010 ("1158/1159") for the year ended 31 March 2013. One of the criteria for continued compliance is that MUSCIT is required to distribute a minimum of 85% of all its income as dividend payments. The Company could lose its investment trust company status if it became a close company at any time during the accounting period.

MUSCIT will be treated as an investment trust company for each subsequent accounting period, subject to there being no subsequent serious breaches of the conditions for approval. Failure by MUSCIT to satisfy the new requirements could result in it being subject to capital gains tax arising on the sale of investments. Further details on the operation of investment trusts can be obtained from the Association of Investment Companies on their website at www.theaic.co.uk.

New rules introduced by HM Revenue and Customs removed the maximum holding in any one investment of 15% and replaced this with a risk diversification approach. The Board has considered this and agreed that the Company's Investment Policy offers suitable risk diversification.

MUSCIT is also an investment company as defined in Section 833 of the Companies Act 2006. The current portfolio of MUSCIT is such that its shares are eligible for inclusion in an ISA up to the maximum annual subscription limit and the Directors expect this eligibility to be maintained.

MUSCIT's investment objective is capital appreciation (rather than income) achieved by investing in small quoted companies listed on the London Stock Exchange or traded on the Alternative Investment Market ("AIM") and to achieve relative outperformance of its benchmark, the FTSE SmallCap (excluding Investment Companies) Index ("SmallCap"). From 1 April 2013 the Company adopted the Numis Smaller Companies Index (excluding Investment Companies) ("NSCI") as its benchmark.

No unquoted investments are permitted.

The Company seeks to achieve its investment objective and diversify risk by investing in a portfolio of quoted UK small companies. At the time of initial investment, a potential investee company must be profitable and smaller than the largest constituent of the NSCI which represents the smallest 10% of the UK Stock Market by value. At the start of January 2013, the largest company in the NSCI had a market capitalisation of over £2.3 billion. The Manager focuses on the smaller end of this Index.

The Manager will normally limit any one holding to a maximum of 4% of the Company's investments. The portfolio weighting of each investment is closely monitored to reflect the underlying liquidity of the particular company; smaller investments are made in less liquid companies. AIM exposure is also closely monitored by the Board and is limited to 30% of total investments, with Board approval required for exposure above 25%. At 31 March 2013 this was 5.4% (2012: 7.9%).

The Manager is focused on identifying high quality niche companies operating in growth markets. This typically leads to investment in companies that enjoy high barriers to entry, pricing power, a sustainable competitive advantage and strong management teams. The portfolio is constructed on a "bottom up" basis and there are no sector constraints.

The Board, in consultation with the Manager, is responsible for determining the gearing strategy for the Company. Gearing is used to enhance returns when the timing is considered appropriate. The Company currently has a credit facility of £15 million through ING Bank. The Board has agreed to limit borrowings to 25% of shareholders' funds.

SHARE CAPITAL

There are currently 33,475,958 Ordinary 10p shares in issue (2012: 33,475,958) none of which are held in Treasury (2012: nil). Holders of Ordinary shares have unrestricted voting rights of one vote per share at all general meetings of the Company.

DESCRIPTION OF PRINCIPAL RISKS ASSOCIATED WITH MUSCIT

The Board carefully considers the principal risks for MUSCIT and seeks to manage these risks through continual and regular review, policy setting, compliance with and enforcement of contractual obligations and active communication with the Manager, the Administrator and shareholders.

The Board applies the principles detailed in the recommendations of the AIC Code as described in the Chairman's Statement. Details of MUSCIT's internal controls may be found in the Corporate Governance section on page 20.

Mitigation of the principal risks is sought and achieved in many ways as shown in italics below:

Investment Manager: Montanaro has been the Manager of MUSCIT since its launch in 1995. The success of MUSCIT and its strong performance is largely attributable to Montanaro. Should the current Manager not be in a position to continue its management of the Company, performance may be impacted.

The Board meetings are attended by the Manager. Montanaro has a large, multi-national specialist team based in the UK. Succession planning within Montanaro and recruitment of personnel are closely monitored by the Board.

Investment & Strategy: MUSCIT may underperform its benchmark as a result of poor stock selection, sector allocation or as a result of being geared in a falling market.

The Manager meets regularly with the Board to discuss portfolio performance and strategy, and provides the Board and shareholders with monthly reports. The portfolio is well diversified thereby spreading investment risk and reducing stock specific risk. The Board receives and reviews monthly a report of all transactions and, through the forum of its Management Engagement Committee, formally reviews the performance of the Manager on an annual basis.

Gearing: one of the benefits of closed-end investment trusts is the ability to use borrowings which can enhance returns in a rising stock market. However, gearing exacerbates movements in the net asset value both positively and negatively and will exaggerate declines in net asset value when prices of quoted UK small companies are falling.

The Board monitors and discusses with the Manager the appropriate level of gearing of MUSCIT at each Board meeting. The Board agreed with the Manager to take out a five year borrowing commitment to December 2016. The Board monitors and discusses with the Manager the appropriate level of gearing for the portfolio and whether the cash balances held are appropriate.

Portfolio Liquidity: as with all small company investment trusts, there are times when the liquidity of the underlying portfolio is poor, such as when small companies are out of favour or during periods of adverse economic conditions. The Manager focuses on "smaller" companies where the opportunities may be more attractive but this can increase overall underlying illiquidity. This may result in the Manager being unable to buy or sell individual holdings within the portfolio. In addition, this may impact the discount of MUSCIT's share price to the net asset value of the portfolio.

One of the benefits of investment trusts is that generally the Manager is not forced to buy or sell individual holdings at inopportune times. The Manager constantly reviews the underlying liquidity of the portfolio, which is well-diversified. Particular attention is paid to the AIM holdings, with the Manager providing the Board with liquidity reports at every meeting. Montanaro deals with a wide range of brokers to enhance its ability to execute and minimise liquidity risk.

Liquidity of MUSCIT Shares: as with many small company investment trusts, there are times when the liquidity of the shares of MUSCIT is low. In the case of MUSCIT, many of the shareholders are large financial institutions with a long-term investment horizon. Unlike other investment trusts where private individuals form a larger part of the share register, this may result in fewer shares being traded in MUSCIT on a daily basis and make it difficult at times for investors to buy or sell shares of MUSCIT.

The Manager is encouraged by the Board to market the strong investment story of MUSCIT to other potential new investors. The goal is to widen the shareholder base to enhance liquidity. In addition, the ability to buy back shares to be held in Treasury for subsequent re-issue enhances the liquidity of MUSCIT's shares.

Discount Volatility: as with all small company investment trusts, the discount can fluctuate significantly both in absolute terms and relative to its peer group.

The Board actively monitors and seeks to manage the discount of MUSCIT and is responsible for share buy backs or issuance from Treasury. Share buy backs may help to reduce the discount.

During the year and up to the date of this report, MUSCIT has not used the authority granted at the Annual General Meeting held in 2012 to make market purchases of up to 5,018,046 Ordinary shares. No Ordinary shares are currently held in Treasury.

The Board encourages the Manager to market MUSCIT to new investors to increase demand for its shares, which may help to increase liquidity and reduce the discount.

Regulatory: a breach of s1158/1159 might lead to MUSCIT being subject to capital gains tax. A breach of the rules of the London Stock Exchange might result in censure by the FCA and/or suspension of MUSCIT's listing on the London Stock Exchange.

The Board has agreed a service level agreement with the Manager which includes active and regular review of compliance with s1158/1159 and compliance with the Company's published Investment Policy. The Board regularly reviews the share register to ensure it does not become a close company. During the year under review the Administrator reviewed compliance with FCA and London Stock Exchange Rules. This is reviewed at each Board meeting.

The Board has been monitoring the progression of the AIFM Directive and has been actively discussing options with providers. This will ensure that the Company will be able to comply with its requirements when the Directive is fully implemented in July 2014.

Operational: if the Administrator's operational procedures proved deficient and its core accounting systems failed, accounting errors might occur resulting in inaccurate net asset valuations, performance data and possibly a qualified audit report and/or loss of s1158/1159 status.

The Board monitors operational issues monthly and reviews them in detail at each Board meeting.

Directors' Report continued

Financial: inappropriate accounting policies or failure to comply with current or new Accounting Standards might lead to a breach of regulations and/or loss of investment trust company status.

The Board monitors financial issues monthly and reviews them in detail at each Board meeting.

Banking: a breach of MUSCIT's loan covenants might lead to funding being summarily withdrawn and investment holdings potentially being sold at a time of poor liquidity.

The main financial covenants to which the Company is subject in respect of the ING Bank N.V. revolving credit facility require it to ensure that total borrowings will not exceed 30% of the adjusted NAV at any time and that the adjusted NAV does not fall below £39,000,000 at any time.

The Board monitors compliance with banking covenants monthly and reviews them with the Administrator and Manager at each Board meeting.

The Company has entered into an interest rate swap agreement, the fair value of this is disclosed in note 15 of the financial statements.

Reputational: inadequate or deficient controls of the Administrator or Manager or other third-party providers might result in breaches of regulations and damage the trust and confidence of shareholders in MUSCIT, leading to a widening of the discount.

The Board continually monitors and reviews issues that may impact the standing of MUSCIT.

Failure to keep current and potential investors informed of the Company's performance and development could result in fewer shares being traded in MUSCIT on a daily basis and also lower investor confidence.

The Board and Manager maintain clear and frequent communication with shareholders and potential investors and are both happy to meet with shareholders.

Company Viability: through falling NAV, or a reduction in the size of the Company through purchases of its own shares, the size of the Company could make its continuing existence unviable in the opinion of investors.

The Board actively monitors and seeks to manage the discount of MUSCIT and is responsible for share buy backs for cancellation or holding in Treasury. The resultant size of the Company is an important consideration of the decision to undertake buy backs.

A description of MUSCIT's system for reviewing its risk environment is shown in the Directors' Report on page 14.

ANALYSIS OF PERFORMANCE USING KEY PERFORMANCE INDICATORS

Results and Dividends: the results for the year are as set out in the Income Statement on page 26. The Directors recommend that a final dividend of 6.76p (2012: final 6.76p) per Ordinary share, amounting to £2,263,000 (2012: final £2,263,000) be paid on 9 August 2013 to shareholders on the share register at the close of business on 28 June 2013.

Net Asset Value: the NAV per Ordinary share, including revenue reserves, at 31 March 2013 was 529.19p (2012: 436.57p).

The Board reviews performance by reference to a number of KPIs and considers that the most relevant KPIs are those that communicate the financial performance and strength of the Company as a whole.

The Board and the Manager monitor the following KPIs:

- the NAV over the previous ten years and since launch relative to the benchmark as disclosed in the Chairman's Statement;
- the level of discount; and
- the Ongoing Charges which were:

	2013	2012
Ongoing Charges	1.3%	1.3%
Performance fees	–	0.6%
Finance costs	0.4%	0.2%
Total Ongoing Charges plus performance fees and finance costs	1.7%	2.1%

Further KPIs are those which show the Company's position in relation to the investment trust tests which it is required to meet and maintain its investment trust status.

SOCIALLY RESPONSIBLE INVESTMENT

The Company has no employees and the Board is comprised entirely of non-executive Directors. Day-to-day management of the Company's business is undertaken by Montanaro as the Investment Manager.

Montanaro receives independent third party corporate governance research and will usually vote in line with International Corporate Governance Network policies. Where possible, it engages with management teams before an AGM or EGM prior to any decision to abstain or vote against a board's recommendation.

In carrying out business with its suppliers, the Company aims to conduct itself responsibly, ethically and fairly.

Securities Carrying Voting Rights

The following information is disclosed in accordance with Large and Medium-Size Companies and Groups (Accounts and Reports) Regulations 2008 and DTR 7.2.6 of the FCA Disclosure and Transparency Rules.

- The Company's capital structure and voting rights are disclosed on page 14.
- Details of the substantial shareholders in the Company are disclosed on page 21.
- The Board's current powers to buy back shares are stated on page 15 and proposals for their renewal are disclosed on page 21.
- There are no restrictions concerning the transfer of securities in the Company; no special rights with regard to control attached to securities; no agreements between holders of securities regarding their transfer known to the Company; and no agreements which the Company is party to that might affect its control following a successful takeover bid.

Management Agreement

The Company's investments are managed by Montanaro Asset Management Limited under a management agreement dated 30 June 1998, amended on 10 June 1999, 31 July 2001 and 2 November 2009. The management fee is comprised of two components: a fixed fee of 1/12 of 1% of the gross assets of MUSCIT, payable monthly in arrears, and a performance fee of 0.1% of the gross assets of MUSCIT for each 1% outperformance (or part thereof) of MUSCIT's NAV, adjusted for dividends paid, against the SmallCap over the financial year, subject to a maximum of 0.5% of the gross assets calculated at the end of the financial year. A performance fee is only payable in respect of any financial year of MUSCIT in the event that the NAV of MUSCIT as at the end of that financial year (as derived from the audited financial statements of MUSCIT and adjusted for dividends subsequently paid): (i) is not less than the NAV of MUSCIT as at the end of the immediately preceding financial year in which the Manager was entitled to a performance fee; and (ii) has outperformed MUSCIT's benchmark during the year by at least 2%. (In such event, the performance fee would be payable in respect of each 1% (or part thereof) outperformance of the benchmark).

In the year to 31 March 2012, being the last financial year in which the Manager was entitled to a performance fee, the Company achieved a NAV of 429.81p (after adjusting for dividends subsequently paid of 6.76p). No performance fee is payable in respect of the year ended 31 March 2013 (2012: £812,000).

Following the adoption of the new benchmark on 1 April 2013, the performance fee will be amended to refer to the NSCI.

Termination of the management agreement is subject to 12 months notice in writing by either party.

On termination of the management agreement in certain circumstances, the Manager will be entitled to a termination fee of 1% of gross assets of MUSCIT as at close of business on the last day of the calendar month immediately preceding the effective date of termination of the agreement.

The Board keeps under review the performance of the Manager. In the opinion of the Directors, the continuing appointment of the Manager on the terms agreed is in the interests of shareholders as a whole. Among the reasons for this view is the investment performance of MUSCIT relative to that of the markets in which MUSCIT invests and the depth and experience of the research capability of Montanaro.

Directors

The Directors in office as at the date of this report together with their biographies are shown on page 12.

Directors' Beneficial and Family Interests

The interests of the current Directors and their families in the voting rights of MUSCIT are set out below:

	As at 31 March 2013 No. of shares	As at 1 April 2012 No. of shares
David Gamble	10,000	10,000
Roger Cuming	5,000	5,000
Kathryn Matthews	1,500	1,500
Michael Moule	10,000	10,000

There have been no changes to the above holdings between 31 March 2013 and the date of this Annual Report. None of the Directors nor any persons connected with them had a material interest in any of MUSCIT's transactions, arrangements or agreements during the year.

Corporate Governance

COMPLIANCE WITH THE PROVISIONS OF THE AIC CODE OF CORPORATE GOVERNANCE

The Board of MUSCIT has considered the principles and recommendations of the AIC Code of Corporate Governance dated 2010 ("AIC Code") by reference to the AIC Corporate Governance Guide for Investment Companies ("AIC Guide"). The AIC Code, as explained by the AIC Guide, addresses all the principles set out in the UK Corporate Governance Code, as well as setting out additional principles and recommendations on issues that are of specific relevance to MUSCIT.

The Board considers that reporting under the principles and recommendations of the AIC Code and by reference to the AIC Guide will provide better information to shareholders.

During the year the Company has complied with the recommendations of the AIC Code and the relevant provisions of the UK Corporate Governance Code 2010, except where compliance would be inappropriate given the size and nature of the Company.

As set out in the AIC Guide accompanying the AIC Code, the Board considers that the UK Code's recommendations with respect to the role of the chief executive, executive directors' remuneration (there are no executive directors) and the need for an internal audit function (not considered necessary given the inherent segregation of duties and internal controls) are not relevant to the Company's circumstances as an externally managed investment trust. The Company has therefore not reported further in respect of these provisions.

Mr Cuming is currently the Senior Director of MUSCIT. The Board considers that Mr Cuming is ideally suited to performing the role of Senior Director. The structure of the Board is such that it is considered unnecessary to identify a Senior Independent non-executive Director.

A copy of the AIC Code and the AIC Guide can be obtained via the AIC's website: www.theaic.co.uk. A copy of the UK Corporate Governance Code can be obtained at: www.frc.org.uk.

Directors' Report continued

ATTENDANCE AT BOARD AND COMMITTEE MEETINGS

	Board		Audit Committee		Remuneration Committee		Management Engagement Committee		Nomination Committee	
	Number of meetings held	Number of meetings attended	Number of meetings held	Number of meetings attended	Number of meetings held	Number of meetings attended	Number of meetings held	Number of meetings attended	Number of meetings held	Number of meetings attended
David Gamble	6	6	2	2	1	1	1	1	1	1
Roger Cuming	6	6	2	2*	1	1*	1	1*	1	1*
Kathryn Matthews	6	6	2	2	1	1	1	1	1	1
Michael Moule	6	6	2	2	1	1	1	1	1	1

* attended by invitation.

The Company holds at least four Board meetings each year at which the Directors review MUSCIT's investments and all other important issues to ensure control is maintained over the Company's affairs. During the year ended 31 March 2013, six Board meetings were held, one of which was a full-day session devoted entirely to reviewing strategic matters.

BOARD RESPONSIBILITIES

Throughout the year, the Board comprised four non-executive Directors. The Board has considered the independent status of each Director under the AIC Guide and has determined that all, with the exception of Mr Cuming, are independent. Mr Moule as chairman and Mr Gamble as a non-executive director, sit on the board of Polar Capital Technology Trust. Their fellow Directors do not consider this to affect their ability to act independently and each Director is deemed independent in outlook and judgement. The Chairman is free from any conflicts of interest and does not have any significant commitments other than those disclosed in his biography on page 12.

The Board has reviewed the fact that Mr Cuming is a senior member of a company that has a shareholding in the Company. The Board is satisfied that internal controls make sure that voting and control of this shareholding is not influenced by Mr Cuming. The Board also believes that the contribution of Mr Cuming is entirely aligned to the overall success of the Company. However, the Board has agreed that Mr Cuming may not be considered independent.

The Board has formalised the arrangements under which Directors, in the furtherance of their duties, may take independent professional advice. The Company also maintains Directors' and Officers' liability insurance.

There were no third party indemnity provisions over the course of the year.

Other than their letters of appointment, none of the Directors has a contract of service with MUSCIT nor has there been any contract or arrangement between MUSCIT and any Director at any time during the year. These letters of appointment are available for inspection on request to the Company Secretary.

The Company has neither executive directors nor employees. However, the Board has engaged external companies to undertake the investment management, administrative and custodial activities of MUSCIT. Clear, documented contractual arrangements are in place between MUSCIT and these firms that define the areas where the Board has delegated functions to them. Further details of the investment management agreement are given on page 17.

A schedule of matters specifically reserved to the Board for its decision has been adopted. These reserved matters include the approval of annual and half-yearly accounts, the approval of dividends, the approval of press releases and circulars, Board appointments and removals and the membership of Committees. Decisions regarding gearing and the capital structure of MUSCIT (including share buy backs and Treasury share transactions) are also taken by the Board, while the day-to-day investment of the portfolio is delegated to the Manager.

ELECTIONS AND RE-ELECTIONS AT THE ANNUAL GENERAL MEETING

In accordance with the Company's current Articles, one-third of the Directors subject to retirement by rotation retire at each AGM. In so far as the number of Directors retiring is less than one-third, those Directors who have been longest in office shall also retire. In accordance with the Company's Articles, the UK Corporate Governance Code and AIC Code, all Directors will be subject to re-election by shareholders at intervals of no more than three years. Directors will also be subject to annual re-election after nine years of service.

The Board will consider the continuing independence of any Director who has served on the Board for nine years or more, giving consideration to:

(i) Employee relationships.

(ii) Material business relationships.

(iii) Family ties.

(iv) Cross-directorships.

(v) Shareholdings.

A Chairman stepping down from that role will be capable of continuing to serve as a Director.

In accordance with the Articles, Mr Gamble and Ms Matthews will retire by rotation at the Annual General Meeting and, being eligible, will offer themselves for re-election.

Fellow Directors recommend the re-election of Mr Gamble and Ms Matthews. Mr Gamble as Chairman has demonstrated good leadership skills to ensure the efficient operation of the Board and maintains excellent relationships with the Manager and other service providers. Kathryn Matthews is recommended for re-election as a Director due to her knowledge and experience of the investment industry, making a valuable contribution to the Board.

PERFORMANCE EVALUATION

The Directors conduct an annual review of Board performance and effectiveness to monitor and improve their overall performance. This process is comprised of six elements:

1. a factual report of Board Committee procedures from MUSCIT's Company Secretary;
2. a self-evaluation by each Director against specified criteria;
3. an assessment of the Chairman by each Director against specified criteria;
4. an assessment of the Directors by the Chairman against specified criteria;
5. an assessment of each Directors' independence; and
6. an assessment of any required training.

The Board evaluation process aims to provide a powerful and valuable feedback mechanism for improving Board effectiveness, maximising strengths and highlighting areas for further development.

Mr Gamble, as Chairman, takes overall responsibility for the evaluation process and has selected a questionnaire methodology to achieve these objectives, which is followed by a feedback session that considers how effective the process has been and identifies any areas for improvement.

The Board has reviewed the time commitment required from all Directors, and noting their contributions and 100% attendance at all Board and Committee meetings and discussions held outside these formal meetings, believes that all Directors have demonstrated the necessary commitment to the role.

The Board considers that outside commitments have not impinged on their duties as a Director of MUSCIT and have enhanced the knowledge brought to the Board meetings.

STEWARDSHIP CODE

The Company has given discretionary voting powers to the Manager. AIC Code Principal 16 recommends that the Board should agree a policy regarding voting rights exercised by Montanaro. However, the Board has agreed that there is no need to set a written policy with Montanaro concerning key operational issues as the Board and Montanaro already have a clear understanding of their respective responsibilities.

The Board encourages the Manager to give due consideration to environmental, social and governance matters whilst recognising the overall investment policy and objectives of the Company. Montanaro reports to the Board at every meeting and the Board reviews a full list of all votes cast on the Company's behalf. Montanaro votes against resolutions it considers may damage shareholders' rights or economic interests. Montanaro gives due weight to what it considers to be socially responsible investments, when making investment decisions, but its overriding objective is to produce good investment returns for shareholders.

During the year the Manager on behalf of the Company exercised its voting authority as follows:

Meetings	
Number of meetings voted at	51
Number of meetings voted against management or abstained	16
Resolutions	
Number of resolutions where voted with management	626
Number of resolutions where voted against management or abstained	16
The actual resolutions voted against	2

BOARD COMMITTEES

The Chairman of each Board Committee fulfils an important leadership role similar to that of the Chairman of the Board, particularly in creating the conditions for overall Committee and individual Director effectiveness.

Each Committee has adopted formal written terms of reference which are available upon request from the Company Secretary and are available on the Company's website www.montanarouksmaller.co.uk.

The Audit Committee is comprised of the three independent non-executive Directors and is chaired by Mr Moule. The Board is satisfied that Mr Moule has recent and relevant financial experience to guide the Committee in its deliberations.

One of the principal responsibilities of the Committee is the monitoring of the process for the production and integrity of the Company's accounts. The Committee also reviews and monitors the effectiveness of the internal control and risk management systems. The Committee meets at least twice a year in conjunction with the annual and half-yearly financial results of MUSCIT. It provides a forum through which MUSCIT's Auditor reports to the Board and it also reviews the terms of appointment, remuneration, independence, objectivity and effectiveness of the Auditor on an annual basis. The Audit Committee reviews the annual and half-yearly financial reports of MUSCIT, monitors the internal controls of service providers and reviews the need for internal audit.

The Audit Committee has reviewed and accepted reports from the Auditor on its procedures for ensuring that its independence and objectivity are safeguarded. The Audit Committee reviews the need for non-audit services and authorises such on a case by case basis, having consideration to the cost-effectiveness of the services and the independence and objectivity of the Auditor. Non-audit work may be given to the external Auditor unless there is a conflict of interest or someone else is considered to have more relevant experience. No non-audit services were provided in the year under review.

The Committee has advised the Board that based on its assessment of their performance and independence, KPMG Audit Plc has fulfilled its obligations to the Company and shareholders and on this basis recommends their reappointment as Auditor.

Directors' Report continued

The Remuneration Committee is comprised of the three independent non-executive Directors, with Kathryn Matthews acting as Chairman. The Remuneration Committee meets as required for the purpose of considering levels of remuneration paid to the Board, and reviews the Directors' Remuneration Report. The Chairman of the Company takes no part in discussions concerning his own salary. This Committee held one meeting during the year.

The Nomination Committee is comprised of the three independent non-executive Directors and meets as required for the purpose of considering recruitment to, and removals from, the Board, with Kathryn Matthews acting as Chairman. Appointments to the Board are made according to a person's existing knowledge and expertise taking into account the Company's agreed strategic priorities. The Board is committed to a policy of succession planning. Following an internal Board evaluation process and as part of its long-term succession planning the Board has decided to search for an additional Director with complementary skills to the existing Board members.

The Management Engagement Committee is comprised of the three independent non-executive Directors and meets at least once a year for the purpose of reviewing the terms of appointment and performance of the Manager and other service providers, with Mr Moule acting as Chairman. During the year the Committee held one meeting.

The Management Engagement Committee considers the performance of the Manager by comparing it to obligations imposed under the terms of the management agreement. The Committee makes recommendations to the full Board on any variations to the terms of the management agreement when it considers it necessary or desirable.

The Management Engagement Committee keeps the performance of the Investment Manager under review. Based on the Manager's performance for the year ended 31 March 2013 and the depth and experience of the research capability, the Committee concluded it was in the best interests of the Company's shareholders to continue the appointment of the Manager.

INTERNAL CONTROL AND FINANCIAL REPORTING

The Board is responsible for establishing and maintaining MUSCIT's system of internal controls and for maintaining its effectiveness. Internal control systems are designed to meet the particular needs of MUSCIT and the risks to which it is exposed and by their very nature provide reasonable but not absolute assurance against misstatement or loss. The Directors have reviewed the effectiveness of the system of internal controls, including financial, operational and compliance controls, and risk management. The Board would take actions to remedy any significant failings or weaknesses identified. The key procedures, which have been established to provide effective internal controls are as follows:

- Throughout the year under review and up to the date of this Annual Report, there has been an ongoing process for identifying, evaluating and managing the significant risks faced by MUSCIT, which accords with guidance in the document entitled "Internal Control: Revised Guidance for Directors on the Combined Code" and is reviewed on a regular basis by the Board. The process involves reports from MUSCIT's Company Secretary and Manager as described below. In addition, the Audit Committee receives internal controls statements from all the third parties to which it delegates functions.
- In accordance with guidance issued to directors of listed companies in October 2005, the Board has carried out a review of the system of internal controls, operated since 1 April 2012.
- Investment management is provided by the Manager, which is regulated by the FCA. The Board is responsible for setting the overall investment policy and monitors the activity of the Manager at regular Board meetings. The Manager provides reports at these meetings, which cover investment performance and compliance issues.
- Capita Sinclair Henderson Limited is responsible for the provision of administration and company secretarial duties. It also reports to the Board on risk control issues for MUSCIT as a whole.
- Custody of assets is undertaken by independent third parties.
- The duties of investment management, accounting and the custody of assets are segregated.
- The procedures of the individual parties are designed to complement one another.
- The Board of MUSCIT clearly defines the duties and responsibilities of its agents and advisers in the terms of their contracts. The appointment of agents and advisers is conducted by the Board after consideration of the quality of the parties involved, and the Board monitors their ongoing performance and contractual arrangements.
- Mandates for authorisation of investment transactions and expense payments are set by the Board.
- The Board reviews financial information produced by MUSCIT's Company Secretary in detail on a monthly basis.

DIALOGUE WITH SHAREHOLDERS

Communication with shareholders is given a high priority by both the Board and the Investment Manager. The Directors are always available to enter into dialogue with shareholders and have a policy of regularly inviting major shareholders to meet with the Board. Shareholders wishing to communicate directly with the Board should contact the Company Secretary at the registered office.

All shareholders have the opportunity to attend and vote at the Annual General Meeting during which the Board and Manager are available to discuss issues affecting MUSCIT. The Investment Manager has signed up to the Stewardship Code and will be publishing its voting records on its website.

Substantial Shareholdings

As at 31 March 2013, MUSCIT has been informed of the following notifiable interests in its voting rights:

Beneficial owner	Ordinary shares	% of voting rights
Derbyshire County Council	2,925,000	8.74
East Riding of Yorkshire Council	2,743,400	8.20
Reliance Mutual Insurance Society Limited	1,885,000	5.63
Jupiter Asset Management Limited	1,875,000	5.60
Newton Investment Management Limited	1,661,565	4.96
Investec Wealth & Investment Limited	1,543,377	4.61
Royal London Asset Management Limited	1,534,839	4.58
Henderson Global Investors Limited	1,450,000	4.33
AEGON UK Group of Companies	1,436,374	4.29
Kames Capital	1,259,912	3.76
City of Bradford Metropolitan District Council	1,083,500	3.24

At the date of this report the Company had been advised that the interests of Investec Wealth & Investment Limited and Kames Capital had fallen below 3% of the total voting rights of the Company.

No other changes to the above holdings have been notified between 31 March 2013 and the date of this report.

Going Concern

The Company's Articles require that the Directors convene a General Meeting in 2014 to be held on or within seven days prior to the accounting reference date of the Company falling in that year, at which a Special Resolution will be proposed providing for the Company to be wound up on a voluntary basis, unless an Ordinary Resolution is passed at the 2013 Annual General Meeting releasing the Directors from this obligation. As set out in the Chairman's Statement, such an Ordinary Resolution will be proposed at the forthcoming Annual General Meeting. The Directors strongly recommend that shareholders vote in favour of continuation of the Company beyond 2014.

The Directors, after due consideration of the Company's cash balances, the liquidity of the Company's investment portfolio and the cost base of the Company, are of the opinion that it is appropriate to presume that the Company will continue in business for the foreseeable future. Accordingly, the financial statements have been prepared on a going concern basis, consistent with previous years.

No provision has been made for the costs of winding up the Company or liquidating its investments in the event that the resolution to release the Directors from the obligation to convene a General Meeting for the purpose of proposing a winding-up resolution is not passed. Such costs are likely to include professional fees (accounting and legal advisers) and, depending on the timing, the costs of terminating existing operational contracts such as management, administration, registrar and custody agreements. At the present time it is not possible to quantify the wind-up costs involved with any reasonable degree of accuracy. With regard to the investments, the value would be determined by investment markets and bid prices at that time.

Payment of Suppliers

It is MUSCIT's payment policy to obtain the best possible terms for all business and therefore there is no consistent policy as to the terms used. The Company agrees with its suppliers the terms on which business will take place and it is MUSCIT's policy to abide by those terms. The Company endeavours to pay suppliers' invoices by the end of the month in which they are received, and this policy will continue for future years. No invoices received by MUSCIT prior to the Balance Sheet date (or 31 March 2012) were unpaid and therefore there were no trade creditors at either year end.

Auditor

KPMG Audit Plc is willing to remain in office and Resolution 6 for its re-appointment will be proposed at the forthcoming Annual General Meeting.

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's Auditor is unaware; and each Director has taken all the steps that he ought to have taken as a Director to make himself aware of any relevant audit information and to establish that the Company's Auditor is aware of that information.

Special Business at the Annual General Meeting

A resolution to renew MUSCIT's authority to purchase (either for cancellation or for placing into Treasury) up to 14.99% of the Ordinary shares in circulation for a further year will be put to shareholders as Resolution 7 at the Annual General Meeting. Purchases will be made on the open market and prices will be in accordance with the terms laid out in Resolution 7. The authority will be used where the Directors consider it to be in the best interests of shareholders.

Resolution number 8, if passed, will give the Directors the general authority (pursuant to paragraph (a) of the Resolution) to allot Ordinary shares (including issues out of Treasury) up to an aggregate nominal amount of £1,115,865, representing one-third of MUSCIT's issued Ordinary shares. In addition, in accordance with the guidance from the Association of British Insurers on the expectations of institutional investors, upon the passing of Resolution 8 the Directors will have the authority (pursuant to paragraph (b) of the Resolution) to allot Ordinary shares up to an additional one-third of the current issued share capital but only for the purposes of a rights issue to existing shareholders. The authority will be used where the Directors consider it to be in the best interests of shareholders.

Resolution number 9, subject to the passing of Resolution 8, will give the Directors the general authority to allot Ordinary shares (including issues out of Treasury) for cash, up to an aggregate nominal amount of £167,380, representing 5% of the issued Ordinary shares and at a price above net asset value per share, without having to offer such shares to existing shareholders in proportion to their existing holdings.

The authorities for the above resolutions will expire at the conclusion of the Company's next Annual General Meeting after the passing of the resolutions.

Directors' Report continued

Resolution number 10, subject to the passing of Resolution number 9, will give the Directors a general authority to sell shares held in Treasury at a discount to net asset value, up to the same aggregate nominal amount of £167,380, representing 5% of the issued Ordinary shares. Any shares will only be re-issued at an absolute profit and at a lower discount than when they were originally purchased.

Any decisions regarding placing shares into Treasury, or issuing shares from Treasury, will be taken by the Directors.

Resolution 11, if passed, will release the Directors from the obligation to convene an Extraordinary General Meeting to be held during 2014 providing for the winding-up of the Company.

Under the Company's Articles, the Directors are required to convene a General Meeting in 2014 at which a Special Resolution will be proposed for the winding up of the Company. Resolution 11, if passed, will release the Directors from the obligation to convene this General Meeting and allow the Company to continue as an investment trust for a further five years. Further information about the duration of the Company is set out in Note 17 to the financial statements.

The Directors strongly recommend that shareholders vote in favour of this resolution to enable continuation of the Company beyond 2014.

Resolution 12, if passed, will allow the Directors to hold a General Meeting, other than an Annual General Meeting, on a minimum of 14 clear days notice. The notice period for Annual General Meetings will remain at 21 clear days. The Directors will only call General Meetings on 14 clear days notice where they consider it in the best interests of the shareholders to do so and the relevant matter requires to be dealt with expediently.

Full details of these Resolutions are provided in the Notice of Annual General Meeting.

The Directors consider that all resolutions to be proposed at the Annual General Meeting are in the best interests of the Company and its members as a whole.

The Directors unanimously recommend that all shareholders vote in favour of all the resolutions, as they intend to do in respect of their own holdings.

By order of the Board

CAPITA SINCLAIR HENDERSON LIMITED
Company Secretary
19 June 2013

Directors' Remuneration Report

The Board has prepared this report, in accordance with the requirements of Schedule 8 to the Large and Medium Sized Companies and Groups (Account and Reports Regulations 2008), in respect of the year ended 31 March 2013. Ordinary Resolution 2 is being proposed to receive and approve this report at the forthcoming Annual General Meeting.

The Company's Auditor is required to audit certain disclosures provided in this report. Where disclosures have been audited, they are indicated in this Report. The Auditor's opinion is included in its Audit Report on page 25.

Remuneration Committee

The Remuneration Committee is comprised of three non-executive directors, Mr Gamble and Mr Moule, with Kathryn Matthews acting as Chairman.

The Remuneration Committee meets as required for the purpose of considering levels of remuneration paid to the Board. Each Director of the Company takes no part in discussions concerning their own salary. This Committee held one meeting during the year.

Policy on Directors' Fees

The Board's policy is that the remuneration of Directors should reflect the experience of the Board as a whole, be fair and comparable to that of other companies of a similar size and capital structure (Ordinary shares and bank borrowings) and that have a similar investment objective (capital growth). It is intended that this policy will continue for the year ending 31 March 2014 and subsequent years.

The fees of the Directors are determined within the limits set out in the Company's Articles of Association. Directors are not eligible for bonuses, pension benefits, share options, long-term incentive schemes or other benefits as they do not feel it is appropriate for the Directors of the Company at this time.

As reported last year, the Remuneration Committee has agreed to review fees on an annual basis. Annual increases are subject to an increase in the net assets and share price of the Company and reference will be made to the RPI and peer group to determine the level of increase. After a strong 2013 and following review of the market, the Board has agreed to increase Directors' fees, effective from 1 April 2013, to £29,000 for the Chairman of the Board, £22,000 for the Chairman of the Audit Committee, £21,000 for the Senior Director and £20,000 for other Directors'.

Directors' Service Contracts

It is the Board's policy that none of the Directors has a service contract. The terms of their appointment provide that a Director shall retire and be subject to election at the first Annual General Meeting after appointment, and at least every three years thereafter. The terms also provide that a Director may be removed without notice and that compensation will not be due on leaving office.

Your Company's Performance

The following graph compares the total return (assuming all dividends are reinvested) over the past five years to Ordinary shareholders to the total shareholder return of the SmallCap and the NSCI. The SmallCap was chosen for comparison purposes as it is the benchmark used for investment performance measurement purposes in the year. The NSCI has been adopted as the new benchmark from 1 April 2013 and has been included for comparative purposes.

Total Return vs SmallCap and NSCI (rebased from March 2008)

Source: Capita Sinclair Henderson Limited

Directors' Emoluments for the Year (Audited)

The Directors who served in the year received the following emoluments in the form of fees:

	Year to 31 March 2013 £	Year to 31 March 2012 £
David Gamble	**27,000**	27,000
Roger Cuming	**19,624***	19,500
Kathryn Matthews	**18,500**	18,500
Michael Moule	**20,000**	20,000

* This includes £124 received as reimbursement of travel expenses.

No sums are paid to any third parties in respect of Directors' services.

Approval

The Directors' Remuneration Report was approved by the Board of Directors on 19 June 2013.

On behalf of the Board
DAVID GAMBLE
Chairman

Statement of Directors' Responsibilities
in respect of the Annual Report and the Financial Statements

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to:

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

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that comply with that law and those regulations.

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

The Directors confirm to the best of their knowledge:

- the financial statements, prepared in accordance with UK Accounting Standards, give a true and fair view of the assets, liabilities, financial position and return of the Company; and
- the Chairman's Statement, the Manager's Report and the Directors' Report include a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that it faces.

On behalf of the Board
DAVID GAMBLE
Chairman
19 June 2013

Independent Auditor's Report
to the Members of Montanaro UK Smaller Companies Investment Trust PLC

We have audited the financial statements of Montanaro UK Smaller Companies Investment Trust PLC for the year ended 31 March 2013 which comprise the Income Statement, the Reconciliation of Movements in Shareholders' Funds, the Balance Sheet, the Statement of Cash Flows and the related notes, set out on pages 26 to 39. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

As explained more fully in the Statement of Directors' Responsibilities set out on page 24, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 March 2013 and of its total return for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the Directors' statement, set out on page 21, in relation to going concern;
- the part of the Corporate Governance Statement on pages 17 to 20 relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review, and
- certain elements of the report to shareholders by the Board on Directors' remuneration.

Salim Tharani (Senior Statutory Auditor)

for and on behalf of

KPMG Audit Plc Statutory Auditor
Chartered Accountants
100 Temple Street
Bristol
BS1 6AG
United Kingdom
19 June 2013

Income Statement
for the year to 31 March 2013

		Year to 31 March 2013			Year to 31 March 2012		
	Notes	**Revenue £000**	**Capital £000**	**Total £000**	Revenue £000	Capital £000	Total £000
Gains on investments designated as fair value through profit or loss	10	**–**	**32,574**	**32,574**	–	6,607	6,607
Dividends and interest	2	**3,844**	**–**	**3,844**	3,667	–	3,667
Management fee	3	**(857)**	**(857)**	**(1,714)**	(781)	(782)	(1,563)
Management performance fee	3	**–**	**–**	**–**	–	(812)	(812)
Other expenses	4	**(315)**	**–**	**(315)**	(246)	–	(246)
Movement in fair value of derivative financial instruments	15	**–**	**(479)**	**(479)**	–	(75)	(75)
Net return before finance costs and taxation		**2,672**	**31,238**	**33,910**	2,640	4,938	7,578
Interest payable and similar charges	6	**(322)**	**(322)**	**(644)**	(160)	(160)	(320)
Net return before taxation		**2,350**	**30,916**	**33,266**	2,480	4,778	7,258
Taxation	7	**–**	**–**	**–**	–	–	–
Net return after taxation		**2,350**	**30,916**	**33,266**	2,480	4,778	7,258
Return per Ordinary share	9	**7.02p**	**92.35p**	**99.37p**	7.41p	14.27p	21.68p

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

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

No Statement of Total Recognised Gains and Losses has been prepared as all such gains and losses are shown in the Income Statement.

No operations were acquired or discontinued in the year.

The notes on pages 30 to 39 form part of these financial statements.

Reconciliation of Movements in Shareholders' Funds

for the year to 31 March 2013

Year to 31 March 2013	Notes	**Called-up share capital £000**	**Share premium account £000**	**Capital redemption reserve £000**	**Special reserve £000**	**Capital reserve £000**	**Distributable revenue reserve £000**	**Total equity shareholders' funds £000**
As at 31 March 2012		**3,348**	**19,307**	**1,362**	**4,642**	**113,343**	**4,146**	**146,148**
Fair value movement of investments	10	**–**	**–**	**–**	**–**	**32,574**	**–**	**32,574**
Costs allocated to capital		**–**	**–**	**–**	**–**	**(1,179)**	**–**	**(1,179)**
Dividends paid in the year	8	**–**	**–**	**–**	**–**	**–**	**(2,263)**	**(2,263)**
Movement in fair value of derivative financial instruments	15	**–**	**–**	**–**	**–**	**(479)**	**–**	**(479)**
Net revenue for the year		**–**	**–**	**–**	**–**	**–**	**2,350**	**2,350**
As at 31 March 2013		**3,348**	**19,307**	**1,362**	**4,642**	**144,259**	**4,233**	**177,151**

Year to 31 March 2012	Notes	Called-up share capital £000	Share premium account £000	Capital redemption reserve £000	Special reserve £000	Capital reserve £000	Distributable revenue reserve £000	Total equity shareholders' funds £000
As at 31 March 2011		3,348	19,307	1,362	4,642	108,565	3,929	141,153
Fair value movement of investments	10	–	–	–	–	6,607	–	6,607
Costs allocated to capital		–	–	–	–	(1,754)	–	(1,754)
Dividends paid in the year	8	–	–	–	–	–	(2,263)	(2,263)
Movement in fair value of derivative financial instruments	15	–	–	–	–	(75)	–	(75)
Net revenue for the year		–	–	–	–	–	2,480	2,480
As at 31 March 2012		3,348	19,307	1,362	4,642	113,343	4,146	146,148

The notes on pages 30 to 39 form part of these financial statements.

Balance Sheet
as at 31 March 2013

	Notes	31 March 2013 £000	31 March 2013 £000	31 March 2012 £000	31 March 2012 £000
Fixed assets					
Investments designated at fair value through profit or loss	10		**179,446**		148,373
Current assets					
Debtors	12	**711**		566	
Cash at bank	21	**12,961**		13,966	
			13,672		14,532
Creditors: amounts falling due within one year					
Other creditors	13	**(413)**		(1,682)	
Revolving credit facility	14	**(15,000)**		(15,000)	
			(15,413)		(16,682)
Net current liabilities			**(1,741)**		(2,150)
Total assets less current liabilities			**177,705**		146,223
Creditors: amounts falling due after more than one year					
Interest rate swap	15		**(554)**		(75)
Net assets			**177,151**		146,148
Share capital and reserves					
Called-up share capital	16		**3,348**		3,348
Share premium account			**19,307**		19,307
Capital redemption reserve			**1,362**		1,362
Special reserve			**4,642**		4,642
Capital reserve			**144,259**		113,343
Distributable revenue reserve			**4,233**		4,146
Total equity shareholders' funds			**177,151**		146,148
Net asset value per Ordinary share	19		**529.19p**		436.57p

These financial statements were approved by the Board of Directors on 19 June 2013.

DAVID GAMBLE

Company Registered Number: 3004101

The notes on pages 30 to 39 form part of these financial statements.

Statement of Cash Flows
for the year to 31 March 2013

	Notes	**Year to 31 March 2013 £000**	**Year to 31 March 2013 £000**	Year to 31 March 2012 £000	Year to 31 March 2012 £000
Operating activities					
Investment income received		**3,681**		3,600	
Deposit interest received		**2**		1	
Interest received on VAT reclaimed on administration and company secretarial fees		**–**		7	
Management fees paid		**(1,688)**		(1,558)	
Performance fees paid		**(812)**		(786)	
Company secretarial fees paid		**(82)**		(86)	
Other cash expenses		**(227)**		(216)	
Net cash inflow from operating activities	20		**874**		962
Servicing of finance					
Interest and similar charges paid		**(646)**		(148)	
Net cash outflow from servicing of finance			**(646)**		(148)
Capital expenditure and financial investment					
Purchases of investments		**(28,187)**		(26,508)	
Sales of investments		**29,217**		41,517	
Net cash inflow from investing activities			**1,030**		15,009
Equity dividends paid			**(2,263)**		(2,263)
(Decrease)/increase in cash	21		**(1,005)**		13,560

The notes on pages 30 to 39 form part of these financial statements.

Notes to the Financial Statements
at 31 March 2013

1 Accounting Policies

ACCOUNTING CONVENTION
The financial statements are prepared on a going concern basis, under the historical cost convention as modified by the revaluation of fixed asset investments and in accordance with UK applicable accounting standards and the Statement of Recommended Practice regarding the Financial Statements of Investment Trust Companies and Venture Capital Trusts ("SORP") issued in January 2009. The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied throughout the year and the preceding year.

INCOME RECOGNITION
Dividend income is included in the financial statements when the investments concerned are quoted ex-dividend and shown net of any associated tax credit where applicable.

Deposit interest and underwriting commissions receivable are included on an accruals basis.

MANAGEMENT EXPENSES AND FINANCE COSTS
All expenses are accounted for on an accruals basis. Management fees and finance costs are allocated 50% to the capital reserve and 50% to the revenue account. This is in line with the Board's expectations of long-term returns from the investment portfolio of the Company. Performance fees are charged 100% to capital.

Costs arising on early settlement of debt are allocated 100% to capital, in accordance with the requirements of the SORP.

All other expenses are allocated in full to the revenue account.

INVESTMENTS
Investments are recognised and derecognised on the trade date where a purchase or sale is under a contract whose terms require delivery within the time frame established by the market concerned, and are initially measured at fair value.

All investments held by the Company are classified as at "fair value through profit or loss". Investments are initially recognised at cost, being the fair value of the consideration given. After initial recognition investments are measured at fair value, with unrealised gains and losses on investments and impairment of investments recognised in the Income Statement and allocated to capital.

For investments actively traded in organised financial markets, fair value is generally determined by reference to quoted market bid prices or closing prices for SETS (London Stock Exchange's electronic trading service) stocks sourced from the London Stock Exchange on the Balance Sheet date, without adjustment for transaction costs necessary to realise the asset.

TREASURY SHARES
The consideration paid for shares held in Treasury is presented as a deduction from equity shareholders' funds, in accordance with FRS 25: "Financial Instruments: Disclosure and Presentation". Any profit on the sale of shares out of Treasury is credited to the share premium account in full.

TAXATION
The charge for taxation is based on the net revenue for the year. Deferred taxation is provided in accordance with FRS 19: "Deferred Taxation", on all timing differences that have originated but not reversed by the Balance Sheet date. Deferred taxation assets are only being recognised to the extent that they are regarded as recoverable.

DIVIDENDS PAYABLE TO SHAREHOLDERS
In accordance with FRS 21: "Events after the Balance Sheet date", dividends to shareholders are recognised as a liability in the period in which they have been declared. Therefore, any interim dividends are not accounted for until paid, and final dividends are accounted for when approved by shareholders at an Annual General Meeting.

BANK LOANS AND BORROWINGS
All bank loans and borrowings are initially recognised at cost, being the fair value of the consideration received, less issue costs where applicable. After initial recognition, all interest bearing loans and borrowings are subsequently measured at amortised cost. Any differences between cost and redemption value is recognised in the Income Statement over the period of the borrowings on an effective interest basis.

DERIVATIVE FINANCIAL INSTRUMENTS
It is the Company's policy not to trade in derivative financial instruments. However, the Company has utilised an interest rate swap to mitigate its exposure to interest rate changes on its bank loan which is subject to a variable rate of interest. Details can be found in note 15.

Derivatives are recognised at fair value. Movement in the fair value of the derivative is recognised in the Income Statement and allocated to capital.

1 Accounting Policies continued

RESERVES

Capital reserve

The following are accounted for in this reserve:

- gains and losses on the realisation of investments;
- net movement arising from changes in the fair value of investments that can be readily converted to cash without accepting adverse terms;
- net movement from changes in the fair value of derivative financial instruments; and
- expenses, together with related taxation effect, charged to this account in accordance with the above policies.

Special reserve

The special reserve was created by a reduction in the share premium account by order of the High Court in August 1998. It can be used for the repurchase of the Company's Ordinary shares.

In accordance with the SORP, the consideration paid for shares bought into and held in Treasury is shown as a deduction from the special reserve.

Capital redemption reserve

The capital redemption reserve accounts for amounts by which the issued capital is diminished through the repurchase of the Company's own shares.

2 Income

	Year to 31 March 2013 £000	Year to 31 March 2012 £000
Income from investments	**3,842**	3,659
UK dividend income	**3,781**	3,550
Overseas dividend income	**61**	109
Other income		
Bank interest	**2**	1
Interest received on VAT reclaimed on administration and company secretarial fees	**–**	7
Total income	**3,844**	3,667
Total income comprises		
Dividends from financial assets designated at fair value through profit or loss	**3,842**	3,659
Interest from financial assets designated at fair value through profit or loss	**2**	1
Dividends and interest	**3,844**	3,660
Other income not from financial assets	**–**	7
	3,844	3,667

3 Management fee

	Year to 31 March 2013			Year to 31 March 2012		
	Revenue £000	**Capital £000**	**Total £000**	Revenue £000	Capital £000	Total £000
Management fee	**857**	**857**	**1,714**	781	782	1,563
Performance fee	**–**	**–**	**–**	–	812	812

The Manager receives a monthly fee equivalent to 1/12 of 1.0% of the gross assets of the Company valued at the close of business on the last business day of each month and is entitled to a performance fee calculated as described in the Directors' Report on page 17.

At 31 March 2013, £161,000 (2012: £947,000) was due for payment to the Manager.

Notes to the Financial Statements continued
at 31 March 2013

4 Other Expenses

	Year to 31 March 2013 £000	Year to 31 March 2012 £000
Administration and company secretarial fees	**89**	86
VAT reclaimed on administration and company secretarial fees	**–**	(53)
Auditor's remuneration for:		
– audit	**20**	20
Other expenses (including Directors' remuneration and VAT)	**206**	193
	315	246

5 Directors' Remuneration

	Year to 31 March 2013 £000	Year to 31 March 2012 £000
Total fees	**85**	85

A breakdown of the Directors' remuneration is set out in the Directors' Remuneration Report on page 23.

The Company has no employees.

6 Interest Payable and Similar Charges

	Year to 31 March 2013			Year to 31 March 2012		
Financial liabilities not at fair value through profit or loss	**Revenue £000**	**Capital £000**	**Total £000**	Revenue £000	Capital £000	Total £000
Interest payable on loan	**322**	**322**	**644**	160	160	320
	322	**322**	**644**	160	160	320

7 Taxation

	Year to 31 March 2013			Year to 31 March 2012		
	Revenue £000	**Capital £000**	**Total £000**	Revenue £000	Capital £000	Total £000
Return on ordinary activities before taxation	**2,350**	**30,916**	**33,266**	2,480	4,778	7,258
Theoretical corporation tax at 24% (2012: 26%)	**564**	**7,420**	**7,984**	645	1,242	1,887
Effects of:						
– capital gains that are not taxable	**–**	**(7,703)**	**(7,703)**	–	(1,698)	(1,698)
– overseas dividend income not liable to corporation tax	**(15)**	**–**	**(15)**	(28)	–	(28)
– UK dividend income not liable to corporation tax	**(883)**	**–**	**(883)**	(901)	–	(901)
– expenses disallowed for taxation purposes	**–**	**–**	**–**	1	–	1
– excess management expenses	**334**	**283**	**617**	283	456	739
	–	**–**	**–**	–	–	–

At 31 March 2013, the Company had surplus management expenses and non-trade losses of £30,175,753 (2012: £27,605,536) which have not been recognised as a deferred taxation asset. This is because the Company is not expected to generate taxable income in future periods in excess of the deductible expenses of those future periods and, accordingly, it is unlikely that the Company will be able to reduce future taxation through the use of existing surplus expenses.

Due to the Company's status as an investment trust and the intention to continue to meet the conditions required to maintain its investment trust status, the Company has not provided deferred tax on any capital gains and losses arising on the revaluation or disposal of investments.

8 Dividends

	Year to 31 March 2013 £000	Year to 31 March 2012 £000
Paid		
2012 Final dividend of 6.76p (2011: 6.76p) per Ordinary share	**2,263**	2,263
Proposed		
2013 Final dividend of 6.76p (2012: 6.76p) per Ordinary share	**2,263**	2,263

9 Return per Ordinary Share

	Year to 31 March 2013			Year to 31 March 2012		
	Revenue	**Capital**	**Total**	Revenue	Capital	Total
Ordinary share	**7.02p**	**92.35p**	**99.37p**	7.41p	14.27p	21.68p

Revenue return per Ordinary share is based on the net revenue after taxation of £2,350,000 (2012: £2,480,000) and 33,475,958 (2012: 33,475,958) Ordinary shares, being the weighted average number of Ordinary shares, excluding any shares held in Treasury.

Capital return per Ordinary share is based on net capital gains for the year of £30,916,000 (2012: £4,778,000), and on 33,475,958 (2012: 33,475,958) Ordinary shares, being the weighted average number of Ordinary shares, excluding any shares held in Treasury.

Normal and diluted return per share are the same as there are no dilutive elements on share capital.

10 Investments

	Year to 31 March 2013 £000	Year to 31 March 2012 £000
Total investments at fair value	**179,446**	148,373

The investment portfolio comprises 44 listed UK equity holdings including 4 holdings totalling £9,766,000 (representing 5.4% of the portfolio) traded on the Alternative Investment Market (“AIM”).

	Year to 31 March 2013 £000	Year to 31 March 2012 £000
Opening book cost	**103,944**	105,747
Opening investment holding gains	**44,429**	47,428
Opening valuation	**148,373**	153,175
Movements in the year		
Purchases at cost	**27,716**	26,702
Sales – proceeds	**(29,217)**	(38,111)
Sales – realised gains on sales	**8,019**	9,606
Increase/(decrease) in investment holding gains	**24,555**	(2,999)
Closing valuation	**179,446**	148,373
Closing book cost	**110,462**	103,944
Closing investment holding gains	**68,984**	44,429
	179,446	148,373

Notes to the Financial Statements continued

at 31 March 2013

10 Investments continued

FAIR VALUE HIERARCHY

In accordance with FRS 29: "Financial Instruments: Disclosures", the Company must disclose the fair value hierarchy of financial instruments.

The fair value hierarchy consists of the following three levels:

- level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities;
- level 2 – inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs).

For financial instruments (within the scope of FRS 29), which are measured at fair value in the Balance Sheet an entity shall disclose the following for each class of financial instruments:

- the level in the fair value hierarchy into which the fair value measurements are categorised in their entirety;
- any significant transfers between level 1 and level 2 of the fair value hierarchy and the reasons for those transfers; and
- for fair value measurements in level 3 of the hierarchy, a reconciliation from the opening balances to the closing balances. As well as highlighting purchases, sales, and gains and losses, this reconciliation will identify transfers into or out of level 3 and the reasons for those transfers.

The table below sets out fair value measurements of financial assets in accordance with the FRS 29 fair value hierarchy system:

	31 March 2013			31 March 2012		
	Level 1	**Level 2**	**Total**	Level 1	Level 2	Total
	£000	**£000**	**£000**	£000	£000	£000
Equity investments	**179,446**	**–**	**179,446**	148,373	–	148,373
	179,446	**–**	**179,446**	148,373	–	148,373

The table below sets out fair value measurements of financial liabilities in accordance with the FRS 29 fair value hierarchy system:

	31 March 2013			31 March 2012		
	Level 1	**Level 2**	**Total**	Level 1	Level 2	Total
	£000	**£000**	**£000**	£000	£000	£000
Revolving credit facility	**–**	**15,000**	**15,000**	–	15,000	15,000
Derivative financial instruments	**–**	**554**	**554**	–	75	75
	–	**15,554**	**15,554**	–	15,075	15,075

TRANSACTION COSTS

During the year, the Company incurred transaction costs of £172,000 (2012: £177,000) and £33,000 (2012: £51,000) on purchases and sales of investments, respectively. These amounts are deducted in determining gains on investments at fair value as disclosed in the Income Statement.

	31 March 2013 £000	31 March 2012 £000
Net gains on investments at fair value though profit or loss		
Gains on sales	**8,019**	9,606
Changes in fair value	**24,555**	(2,999)
	32,574	6,607

A list of the investments by market value and an analysis of the investment portfolio by industrial or commercial sector are set on pages 10 and 11.

11 Significant Holdings

The Company has a holding of 3% or more of the voting rights attached to shares that is material in the context of the financial statements in the following investments:

Security	% of voting rights
Latchways PLC	3.1

12 Debtors

	31 March 2013 £000	31 March 2012 £000
Prepayments and accrued income	**68**	84
Dividends receivable	**643**	482
	711	566

The carrying amount for prepayments, accrued income and dividends receivable disclosed above reasonably approximates to its fair value at the year end and is expected to be realised within a year from the Balance Sheet date.

13 Other Creditors

	31 March 2013 £000	31 March 2012 £000
Due to brokers	**–**	471
Accruals and deferred income	**413**	1,211
	413	1,682

The carrying amount for accruals and deferred income disclosed above reasonably approximates to its fair value at the year end and is expected to be realised within a year from the Balance Sheet date.

14 Revolving Credit Loan Facility

	31 March 2013 £000	31 March 2012 £000
Falling due within one year	**15,000**	15,000
	15,000	15,000

On 19 December 2011 the Company agreed a £15,000,000 Floating Rate Revolving Credit Loan Facility with ING Bank N.V. At the same time the Company entered into a £15,000,000 Interest Rate Swap with ING Bank N.V.

The Floating Rate Revolving Credit Loan Facility is available for a five year term from 19 December 2011 to 19 December 2016. The loan is currently drawn down until 19 June 2013 and will be rolled over on a six monthly basis. Interest is payable at six month LIBOR plus a margin and MLA costs.

The Interest Rate Swap is for five years and enables the Company to fix the effective interest rate of the £15,000,000 loan over its term at 4.2921%* per annum.

* Including margin and mandatory costs.

15 Derivative Financial Instruments

An interest rate swap is an agreement between two parties to exchange fixed and floating rate interest payments based upon interest rates defined in the contract without the exchange of the underlying principal amounts.

The Company entered into an agreement on 19 December 2011 which swapped its obligation to pay variable rates of interest for a fixed rate of 4.2921% per annum until 19 December 2016.

The fair value of the derivative financial instrument is shown below:

	31 March 2013 £000	31 March 2012 £000
Opening valuation	**(75)**	–
Movement in fair value	**(479)**	(75)
Closing valuation	**(554)**	(75)

Notes to the Financial Statements continued
at 31 March 2013

16 Share Capital

	31 March 2013 £000	31 March 2012 £000
Allotted, called-up and fully paid:		
33,475,958 (2012: 33,475,958) Ordinary shares of 10p each	**3,348**	3,348

Voting rights
Ordinary shareholders have unrestricted voting rights at all general meetings of the Company.

At the Annual General Meeting on 27 July 2012 the Company was granted the authority to purchase 5,018,046 Ordinary shares. This authority is due to expire at the conclusion of the next Annual General Meeting.

During the year no shares were purchased for cancellation.

The Company does not have any externally imposed capital requirements. The capital of the Company is managed in accordance with its investment policy in pursuit of its investment objective, both of which are detailed above.

17 Duration of the Company
The Articles of Association prescribe that shareholders should have the opportunity to consider the future of the Company at regular intervals. At the Annual General Meeting to be held on 26 July 2013 an Ordinary Resolution will be proposed to release the Directors from the obligation to convene a General Meeting during 2014 for the purpose of voluntarily winding up the Company, as provided for in the Company's Articles of Association. If the Ordinary Resolution is passed, the Directors will be required to convene a General Meeting to propose the winding up of the Company in 2018, and every five years thereafter, unless at any Annual General Meeting held within, and not more than, 18 months prior to the expiry of the relevant period of five years, an Ordinary Resolution is passed releasing the Directors from the obligation to convene such a General Meeting.

18 Own Shares Held in Treasury
The Company has previously taken advantage of the regulations which came into force on 1 December 2003 to allow companies, including investment trusts, to buy their own shares and hold them in Treasury for re-issue at a later date. There were no shares held in Treasury at any time during the year.

19 Net Asset Value per Ordinary Share
Net asset value per Ordinary share is based on net assets of £177,151,000 (2012: £146,148,000) and on 33,475,958 (2012: 33,475,958) Ordinary shares, being the number of Ordinary shares in issue at the year end.

20 Reconciliation of Net Revenue Before Finance Costs and Taxation to Net Cash Inflow from Operating Activities

	Year to 31 March 2013 £000	Year to 31 March 2012 £000
Net revenue before finance costs and taxation	**2,672**	2,640
Management fee charged to capital	**(857)**	(1,594)
(Decrease)/increase in creditors	**(796)**	49
Increase in prepayments and accrued income	**(145)**	(133)
Net cash inflow from operating activities	**874**	962

21 Reconciliation of Net Cash Flows to Movements in Net Debt

	Year to 31 March 2013 £000	Year to 31 March 2012 £000
(Decrease)/increase in cash in year	**(1,005)**	13,560
Movement in net funds	**(1,005)**	13,560
Net debt at beginning of year	**(1,034)**	(14,594)
Net debt at end of year	**(2,039)**	(1,034)

ANALYSIS OF NET DEBT

	1 April 2012 £000	Cash flows £000	**31 March 2013 £000**
Cash at bank	13,966	(1,005)	**12,961**
Debt due in less than one year	(15,000)	–	**(15,000)**
	(1,034)	(1,005)	**(2,039)**

22 Analysis of Financial Assets and Liabilities

As required by FRS 29: “Financial Instruments: Disclosures”, an analysis of financial assets and liabilities, which identifies the risk to the Company of holding such items, is given below.

BACKGROUND

The Company’s financial instruments comprise securities, cash balances and debtors and creditors that arise from its operations, for example, in respect of sales and purchases awaiting settlement and debtors for accrued income.

The risk management policies and procedures outlined in this note have not changed substantially from the previous accounting period.

The Company has little or no exposure to cash flow or foreign currency risk.

The principal risks the Company faces in its portfolio management activities are:

- credit risk;
- market price risk, i.e. movements in the value of investment holdings caused by factors other than interest rate or currency movement;
- interest rate risk;
- liquidity risk, i.e. the risk that the Company has difficulty in realising assets or otherwise raising funds to meet commitments associated with financial instruments; and
- gearing.

The Manager monitors the financial risks affecting the Company on a daily basis. The Directors receive financial information on a monthly basis which is used to identify and monitor risk.

(i) Credit Risk

Credit risk is the risk of financial loss to the Company if the contractual party to a financial instrument fails to meet its contractual obligations.

The carrying amounts of financial assets best represent the maximum credit risk exposure at the Balance Sheet date.

The Company’s listed investments are held on its behalf by HSBC acting as agent, the Company’s custodian. Bankruptcy or insolvency of the custodian may cause the Company’s rights with respect to securities held by the custodian to be delayed. The Board monitors the Company’s risk by reviewing the custodian’s internal controls reports.

Investment transactions are carried out with a large number of brokers whose creditworthiness is reviewed by the Manager.

Transactions are ordinarily undertaken on a delivery versus payment basis whereby the Company’s custodian bank ensures that the counterparty to any transaction entered into by the Company has delivered in its obligations before any transfer of cash or securities away from the Company is completed.

The banks at which cash is held are under constant review.

The maximum exposure to credit risk at 31 March 2013 was:

	31 March 2013 £000	31 March 2012 £000
Cash at bank	**12,961**	13,966
Debtors and prepayments	**711**	566
	13,672	14,532

None of the Company’s assets are past due or impaired.

(ii) Market Price Risk

Market price risk arises mainly from uncertainty about future prices of financial instruments. The value of shares and the income from them may fall as well as rise and shareholders may not get back the full amount invested. The Manager continues to monitor the prices of financial instruments held by the Company on a real time basis. Adherence to the Company’s investment policy shown on page 40 mitigates the risk of excessive exposure to one issuer or sector.

The Board manages the market price risks inherent in the investment portfolio by ensuring full and timely access to relevant information from the Manager. The Board meets regularly and at each meeting reviews the investment performance, the investment portfolio and the rationale for the current investment positioning to ensure consistency with the Company’s objectives and investment policy. The portfolio does not seek to reproduce the index, investments are selected based upon the merit of individual companies and therefore the portfolio may well diverge from the short-term fluctuations of the benchmark.

Notes to the Financial Statements continued
at 31 March 2013

22 Analysis of Financial Assets and Liabilities continued

Fixed asset investments are valued at fair value as detailed in note 1. A list of the Company's equity investments, an analysis of the investment portfolio by broad industrial and commercial sector, an analysis of the portfolio by market capitalisation of holdings and a description of the 10 largest equity investments is set out on pages 8 to 11.

The maximum exposure to market price risk is the fair value of investments of £179,446,000 (2012: £148,373,000).

If the investment portfolio valuation fell by 1% from the amount detailed in the financial statements as at 31 March 2013 it would have the effect, with all other variables held constant, of reducing the net capital return before taxation by £1,794,000 (2012: £1,484,000). An increase of 1% in the investment portfolio valuation would have an equal and opposite effect on the net capital return before taxation.

(iii) Interest Rate Risk

Changes in interest rates may cause fluctuations in the income and expenses of the Company. The Revolving Credit Loan Facility with ING Bank N.V. is a floating rate facility (see note 14). The amount of such borrowings and the approved levels are monitored and reviewed regularly by the Board. The Company mitigates the risk by the use of an interest rate swap to fix the interest rates on borrowings.

The Company received interest on cash deposits over £25,000 at a rate of 0.03%. The interest received in the year amounted to £2,000 (2012: £1,000).

The interest risk profile of the Company is given below.

If interest rates had reduced by 1% from those paid as at 31 March 2013 it would have the effect, with all other variables held constant, of increasing the net revenue return before taxation on an annualised basis by £150,000 (2012: £150,000). If there was an increase in interest rates of 1% the net revenue return before taxation on an annualised basis would have decreased by £20,000 (2012: £10,000). The calculations are based on cash at bank, short-term deposits and the Revolving Credit Facility as at 31 March 2013 and these may not be representative of the year as a whole.

Due to the structure of the loan facility, changes in interest rates would not have an effect on the fair value of the loan.

(iv) Liquidity Risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities. The Manager does not invest in unlisted securities on behalf of the Company. However, the investments held by the Company consist of UK quoted small companies which are inherently less liquid than quoted large companies. The Manager reviews the portfolio liquidity on a regular basis. Short-term flexibility is achieved through the use of bank borrowings. Liquidity risk is mitigated by the fact that the Company has £13.7 million cash at bank and short-term debtors which can satisfy its creditors and that as a closed end fund assets do not need to be liquidated to meet redemptions.

(v) Gearing

Gearing can have amplified effects on the net asset value of the Company. It can have a positive or negative effect depending on market conditions. It is the Company's policy to determine the adequate level of gearing appropriate to its own risk profile.

(vi) Use of Derivatives

It is the Company's policy not to trade in derivative financial instruments. However, the Company has utilised an interest rate swap to mitigate its exposure to interest rate changes on its Revolving Credit Facility.

FINANCIAL ASSETS

The Company's financial assets consist of listed equity shares, which neither pay interest nor have a maturity date, cash at bank and short-term debtors. No fixed interest assets were held at 31 March 2013 nor during the year. All financial assets are in sterling and disclosed at fair value through profit or loss.

FINANCIAL LIABILITIES

The Company finances its operations through equity, retained profits and bank borrowings (see note 14). The change in the fair value of financial liabilities during the year was not related to the credit risk profile. The interest rate risk profile of the financial liabilities of the Company as at 31 March 2013 is as follows:

	Total £000	Weighted average interest rate %	Period until maturity Years
Amounts drawn down under revolving credit loan facility	**15,000**	**3.69**	**0.22**
Derivative financial instruments	**554**	**0.60**	**3.72**
Financial liabilities upon which no interest is paid	**413**	**–**	**–**

22 Analysis of Financial Assets and Liabilities continued

The interest rate risk profile of the financial liabilities of the Company as at 31 March 2012 was as follows:

	Total £000	Weighted average interest rate %	Period until maturity Years
Amounts drawn down under revolving credit loan facility	15,000	3.96	0.22
Derivative financial instruments	75	0.33	4.22
Financial liabilities upon which no interest is paid	1,682	–	–

The maturity profile of the Company's financial liabilities is as follows:

	31 March 2013 £000	31 March 2012 £000
In one year or less	**15,413**	16,682
In more than one year but not more than two years	**–**	–
In more than two years but not more than five years	**554**	75
	15,967	16,757

The Company had nil undrawn under the fixed Revolving Credit Loan Facility at 31 March 2013 (2012: nil).

The Company's Revolving Credit Loan Facility is measured at cost and denominated in sterling. All other financial liabilities are in sterling and disclosed at fair value. It is considered that, because of the short-term nature of the facility, cost approximates to fair value.

23 Capital Management Policies

The objective of the Company is to achieve capital appreciation through investing in small quoted companies listed on the London Stock Exchange or traded on AIM and to achieve relative outperformance of its benchmark, the FTSE SmallCap (excluding Investment Companies) Index. No unquoted investments are permitted. In pursuing this long-term objective, the Board has a responsibility for ensuring the Company's ability to continue as a going concern. It must therefore maintain an optimal capital structure through varying market conditions. This involves the ability to: issue and buy back share capital within limits set by the shareholders in general meeting; borrow monies in accordance with the Articles of Association; and pay dividends to shareholders out of distributable revenue reserves.

Details of Ordinary share capital are set out in note 16 on page 36. Dividend payments are set out in note 8 on page 33.

	31 March 2013 £000	31 March 2012 £000
Called-up share capital	**3,348**	3,348
Share premium account	**19,307**	19,307
Capital redemption reserve	**1,362**	1,362
Special reserve	**4,642**	4,642
Capital reserve	**144,259**	113,343
Distributable revenue reserve	**4,233**	4,146
Total equity shareholders' funds	**177,151**	146,148

The Company's objectives for managing capital are the same as the previous year and have been complied with throughout the year.

24 Previous Commitments and Contingent Liabilities

At 31 March 2013, there were nil capital commitments (2012: nil).

25 Related Party Transactions

Under the Listing Rules the Manager is regarded as a related party of the Company. The amounts paid to the Manager are disclosed in note 3. However, the existence of an independent Board of Directors demonstrates that the Company is free to pursue its own financial and operating policies, and therefore, in terms of FRS 8: "Related Party Transactions", the Manager is not considered a related party. The relationship between the Company, its Directors and the Manager is disclosed in the Directors' Report.

Company Summary

Current Investment Objective
MUSCIT's investment objective is capital appreciation through investing in small quoted companies listed on the London Stock Exchange or traded on the Alternative Investment Market ("AIM") and to achieve relative outperformance of its benchmark, the Numis Smaller Companies Index (excluding Investment Companies) ("NSCI").

No unquoted investments are permitted.

The benchmark to 31 March 2013 was the FTSE SmallCap (excluding Investment Companies) Index ("SmallCap").

Current Investment Policy
The Company seeks to achieve its objective and to diversify risk by investing in a portfolio of quoted UK smaller companies. At the time of initial investment, a potential investee company must be profitable and smaller than the largest constituent of the NSCI, which represents the smallest 10% of the UK Stock Market by value. At the start of 2013, this was any company below £2.3 billion in size. The Manager focuses on the smaller end of this Index.

In order to manage risk the Manager will normally limit any one holding to a maximum of 4% of the Company's investments. The portfolio weighting of each investment is closely monitored to reflect the underlying liquidity of the particular company. The Company's AIM exposure is also closely monitored by the Board and is limited to 30% of total investments with Board approval required for exposure to be above 25%.

The Manager is focused on identifying high quality niche companies operating in growth markets. This typically leads the Manager to invest in companies that enjoy high barriers to entry, pricing power, a sustainable competitive advantage and strong management teams. The portfolio is therefore constructed on a "bottom up" basis and there are no sectoral constraints placed on the Manager.

The Board, in consultation with the Manager, is responsible for determining the gearing strategy of the Company. Gearing is used to enhance returns when the timing is considered appropriate. The Company currently has a credit facility of £15 million through ING Bank of which £15 million was drawn as at 31 March 2013. The Board has agreed to limit borrowings to 25% of shareholders' funds.

Benchmark (capital return)
For the year under review the benchmark was the SmallCap. From 1 April 2013 the Company adopted the NSCI.

Gross Assets
£193,118,000 as at 31 March 2013.

Shareholders' Funds
£177,151,000 as at 31 March 2013.

Market Capitalisation
£146,290,000 as at 31 March 2013.

Capital Structure
As at 31 March 2013 and at the date of this report, the Company had 33,475,958 Ordinary shares of 10p each in issue (of which none were held in Treasury).

Wind-up Date
In accordance with the Articles of Association, an Ordinary Resolution will be put to shareholders at the Annual General Meeting to be held on 26 July 2013 to release the Directors from the obligation to convene a General Meeting in 2014 for the purpose of winding up the Company.

Management Fee
The management fee comprises two components: a fixed fee of 1/12 of 1% of the gross assets of the Company, payable monthly in arrears, and a performance fee of 0.1% of the gross assets of the Company for each 1% outperformance (or part thereof) of the Company's NAV against the SmallCap over the financial year, subject to a maximum of 0.5% of the gross assets calculated at the end of the financial year. For further details see page 17.

Administration and Company Secretarial Fees
Secretarial and administrative services are provided by Capita Sinclair Henderson Limited, under an agreement dated 3 November 2011. Fees for these services of £89,000 were paid in the year to 31 March 2013, and are subject to an annual RPI uplift.

Sources of Information
All information contained within the Chairman's Statement and the Manager's Report has been provided by Montanaro Asset Management Limited unless otherwise noted.

Glossary of Terms

Articles
Articles of Association of the Company, being its Constitutional Document.

NAV
NAV stands for Net Asset Value and represents shareholders' funds expressed as an amount per individual share. Shareholders' funds are the total value of a company's assets at current market value less its liabilities.

Discount/Premium
If the share price of an investment trust is lower than the NAV per share, the shares are said to be trading at a discount. The size of the discount is calculated by subtracting the share price from the NAV per share and is usually expressed as a percentage of the NAV per share. If the share price is higher than the NAV per share, the shares are said to be trading at a premium.

Gearing
Gearing is the process whereby growth or decline in the total assets of a company has an exaggerated effect on the NAV of that company's ordinary shares due to the presence of borrowings or share classes with a prior ranking entitlement to capital.

Net Gearing
Net gearing is the total debt, net of cash and equivalents, as a percentage of the total shareholders' funds.

Gross Assets
Gross assets are the sum of both fixed and current assets with no deductions.

Montanaro, Manager or Investment Manager
Montanaro Asset Management Limited.

MUSCIT
Montanaro UK Smaller Companies Investment Trust PLC.

Ongoing Charges (formerly TER)
Ongoing Charges, the Company's expenses (excluding performance fees and interest payable) expressed as a percentage of its average monthly Net Assets.

Shareholder Information

Sources of Further Information
The Company's share price is listed in the Financial Times under "Investment Companies".

Information on the Company is also available on the Company's website: www.montanarouksmaller.co.uk.

Key Dates

31 March 2013	Company year end
June 2013	Annual results
26 June 2013	Ex-dividend
26 July 2013	Annual General Meeting
9 August 2013	Dividend payable
November 2013	Interim results

Half-Yearly Report
To reduce ongoing costs the Board has decided not to print the Half-Yearly Report. The Report will be published on the Company's website: www.montanarouksmaller.co.uk.

Frequency of NAV Publication
The Company's NAV is released to the London Stock Exchange on a daily basis.

ISA Status
The Company's shares are fully eligible for inclusion in ISAs.

AIC
The Company is a member of the Association of Investment Companies.

This document is important and requires your immediate attention. If you are in any doubt as to what action you should take, you are recommended to seek your own financial advice from your stockbroker or other independent adviser authorised under the Financial Services and Markets Act 2000 immediately.

If you have sold or otherwise transferred all of your shares in Montanaro UK Smaller Companies Investment Trust PLC, please forward this document as soon as possible to the purchaser or transferee or to the stockbroker, bank or other agent through whom the sale or transfer was effected for transmission to the purchaser or transferee.

Notice of Annual General Meeting

Notice is hereby given that the Eighteenth Annual General Meeting of the Company will be held at the offices of Montanaro Asset Management Limited, 53 Threadneedle Street, London EC2R 8AR on Friday, 26 July 2013 at 12 noon for the following purposes:

Ordinary Business

RESOLUTION 1 – ORDINARY RESOLUTION
To receive and, if thought fit, to accept the Reports of the Directors and the Auditor and the audited financial statements for the year ended 31 March 2013.

RESOLUTION 2 – ORDINARY RESOLUTION
To receive and, if thought fit, to receive and approve the Directors' Remuneration Report for the year ended 31 March 2013.

RESOLUTION 3 – ORDINARY RESOLUTION
To declare a final dividend of 6.76p per Ordinary share for the year ended 31 March 2013.

RESOLUTION 4 – ORDINARY RESOLUTION
To re-elect David Gamble as a Director of the Company.

RESOLUTION 5 – ORDINARY RESOLUTION
To re-elect Kathryn Matthews as a Director of the Company.

RESOLUTION 6 – ORDINARY RESOLUTION
To re-appoint KPMG Audit Plc as Auditor to the Company to hold office from the conclusion of this Meeting until the conclusion of the next General Meeting at which financial statements are laid and to authorise the Directors to determine their remuneration.

Special Business

RESOLUTION 7 – SPECIAL RESOLUTION
THAT in substitution for the Company's existing authority to make market purchases of Ordinary shares of 10p each in the capital of the Company ("Ordinary shares"), the Company be and is hereby generally and unconditionally authorised in accordance with Section 701 of the Companies Act 2006 ("the Act") to make market purchases (within the meaning of Section 693(4) of the Act) of Ordinary shares, provided that:

(i) the maximum number of Ordinary shares hereby authorised to be purchased shall be 5,018,046 or, if less, 14.99% of the number of shares in issue immediately following the passing of this resolution;

(ii) the minimum price which may be paid for each Ordinary share is 10p;

(iii) the maximum price payable by the Company for each Ordinary share is the higher of (i) 105% of the average of the mid-market value of the Ordinary shares in the Company for the five business days prior to the date of the market purchase and (ii) the higher of the price of the last independent trade and the highest current bid as stipulated by Article 5(1) of Buy-Back and Stablisation Regulation 2003;

(iv) the authority hereby conferred shall expire at the conclusion of the Annual General Meeting of the Company in 2014, unless such authority is renewed prior to such time; and

(v) the Company may make a contract to purchase Ordinary shares under the authority hereby conferred prior to the expiry of such authority which will or may be executed wholly or partly after the expiration of such authority and may make a purchase of Ordinary shares pursuant to any such contract.

RESOLUTION 8 – ORDINARY RESOLUTION

THAT the Directors of the Company be and are hereby generally and unconditionally authorised (in substitution for any authorities previously granted to the Directors) to the extent unused, pursuant to Section 551 of the Companies Act 2006 (the "Act"), to exercise all the powers of the Company to allot shares and to grant rights to subscribe for, or to convert any security into shares in the Company ("Rights"):

(a) up to an aggregate nominal amount of £1,115,865, (being one-third of the issued share capital (excluding Treasury shares) as at the date of this report); and

(b) comprising equity securities (within the meaning of section 560 of the Act) up to a further aggregate nominal amount of £1,115,865 in connection with an offer by way of a rights issue:

  (i) to holders of Ordinary shares in proportion (as nearly as may be practicable) to their existing holdings; and

  (ii) to holders of other equity securities (if any) as required by the rights of those securities or as the Directors otherwise consider necessary,

  and so that Directors may impose any limits or restrictions and make any arrangements which they consider necessary or appropriate to deal with Treasury shares, fractional entitlements, record dates, legal, regulatory or practical problems in, or under the laws of, any territory or the requirements of any regulatory body or stock exchange or any other matter (including any such problems arising by virtue of equity securities being represented by depositary receipts),

provided that the authorities conferred on the Directors by paragraphs (a) and (b) above shall, unless renewed, varied or revoked by the Company in general meeting, expire at the conclusion of the next Annual General Meeting of the Company after the passing of this resolution, save that the Company may before such expiry make offers or agreements which would or might require shares to be allotted or Rights to be granted after such expiry and so the Directors of the Company may allot shares or grant Rights in pursuance of such offers or agreements as if the authority conferred hereby had not expired.

RESOLUTION 9 – SPECIAL RESOLUTION

THAT, subject to the passing of Resolution 8 above (and in substitution for all subsisting authorities to the extent unused but without prejudice to the exercise of any such power prior to the date hereof), the Directors be and are hereby empowered pursuant to Section 570 and Section 573 of the Companies Act 2006 (the "Act") to allot equity securities (within the meaning of Section 560 of the Act) for cash pursuant to the authority conferred by Resolution 8 as if Section 561 of the Act did not apply to any such allotment, provided that this power shall be limited to the allotment of equity securities:

(a) in connection with an offer of equity securities (but in the case of the authority granted under paragraph (b) of Resolution 8, by way of a rights issue only):

  (i) to holders of Ordinary shares in proportion (as nearly as may be practicable) to their existing holdings; and

  (ii) to holders of other equity securities (if any) as required by the rights of those securities or as Directors otherwise consider necessary,

  and so that the Directors may impose any limits or restrictions and make any arrangements which they consider necessary or appropriate to deal with any Treasury shares, fractional entitlements, record dates, legal, regulatory or practical problems in, or under the laws of, any territory or the requirements of any regulatory body or stock exchange or any other matter (including any such problems arising by virtue of equity securities being represented by depositary receipts); and

(b) otherwise than pursuant to sub-paragraph (a) above, up to an aggregate nominal amount of £167,380 (being 5% of the issued share capital (excluding Treasury shares) as at the date of this report),

and shall expire at the conclusion of the Company's next Annual General Meeting after the passing of this resolution, save that the Company may before such expiry make an offer or agreement which would or might require equity securities to be allotted after such expiry and the Directors may allot equity securities in pursuance of any such offer or agreement as if the power conferred by this resolution had not expired.

Notice of Annual General Meeting continued

RESOLUTION 10 – SPECIAL RESOLUTION

THAT, subject to the passing of Resolution 9 set out above, the Directors of the Company be and are hereby authorised, for the purposes of paragraph 15.4.11 of the Listing Rules of the United Kingdom Listing Authority, to issue Ordinary shares of 10p each in the capital of the Company at a price below the net asset value per share of the existing Ordinary shares in issue, provided always that such issue will be limited to:

(i) an aggregate nominal amount of £167,380, being 5% of the Ordinary shares in issue as at the date of this report;

(ii) the sale of shares which, immediately before such sale, were held by the Company as Treasury shares; and

(iii) the authority contained in Resolution 9 set out above.

RESOLUTION 11 – ORDINARY RESOLUTION

THAT the Directors be released from the obligation to convene a General Meeting during 2014 for the purpose of providing for the Company to be wound-up on a voluntary basis as stated in the Company's Articles of Association.

RESOLUTION 12 – SPECIAL RESOLUTION

THAT a General Meeting other than an Annual General Meeting may be called on not less than 14 clear days' notice.

By order of the Board

CAPITA SINCLAIR HENDERSON LIMITED
Company Secretary
19 June 2013

Registered Office:
Beaufort House
51 New North Road
Exeter EX4 4EP

Note 1: Pursuant to Section 324 of the Companies Act 2006, a member entitled to attend and vote at this meeting may appoint one or more persons as his/her proxy or proxies to attend, speak and vote on his/her behalf at the meeting. A proxy need not be a member of the Company. If multiple proxies are appointed, they must not be appointed in respect of the same shares. To be effective, the enclosed form of proxy, together with any power of attorney or other authority under which it is signed or a notarially certified copy thereof, should be lodged at the office of the Company's Registrar, Capita Registrars, PXS, 34 Beckenham Road, Beckenham, Kent BR3 4TU, not later than 48 hours (excluding non-working days) before the time of the meeting or any adjournment thereof. The appointment of a proxy will not prevent a member from attending the meeting and voting in person if he/she so wishes. A member present in person or by proxy shall have one vote on a show of hands and on a poll every member present in person or by proxy shall have one vote for every Ordinary share of which he/she is the holder. The termination of the authority of a person to act as proxy must be notified to the Company in writing. Amended instructions must be received by the Company's Registrar by the deadline for receipt of proxies. To appoint more than one proxy, shareholders will need to complete a separate proxy form in relation to each appointment (you may photocopy the proxy form), stating clearly on each proxy form the number of shares in relation to which the proxy is appointed. A failure to specify the number of shares to which each proxy appointment relates or specifying an aggregate number of shares in excess of those held by the member will result in the proxy appointment being invalid. Please indicate if the proxy instruction is one of multiple instructions being given. All proxy forms must be signed and should be returned together in the same envelope.

Note 2: Shareholders who hold their shares electronically may submit their votes through CREST, by submitting the appropriate and authenticated CREST message so as to be received by the Company's Registrar not later than 48 hours (excluding non-working days) before the start of the meeting or any adjournment thereof. Instructions on how to vote through CREST can be found by accessing the following website: www.euroclear.com/CREST. Shareholders are advised that CREST is the only method by which completed proxies can be submitted electronically. CREST members who wish to appoint a proxy or proxies by utilising the CREST electronic proxy appointment service may do so for this meeting and any adjournment thereof by following the procedures described in the CREST Manual. CREST personal members or other CREST sponsored members, and those CREST members who have appointed a voting service provider(s), should refer to their CREST sponsor or voting service provider(s), who will be able to take the appropriate action on their behalf. In order for a proxy appointment or instruction made by means of CREST to be valid, the appropriate CREST message (a "CREST Proxy Instruction") must be properly authenticated in accordance with Euroclear UK & Ireland Limited's specifications and must contain the information required for such instructions, as described in the CREST Manual (available via www.euroclear.com/crest). The message, in order to be valid, must be transmitted so as to be received by the Company's agent (ID RA10) by the latest time for receipt of proxy appointments specified in Note 1 above. For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by the CREST Applications Host) from which the Company's agent is able to retrieve the message by enquiry to CREST in the manner prescribed by CREST. After this time, any change of instructions to proxies appointed through CREST should be communicated to the appointee through other means. CREST members and, where applicable, their CREST sponsors or voting service providers should note that Euroclear UK & Ireland Limited does not make available special procedures in CREST for any particular messages. Normal system timings and limitations will therefore apply in relation to the input of CREST Proxy Instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member is a CREST personal member or sponsored member or has appointed a voting service provider(s), to procure that his CREST sponsor or voting service provider(s) take(s)) such action as shall be necessary to ensure that a message is transmitted by means of the CREST system by any particular time. In this connection, CREST members and, where applicable, their CREST sponsors or voting service providers are referred, in particular, to those sections of the CREST Manual concerning practical limitations of the CREST system and timings. The Company may treat as invalid a CREST Proxy Instruction in the circumstances set out in Regulation 35(5) (a) of the Uncertificated Securities Regulations 2001.

Note 3: A person to whom this notice is sent who is a person nominated under Section 146 of the Companies Act 2006 to enjoy information rights (a "Nominated Person") may, under an agreement between him/her and the shareholder by whom he/she was nominated, have a right to be appointed (or to have someone else appointed) as a proxy for the Annual General Meeting. If a Nominated Person has no such proxy appointment right or does not wish to exercise it, he/she may, under any such agreement, have a right to give instructions to the shareholder as to the exercise of voting rights. The statements of the rights of members in relation to the appointment of proxies in Note 1 above do not apply to a Nominated Person. The rights described in this Note can only be exercised by registered members of the Company.

Note 4: As at 18 June 2013 (the business day prior to the publication of this notice) the Company's issued share capital amounted to 33,475,958 Ordinary shares carrying one vote each. The total voting rights in the Company as at 18 June 2013 were 33,475,958 votes.

Note 5: Pursuant to Regulation 41 of the Uncertificated Securities Regulations 2001, as amended and/or the purposes of Section 360B of the Companies Act 2006, the Company specifies that only those Shareholders registered on the Register of Members of the Company as at 6.00 pm on 24 July 2013 (or, in the event that the meeting is adjourned, only those Shareholders registered on the Register of Members of the Company as at 6.00 pm on the day which is two days prior to the adjourned meeting) shall be entitled to attend in person or by proxy and vote at the Annual General Meeting in respect of the number of shares registered in their name at that time. Changes to entries on the Register of Members after that time shall be disregarded in determining the rights of any person to attend or vote at the meeting.

Note 6: In accordance with Section 319A of the Companies Act 2006, the Company must cause any question relating to the business being dealt with at the meeting put by a member attending the meeting to be answered. No such answer need be given if:

a) to do so would:
   (i) interfere unduly with the preparation for the meeting, or
   (ii) involve the disclosure of confidential information;
b) the answer has already been given on a website in the form of an answer to a question; or
c) it is undesirable in the interests of the Company or the good order of the meeting that the question be answered.

Note 7: A corporation which is a member can appoint one or more corporate representatives who may exercise, on its behalf, all its powers as a member provided that no more than one corporate representative exercises powers over the same share.

Notice of Annual General Meeting continued

Note 8: Members should note that it is possible that, pursuant to requests made by members of the Company under Section 527 of the Companies Act 2006, the Company may be required to publish on a website a statement setting out any matter relating to: (i) the audit of the Company's accounts (including the auditor's report and the conduct of the audit) that are to be laid before the Annual General Meeting; or (ii) any circumstances connected with an auditor of the Company ceasing to hold office since the previous meeting at which annual accounts and reports were laid in accordance with Section 437 of the Companies Act 2006. The Company may not require the members requesting any such website publication to pay its expenses in complying with Sections 527 or 528 of the Companies Act 2006. Where the Company is required to place a statement on a website under Section 527 of the Companies Act 2006, it must forward the statement to the Company's auditor not later than the time when it makes the statement available on the website. The business which may be dealt with at the Annual General Meeting includes any statement that the Company has been required under Section 527 of the Companies Act 2006 to publish on a website.

Note 9: A copy of this and, if applicable, any members' statements, members' resolutions or members' matters of business received by the Company after the date of this Notice, will be available on the Company's website: www.montanarouksmaller.co.uk.

Note 10: The following documents will be available for inspection at the registered office of the Company, and at the offices of Montanaro Asset Management Limited, 53 Threadneedle Street, London EC2R 8AE, during normal business hours on any weekday (Saturdays, Sundays and public holidays excepted) from the date of this notice until the conclusion of the Annual General Meeting:

(a) letters of appointment of the Directors of the Company; and

(b) a copy of the Articles of Association of the Company.

Registered in England and Wales No. 3004101.

Form of Proxy
for use at the Eighteenth Annual General Meeting

I/We (block capitals please)____

Address ____

being a member/members of Montanaro UK Smaller Companies Investment Trust PLC, hereby appoint the

Chairman of the meeting /____________________________________ (see note 1)

for the following number of shares ☐

as my/our proxy to vote for me/us on my/our behalf at the Eighteenth Annual General Meeting of the Company to be held at the offices of Montanaro Asset Management Limited, 53 Threadneedle Street, London EC2R 8AR on Friday, 26 July 2013 at 12 noon and at any adjournment thereof.

Signature ______________________________

Dated ______________________________ 2013

Please indicate with an X in the spaces below how you wish your votes to be cast.

☐ Please tick here to indicate that this proxy appointment is one of multiple appointments being made.

		For	Against	Withheld
RESOLUTION 1	To receive the Reports of the Directors and Auditor and the audited financial statements for the year ended 31 March 2013.			
RESOLUTION 2	To approve the Directors' Remuneration Report for the year ended 31 March 2013.			
RESOLUTION 3	To declare a final dividend of 6.76p per Ordinary share for the year ended 31 March 2013.			
RESOLUTION 4	To re-elect David Gamble as a Director of the Company.			
RESOLUTION 5	To re-elect Kathryn Matthews as a Director of the Company			
RESOLUTION 6	To re-appoint KPMG Audit Plc as Auditor and to authorise the Directors to determine their remuneration.			
RESOLUTION 7	That the Company be authorised to make market purchases of up to 14.99% of its Ordinary shares.			
RESOLUTION 8	To allot relevant securities in accordance with Section 551 of the Companies Act 2006.			
RESOLUTION 9	To allot relevant securities for cash and to disapply pre-emption rights, in accordance with Sections 570 and 573 of the Companies Act 2006.			
RESOLUTION 10	To issue shares held in Treasury at a discount to net asset value.			
RESOLUTION 11	To release the Directors from the obligation to convene a General Meeting during 2014 to propose the winding up of the Company.			
RESOLUTION 12	To hold a General Meeting on not less than 14 clear days' notice.			

Notes

1 A member may appoint a proxy of his or her own choice. If such an appointment is made, delete the words "the Chairman of the Meeting" and insert the name of the person appointed proxy in the space provided.

2 The "Vote Withheld" option is provided to enable you to instruct the registered holder to abstain from voting. A "Vote Withheld" is not a vote in law and will not be counted in the calculation of the proportion of the votes "For" or "Against" a Resolution.

3 You are entitled to appoint more than one proxy provided that each proxy is appointed to exercise rights attached to a different share or shares held by you. You may not appoint more than one proxy to exercise rights attached to any one share. To appoint more than one proxy, (an) additional Proxy Form(s) may be obtained by contacting the Registrars helpline on 0871 664 0300 if calling within the UK or +44 20 8639 3399 if calling from outside the UK. Lines are open 8:30am – 5:30pm Monday–Friday. Calls to the helpline from within the UK cost 10p per minute (including VAT) from a BT landline. Other service providers' costs may vary. Calls to the helpline from outside the UK will be charged at applicable international rates. Calls may be recorded and monitored for security and training purposes. Or you may photocopy this form. Please indicate in the box next to the proxy holder's name the number of shares in relation to which they are authorised to act as your proxy. Please also indicate by ticking the box provided, if the proxy instruction is one of multiple instructions being given. All forms must be signed and should be returned together in the same envelope.

4 If the appointor is a corporation, this form must be under its common seal or under the hand of some officer or attorney duly authorised in that behalf.

5 In the case of joint holders, the signature of any one holder will be sufficient, but the names of all the joint holders should be stated.

6 If this form is returned without any indication as to how the person appointed proxy shall vote, he/she will exercise his/her discretion as to how he/she votes or whether he/she abstains from voting.

7 To be valid, this form must be completed and deposited at the office of the Registrar of the Company by post to Capita Registrars, PXS, 34 Beckenham Road, Beckenham, Kent BR3 4TU or by hand during normal business hours to Capita Registrars, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4TU, not less than 48 hours before the time fixed for holding the meeting or adjourned meeting.

Please see enclosed self addressed envelope for return of this proxy form.

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