MONTANARO

UK Smaller Companies Investment Trust PLC

Annual Report and Accounts 2016

The Montanaro UK Smaller Companies Investment Trust PLC ("MUSCIT" or the "Company") was launched in March 1995 and its shares are premium listed on the London Stock Exchange.

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.

Contents

Highlights
for the year ended 31 March 2016

Results

	As at 31 March 2016	As at 31 March 2015	% change
Ordinary share price	461.0p	463.0p	-0.4
Net Asset Value ("NAV") per Ordinary share	570.6p	564.7p	1.1
NAV (excluding current period revenue) per Ordinary share	558.4p	554.4p	0.7
Discount to NAV (excluding current period revenue)	17.4%	16.5%	
NSCI*	6,674.2	6,578.9	1.4

* Capital only.

	Year to 31 March 2016	Year to 31 March 2015	% change
Revenue return per Ordinary share	12.1p	10.3p	17.5
Dividend per Ordinary share	10.0p	8.9p	12.4
Gross assets	£219.6m	£207.7m	5.7
Net assets	£191.0m	£189.0m	1.1
Market capitalisation	£154.3m	£155.0m	-0.4
Net gearing employed*	9.9%	5.4%	
Ongoing charges	1.2%	1.2%	
Portfolio turnover**	16.5%	19.3%	

* Borrowing net of cash.
** Calculated using average transactions as a percentage of the average total Investments at fair value during the year.

Performance

Capital Return	1 year	3 year	5 year	10 year	Since launch
Share price	-0.4	5.5	29.9	73.6	385.3
NAV (excluding current period revenue)	0.7	6.9	34.8	84.1	466.3
Benchmark*	1.4	20.4	45.1	9.2	125.0

Total Return	1 year	3 year	5 year	10 year	Since launch
Share price**	1.2†	10.8†	41.7†	108.2†	459.0
NAV**	2.5†	12.5†	45.6†	114.5†	549.9
Benchmark*	4.2	31.0	67.6	47.3	314.8

* The Benchmark is a composite index comprising the FTSE SmallCap Index (excluding investment companies) until 31 March 2013 and the NSCI from 1 April 2013 onwards.

** Returns have been adjusted for dividends paid.

† Source: The Association of Investment Companies ("AIC").

Strategic Report

Chairman's Statement

Background

I am pleased to present the twenty-first 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 £191 million.

In spite of all the recent economic and political uncertainty, we continue to believe that our Investment Trust offers a very attractive investment opportunity. The closed-ended structure is ideal for shareholders to invest in quoted UK "smaller" companies which are less well-researched and more illiquid than larger, blue chip companies, without having to be concerned about the impact of cash flows that affect open-ended funds.

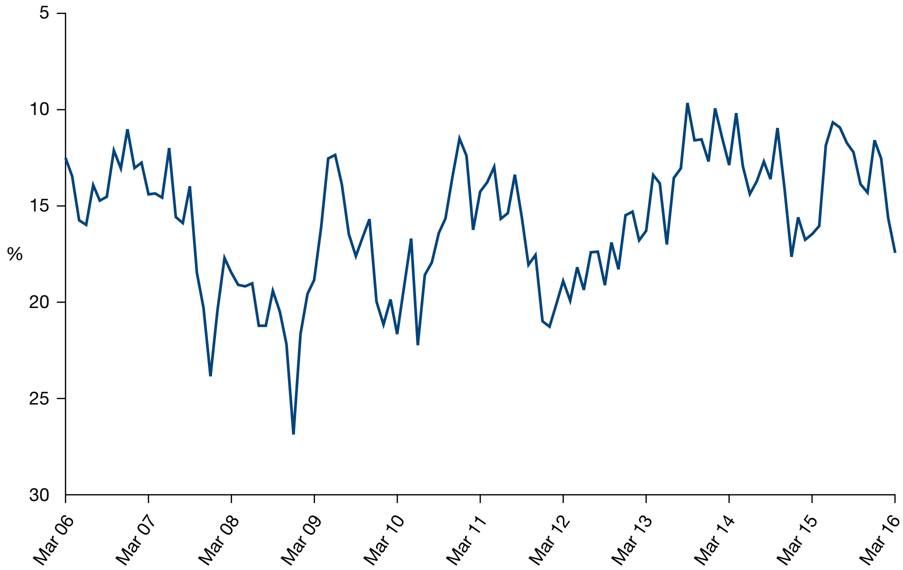
Results

In the year to 31 March 2016, the NAV of MUSCIT (excluding current period revenue) rose by 0.7% to 558.4p in comparison with a gain of 1.4% by the NSCI. During the same period, the Company's share price fell by 0.4% to 461.0p reflecting the widening of the discount, which was seen across most investment trusts last year.

Discount

As previously mentioned, the discount of MUSCIT's share price to NAV widened to 17.4% on 31 March 2016, reflecting investors' uncertainty over the future of the UK and the robustness of the economic recovery.

Share Price Discount to NAV*



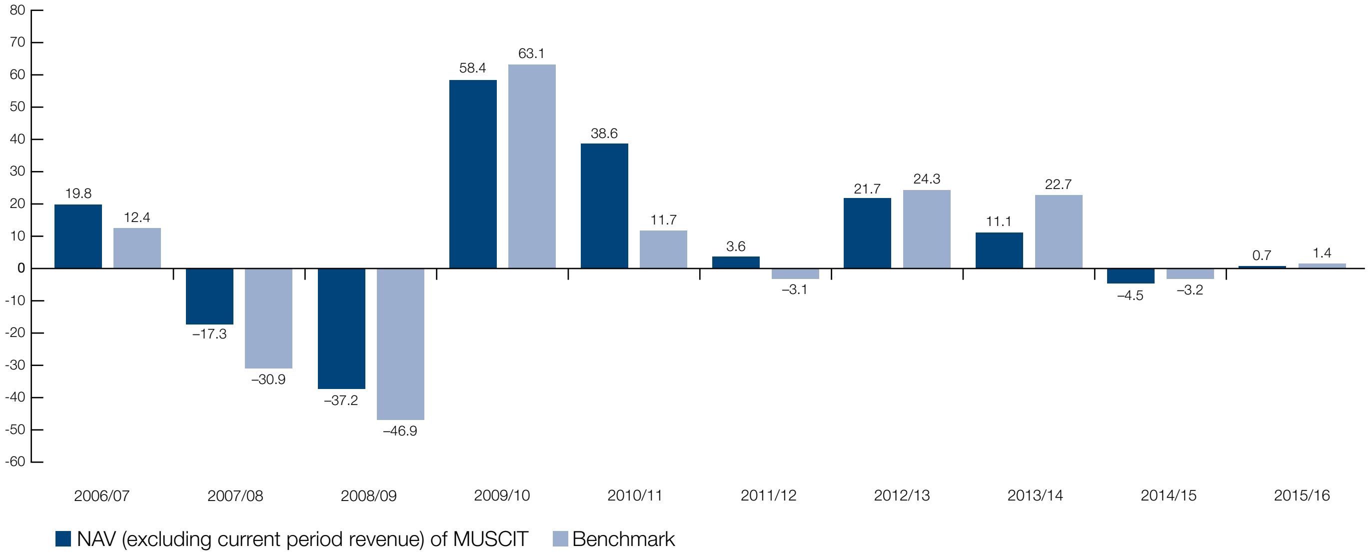
* Discount based on NAV (excluding current period revenue).

Source: Montanaro Asset Management Limited.

Strategic Report continued

Chairman's Statement continued

Annual NAV Performance vs Benchmark



Source: Capita Sinclair Henderson Limited.

Share Buy Backs

The Board is responsible for the implementation of the share buy-back programme which is undertaken at arms' length from Montanaro Asset Management Limited ("Montanaro" or the "Manager"). No shares were bought back during the year.

As at 31 March 2016, no shares were held in Treasury.

Gearing

The Board, in discussion with the Manager, regularly reviews the gearing strategy of the Company and approves the arrangement of any gearing facility to support the strategy. This is a key feature of investment trusts that we believe offers a strong competitive advantage over alternative open-ended investment funds. The ability to gear can significantly enhance investment returns to shareholders and as such the Board strongly encourages active use of the gearing facility by the Manager.

During the course of year, the three-year revolving credit facility with ING Bank, maturing in February 2017 was increased from £10 million to £15 million.

At 31 March 2016, net gearing was 9.9%.

Dividend

MUSCIT's primary aim is to deliver capital growth to its shareholders rather than dividend income. However, the high quality of the companies in which we have been invested has allowed us to maintain a consistent dividend policy. The Board proposes a final dividend of 10.0p per Ordinary share, which represents an increase of 12.4% compared to last year.

Auditor

During the year, as part of good governance, the Audit and Management Engagement Committee undertook an audit tender process. The Committee recommended the appointment of Ernst & Young LLP ("EY") as Auditor. The recommendation was accepted by the Board and the appointment of EY in place of KPMG LLP ("KPMG") will be proposed at the forthcoming Annual General Meeting ("AGM"). The Board would like to thank KPMG for its service over the past 20 years.

Directors

After ten years on the Board, Michael Moule stepped down as a Director on 31 July 2015. The Board would like to thank Michael Moule for his invaluable contribution and contagious enthusiasm during his tenure. He is much missed.

Given the importance and increasing responsibilities of the role of a Chairman of an investment trust and my other commitments, many of which are also in the financial services sector, I have decided to step down as Chairman at the next AGM on 22 July 2016. I will remain on the Board as a Non-Executive Director.

I am delighted that Roger Cuming will be replacing me as Chairman with effect from 22 July 2016. Roger, a Director of the Company since 2009, has a wealth of experience in the investment industry and in investment trusts in particular. Following Roger's appointment as Chairman, Kate Bolsover will replace him as Senior Independent Director.

Outlook

The economic outlook for the UK remains encouraging, supported by record low interest rates, weaker Sterling and a benign inflation outlook. Historically, such a backdrop has proven to be positive for smaller companies, which tend to derive a greater portion of their profits from the domestic economy than larger companies.

However, much of the stock market's attention over the coming months will be drawn to the "Brexit" debate in the run-up to the 23 June referendum. The odds of the "Remain" or "Exit" choices remain too close to call: emotions will play an important part in the outcome of what is a complex question. Regardless of the result, we are hoping that the referendum will bring some welcome clarity to the UK's future within the European Union.

It is important that politics do not divert SmallCap investors' attention away from making long-term investment decisions. It is interesting to note that over the past 60 years, during which the UK has experienced periods of political upheaval and economic hardship, quoted smaller companies have outperformed larger companies by 3.5% per annum on average.

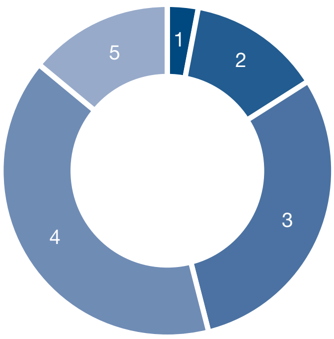
The UK SmallCap market remains less well-researched and is becoming increasingly so as competition and new regulations such as MiFID II cause brokers to withdraw from the market. We remain confident that current conditions will continue to offer investment opportunities for those in a position to complete the in-house research and due diligence required. With one of the largest specialist SmallCap teams in Europe, we believe that the Manager is well placed to seize the attractive opportunities that often emerge during periods of political uncertainty.

KATHRYN MATTHEWS
Chairman
10 June 2016

Strategic Report continued

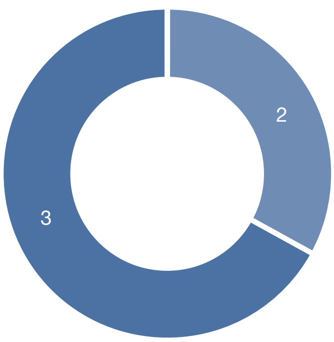
Manager's Report

Breakdown by Market Cap (Ex Cash)



1	£0–£250m	3%
2	£250m–£500m	13%
3	£500m–£1bn	30%
4	£1bn–£1.5bn	40%
5	>£1.5bn	14%

Breakdown by Index (Ex Cash)



1	FTSE 100	0%
2	FTSE 250*	33%
3	NSCI	67%
4	UK AIM	0%

Montanaro

Montanaro was established in 1991. We have one of the largest and most experienced specialist teams in the UK dedicated exclusively to researching and investing in quoted European small companies. We have a team of 29, which gives us the benefit of local contacts and knowledge that is so essential.

At 31 March 2016, Montanaro's assets under management were over £2 billion.

Investment Philosophy and Approach

Montanaro specialises in quoted UK small companies with a particular focus on those with a stock market value below £1 billion at the time of investment.

Investment ideas typically are generated internally, rather than through brokers, and are researched in detail in-house. With around 2,000 UK companies within our universe, we are spoilt for choice. There is never a shortage of exciting new ideas. Before conducting detailed research on an individual company, we gather and carefully review extensive trade and industry data to help us to understand the sector in which a company operates and its growth drivers.

Investments are focused exclusively on companies that are profitable. We are mindful of our 'circle of competence' – complicated, blue-sky companies are not for us. We focus on companies we can understand, typically niche franchises with good and experienced management, sound finances, simple business models, good order visibility, high barriers to entry, a strong, normally dominant market position and a competitive advantage that ensures pricing power. If there is a choice of more than one company in a specific sector, we would normally invest in the market leader. We prefer companies that can demonstrate self-funded organic growth rather than those on the acquisition treadmill.

We believe that *"you get what you pay for in life"* – it is worth paying more for a higher quality company. We like cash-generative companies with high operating profit margins, an indicator that they are providing goods or services of value to their clients, which are better able to withstand a downturn. We carefully assess potential catalysts for share price performance such as positive news flow. We never lose sight of our primary goal, which is to make money for shareholders through sound investment based on our own rigorous, fundamental analysis. We also take a conservative approach. We also believe that it is right and proper to align our interests with those of our investors – we invest in our own funds.

* Represents those holdings that are in the FTSE 250 and are above the threshold for the NSCI.

To ensure that we remain well informed, we regularly visit the companies in which we invest. This is the fun part of the job and where we feel we can add the most value. We place great emphasis on management and seek to gain an understanding of their goals and aspirations by seeing them operate in their own environment. It is a privilege to meet them. The track record of executives is examined in detail along with board structure, the level of insider ownership and the emphasis placed by management on sound corporate governance. Good communication and regular dialogue with management are an important part of our investment process. We are more interested in where an industry and a specific company will be in 5–10 years than its next set of figures. We are genuine long-term investors, seemingly an increasing rarity these days.

We believe that the major risk of investing in quoted UK small companies is stock specific. Having a high level of in-house resources and a disciplined investment process means that we are well-equipped to manage this risk. In addition, we have a number of risk disciplines aimed at limiting our exposure to a particular sector or company. For example, if a stock reaches a 4% weighting in the portfolio, we will consider reducing our exposure even if we believe the outlook is still positive – no company is immune to external shocks or unexpected surprises.

In summary, we invest in well managed, high-quality companies in growth markets at sensible valuations. We are long-term investors and keep turnover and transaction costs low. We follow the companies in which we invest very closely over many years, measured more in decades than the short-termism of others. We would rather pay more for a higher quality, more predictable company that can be valued with greater certainty. We like to sleep at night.

The Portfolio

The portfolio at 31 March 2016 consisted of 45 companies of which the top ten holdings represented 35.5%.

At 31 March 2016, the Company held no investments in companies traded on AIM.

Sector distribution within the portfolio is driven by stock selection. Although weightings relative to the market are monitored, overweight and underweight positions are held based on where the greatest value and upside are perceived to be.

Review

UK SmallCap eked out a positive return in the fiscal year to 31 March 2016 with the NSCI returning 1.4%. By comparison, the Company's NAV (excluding current period revenue) rose by 0.7%. It was reassuring to have protected our investors' capital in a challenging and volatile market environment which saw the FTSE All-Share Index decline by 7.3%.

During the first nine months of the fiscal year the Company performed well, returning 8.1% and outperforming the benchmark index by more than 5%. In this period, UK SmallCap acquired something of a "safe haven" status. The asset class was rewarded for its domestic focus on concerns over the outlook for the global economy. Meanwhile, the portfolio also benefited from its low exposure to weak commodity markets.

The final three months of the review period proved in sharp contrast to this. Investor enthusiasm for UK SmallCap was dampened by market volatility emanating from China and concerns closer to home in the form of "Brexit". It was no surprise that the "risk-off" attributes of gold proved popular. In addition, relative performance was impacted by a rebound in low quality energy and materials stocks to which we have little exposure, while the cyclical rally was given further fuel by the announcement of yet more quantitative easing in Europe.

Gearing

The Alternative Investment Fund Manager ("AIFM"), in consultation with the Board, is responsible for determining the gearing levels of the Company. In 2015, the Company started the financial year with a modest level of gearing at 5.4%. Gearing rose after the weak summer months, reaching 9.9% by the end of the financial year.

Outlook

Mark Twain, the American author, once quipped that *"History doesn't repeat itself but it often rhymes"*. Whilst he was not thinking of UK SmallCap when he said this, the behaviour of the asset class follows his observation with remarkable precision. Research we conducted in 2009 (using data going back to the 1950s) showed that SmallCap outperformed LargeCap during bull markets by an average of 8% per annum As we updated our analysis to include the current bull market that began in March 2009, we found that SmallCap had outperformed by no less than 8.3% per annum during this period. With such forecasting skills, Mark Twain could have made quite a career as a SmallCap investor.

The primary reason for this outperformance has been the relative strength of the UK economy since the financial crisis. Real GDP growth over the last six years has averaged 2% per annum, broadly in line with the United States and comfortably ahead of Germany (1.6%), France (1%) and Japan (0.7%). Alongside this, employment and consumer confidence, the twin drivers of household consumption, have rebounded. Looking ahead, we expect low interest rates and cheap fuel costs, combined with a positive wealth effect from rising home prices, to continue to support consumers' purchasing power.

Strategic Report continued

Manager's Report continued

In light of this, it is natural to ask where SmallCap is headed from here. According to Professors Dimson and Marsh, at the end of March 2016 the NSCI was trading on a trailing P/E of 13.8x, which compared to a multiple of 17.3x for the FTSE All-Share Index. The last six years of outperformance have therefore not eroded the attractiveness of SmallCap on valuation grounds. A 20% discount is significant and can be attributed, at least in part, to the more robust earnings momentum within the SmallCap market. Reassuringly, it is also a sign that investor exuberance is not yet upon us. The bull market may well have further to run.

Furthermore, small company balance sheets are in good shape; in many respects, balance sheets and cash positions are stronger than ever. Indeed, SmallCap dividends appear safer than those of larger companies, with the dividend cover of the FTSE 250 at 2.2x compared to 0.9x for the FTSE 100 (Source: Financial Times). Rarely have we seen such a flurry of LargeCap dividend cuts than over the past twelve months.

Although markets ended the fiscal year in "risk-off" mode, there are two reasons for cautious optimism. The first is that the recent reporting season suggests that investors are again focusing on company fundamentals, rewarding businesses that deliver and punishing those that underachieve. Secondly, any market weakness in the run-up to the EU referendum on 23 June may lead to an attractive entry point for UK SmallCap investors.

As we enter a new fiscal year, we are encouraged by the greater dispersion of returns within the UK market, coupled with valuations that are more attractive compared to this time last year. As always, we will remain highly selective in our investment approach, focusing exclusively on those smaller companies that meet our stringent quality and growth standards. We look forward to the future with confidence.

MONTANARO ASSET MANAGEMENT LIMITED
10 June 2016

The Company

MUSCIT is a closed-ended investment trust and its shares are premium listed on the London Stock Exchange with registration number 3004101. It has been granted approval from HM Revenue & Customs ("HMRC") as an investment trust under s1158/1159 of the Corporation Tax Act 2010 ("s1158/1159"), subject to there being no serious breaches of the conditions for approval.

Rules introduced by HMRC 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 ("Act"). The current portfolio of MUSCIT is such that its shares are eligible for inclusion in ISAs up to the maximum annual subscription limit and the Directors expect this eligibility to be maintained.

INVESTMENT OBJECTIVE

MUSCIT's investment objective is 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 NSCI.

No unquoted investments are permitted.

The Attractions of Quoted Small Companies ("SmallCap")

The key attraction of investing in SmallCap is that investors have the opportunity to make higher returns than from investing in LargeCap. It is easier for small companies to grow faster than it is for large companies; hence they offer investors the potential for higher earnings growth. In the UK, research shows that, since 1954, SmallCap equities have outperformed LargeCap by an average of 3.5% per annum ("the SmallCap Effect"). As a result, investors have received seven times higher returns.

The SmallCap market gives investors access to global market-leading companies managed by dynamic entrepreneurs operating in attractive niche markets that are growing. However, due to a lack of broker research and the illiquidity of their shares, it takes time to get to know and understand these companies. This requires a level of in-house resources beyond the scope of most institutional investors. This is why many institutions are attracted to the asset class and equally why they will often outsource the day-to-day investment decisions to dedicated specialists such as Montanaro.

INVESTMENT POLICY

The Company seeks to achieve its objective and to manage risk by investing in a diversified portfolio of quoted UK small companies. At the time of initial investment, a potential investee company must be profitable and no bigger than the largest constituent of the NSCI, which represents the smallest 10% of the UK Stock Market by value. At the start of 2016, this was any company below £1.3 billion in size. The Manager focuses on the smaller end of this Index.

In order to manage risk, the Manager limits any one holding to a maximum of 4% of the Company's investments at the time of initial investment. 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 above 25%. The Company currently has a small exposure to investments in companies traded on AIM.

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.

The AIFM in consultation with the Board, is responsible for determining the gearing levels of the Company and has determined that the Company's borrowings should be limited to 25% of shareholders' funds. Gearing is used to enhance returns when the timing is considered appropriate. The Company currently has credit facilities of £30 million with ING Bank, of which £28 million was drawn down at 31 March 2016 (amounting to net gearing of 9.9%).

COMPANY INFORMATION

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 weighted average discount than when they were originally purchased and to produce a positive absolute return.

At 31 March 2016, no shares were held in Treasury.

Benchmark

Following a review to assess the most appropriate benchmark against which its performance should be measured, the Company adopted the NSCI on 1 April 2013. Prior to this date, the benchmark was the FTSE SmallCap Index. Both benchmarks excluded investment companies.

Strategic Report continued

The Company continued

Dividends

The results for the year are shown in the Income Statement on page 31. The Directors recommend that a final dividend of 10.0p (2015: final 8.9p) per Ordinary share, amounting to £3,348,000 (2015: £2,979,000) be paid on 10 August 2016 to shareholders on the share register at the close of business on 1 July 2016.

Directors

After ten years on the Board, Michael Moule retired on 31 July 2015.

The Board strives to maintain a diversity of age, skills, gender and experience. At 31 March 2016, the Board comprised two female and two male Directors.

Corporate Governance

The Directors have reviewed the recommendations of the AIC Code of Corporate Governance (the "AIC Code"). 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.

AIFMD

The Alternative Investment Fund Managers' Directive ("AIFMD") relates to European legislation that creates a European-wide framework for regulating managers of alternative investment funds ("AIFs"). Closed-ended investment companies fall within the remit of these regulations, which came fully into force on 22 July 2014.

In order to comply with the AIFMD, the Company appointed Montanaro as its AIFM and Bank of New York ("BONY") as Depositary and Custodian.

ANALYSIS OF PERFORMANCE USING KEY PERFORMANCE INDICATORS ("KPIs")

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

The NAV per Ordinary share (excluding current period revenue), at 31 March 2016 was 558.4p. Over the previous ten years and since launch, the NAV has increased by 84.1% and 466.3% respectively. In comparison, the benchmark has increased by 9.2% over the previous ten years and 125.0% since launch.

The Level of Discount

The discount of MUSCIT's share price to NAV (excluding current period revenue) stood at 17.4% on 31 March 2016 in comparison with a weighted sector average of 12.8%.

The Ongoing Charges

	2016	2015
Ongoing charges	**1.2%**	1.2%
Finance costs	**0.4%**	0.4%
Total ongoing charges plus performance fees and finance costs	**1.6%**	1.6%

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

ENVIRONMENTAL, HUMAN RIGHTS, EMPLOYEE, SOCIAL AND COMMUNITY ISSUES

The Board recognises the requirement under Section 414C of the Act to detail information about environmental matters, human rights, social and community issues, including information about any policies it has in relation to these matters and the effectiveness of these policies. These requirements do not apply to the Company as it has no employees, all the Directors are non-executive and it has outsourced its functions to third party service providers. Therefore, the Company has not reported further in respect of these provisions.

Socially Responsible Investment

Day-to-day management of the Company's business is undertaken by Montanaro.

The Manager has signed up to the Stewardship Code and has published its voting records on its website.

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

The Company aims to conduct itself responsibly, ethically and fairly.

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 above. The Board has carried out a robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity. A summary of the Company's risk management and internal control processes can be found in the Corporate Governance Statement on pages 22 and 23. Details of MUSCIT's principal risks and how these are mitigated are set out below. The principal financial risks are summarised in note 20 to the financial statements.

Liquidity and Discount Management: The Company's share price performance lags NAV performance due to poor performance, or because SmallCap is out of favour. The Company may become vulnerable to arbitrageurs or a sale from a sizeable shareholder.

The Board regularly reviews the relative level of discount against the sector, the Company's investment performance relative to the competition and the benchmark, and the underlying liquidity of the investments and shareholder register.

Share buybacks cause the size of the Company to become too small to be viable in terms of ongoing charges or for thresholds of institutional investors.

When the Board considers share buybacks it will take into consideration the impact on the size, liquidity and ongoing viability of the Company.

Corporate Ownership and Management Structure of Montanaro: A change in ownership and/or management structure of Montanaro.

The Board has no control over Montanaro's corporate future and any uncertainty that may occur from any changes in it. The Board could change the Manager under the terms of the contract if it was not happy with the new ownership structure. The Board is in regular contact with the senior management of Montanaro.

Poor Investment Performance: Underperformance of benchmark and/or peer group.

A review is undertaken at each Board meeting with the Manager to compare and review the performance of the portfolio with the benchmark and the peer group. In addition, the Board seeks to understand the reasons for any underperformance as well as seeking comfort over consistency of investment approach and style.

Ultimately, the Board can terminate the Investment Management Agreement if unsatisfactory performance is considered irreversible and the causes cannot be rectified.

Risk Oversight: The Manager is taking too much risk in the portfolio leading to unacceptable volatility in performance or there is excessive portfolio turnover.

Risk oversight is primarily the responsibility of the AIFM, but the Board provides additional oversight in its portfolio reviews at each Board meeting. Portfolio turnover is reviewed at each Board meeting.

Key Man Risk: A change in key investment management personnel who are involved in the management of the MUSCIT portfolio could impact on future investment performance and lead to loss of investor confidence.

Montanaro operates a team approach in the management of the portfolio which mitigates against the impact of the departure of any one member of the investment team. There is an identified lead manager within Montanaro offering continuity of communication with MUSCIT's shareholders. The Board is in regular contact with Montanaro and its designated manager and will be asked for their approval to any proposed change in the lead manager.

Operational Risk: Key operational risks include transactions not subject to best execution, counterparty risk, errors in settlement, title and corporate actions, misstatement of NAV and breach of the Investment Policy.

The Board monitors operational issues regularly and reviews them in detail at each Board meeting. The internal control reports of each service provider are reviewed annually.

Breach of Regulation: Failure to comply with the Companies Act 2006, Stock Exchange rules, Financial Conduct Authority ("FCA") Listing Rules and Disclosure & Transparency Rules, Anti-Money Laundering procedures or other applicable regulations.

Shareholder reports and results announcements are reviewed by the Board prior to publication. Annual results are audited prior to release of the document to shareholders. Control reports from the Manager and Administrator are provided to monitor controls over ensuring compliance with applicable laws and regulations.

On behalf of the Board
KATHRYN MATTHEWS
Chairman
10 June 2016

Ten Largest Holdings
as at 31 March 2016

35.5%
of the portfolio

Consort Medical
Health Care, Equipment and Services

Medical device technologies for drug delivery.

Value	Portfolio	Market cap
£8.9m	4.2%	£528m

Marshalls
Construction and Materials

The UK's leading provider of landscaping products.

Value	Portfolio	Market cap
£8.0m	3.8%	£710m

Dechra Pharmaceuticals
Pharmaceuticals and Biotechnology

An international veterinary pharmaceutical business.

Value	Portfolio	Market cap
£7.8m	3.7%	£1,118m

Big Yellow Group
Real Estate/Real Estate Investment Trusts ("REIT")

A REIT focused on the self-storage market.

Value	Portfolio	Market cap
£7.7m	3.7%	£1,219m

NCC Group
Software and Computer Services

Software business specialising in escrow and cyber security.

Value	Portfolio	Market cap
£7.7m	3.7%	£691m

Dignity

General Retailers

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

£7.5m	3.6%	£1,230m
Value	Portfolio	Market cap

Cineworld Group

Travel and Leisure

A leading cinema operator in the UK.

£7.3m	3.5%	£1,426m
Value	Portfolio	Market cap

Domino's Pizza Group

Travel and Leisure

The largest pizza delivery company in the UK.

£6.9m	3.3%	£1,670m
Value	Portfolio	Market cap

Shaftesbury

Real Estate/Real Estate Investment Trusts

A specialist REIT operating in the heart of London's tourist district (Carnaby St, Chinatown, Covent Garden).

£6.3m	3.0%	£2,537m
Value	Portfolio	Market cap

Bovis Homes Group

Household Goods and Home Construction

A house builder operating primarily in the south of England.

£6.3m	3.0%	£1,252m
Value	Portfolio	Market cap

Investment Portfolio
as at 31 March 2016

Holding	Sector	Value £'000	Market cap £m	% of portfolio 31 March 2016	% of portfolio 31 March 2015
Consort Medical	Health Care, Equipment and Services	8,869	528	4.2	3.6
Marshalls	Construction and Materials	8,010	710	3.8	3.5
Dechra Pharmaceuticals	Pharmaceuticals and Biotechnology	7,844	1,118	3.7	3.0
Big Yellow Group	Real Estate/Real Estate Investment Trusts	7,745	1,219	3.7	3.3
NCC Group	Software and Computer Services	7,734	691	3.7	3.1
Dignity	General Retailers	7,454	1,230	3.6	3.2
Cineworld Group	Travel and Leisure	7,256	1,426	3.5	3.6
Domino's Pizza Group	Travel and Leisure	6,864	1,670	3.3	–
Shaftesbury	Real Estate/Real Estate Investment Trusts	6,328	2,537	3.0	2.9
Bovis Homes Group	Household Goods and Home Construction	6,315	1,252	3.0	3.2
Cranswick	Food Producers	6,137	1,061	2.9	2.0
Victrex	Chemicals	6,015	1,409	2.9	2.4
Rathbone Brothers	Financial Services	5,908	1,016	2.8	2.5
McCarthy and Stone	Household Goods and Home Construction	5,753	1,365	2.8	–
Hilton Food Group	Food Producers	5,710	367	2.7	2.5
Jupiter Fund Management	Financial Services	4,993	1,873	2.4	2.5
Clarkson	Industrial Transportation	4,810	671	2.3	2.9
James Fisher and Sons	Industrial Transportation	4,617	662	2.2	2.3
Diploma	Support Services	4,607	841	2.2	2.0
Berendsen	Support Services	4,451	2,076	2.1	2.1
Twenty Largest Holdings		**127,420**		**60.8**	
Entertainment One	Media	4,321	648	2.1	3.0
Halma	Electronic and Electrical Equipment	4,284	3,452	2.1	1.6
Mears Group	Support Services	4,242	427	2.0	2.2
Wilmington Group	Media	4,173	224	2.0	1.2
Helical Bar	Real Estate/Real Estate Investment Trusts	4,053	456	1.9	2.1
Arrow Global Group	Financial Services	4,004	437	1.9	1.6
Ricardo	Support Services	3,976	442	1.9	–
Ted Baker	Personal Goods	3,932	1,197	1.9	2.3
AG Barr	Beverages	3,869	619	1.9	2.2
St. Modwen Properties	Real Estate/Real Estate Investment Trusts	3,845	671	1.8	2.0
Workspace Group	Real Estate/Real Estate Investment Trusts	3,746	1,272	1.8	–
Restaurant Group	Travel and Leisure	3,671	789	1.8	2.6
Renishaw	Electronic and Electrical Equipment	3,670	1,336	1.8	2.1
AVEVA Group	Software and Computer Services	3,648	1,007	1.7	1.7
RPS Group	Support Services	3,320	462	1.6	1.8
Galliford Try	Household Goods and Home Construction	3,200	1,188	1.5	1.6
Ascential	Media	2,974	921	1.4	–
SuperGroup	Personal Goods	2,794	1,154	1.3	1.4
Dialight	Electronic and Electrical Equipment	2,565	185	1.2	1.7
Dunelm Group	General Retailers	2,257	1,852	1.1	1.6
Senior	Aerospace and Defence	2,178	957	1.0	2.2
Paypoint	Support Services	2,057	509	1.0	1.1
Card Factory	General Retailers	1,962	1,114	0.9	–
Brewin Dolphin Holdings	Financial Services	1,945	734	0.9	2.0
ITE Group	Media	1,396	378	0.7	0.9
Total Portfolio		**209,502**		**100.0**	

Analysis of Investment Portfolio by Industrial or Commercial Sector

as at 31 March 2016

Sector	% of portfolio	% of NSCI
Oil and Gas Producers	–	2.8
Oil Equipment, Services and Distribution	–	0.9
Oil and Gas	**–**	**3.7**
Chemicals	2.9	1.9
Industrial Metals	–	0.9
Mining	–	4.1
Basic Materials	**2.9**	**6.9**
Construction and Materials	3.8	3.6
Aerospace and Defence	1.0	1.0
General Industrials	–	1.1
Electronic and Electrical Equipment	5.1	1.8
Industrial Engineering	–	2.3
Industrial Transportation	4.5	1.9
Support Services	10.8	11.8
Industrials	**25.2**	**23.5**
Beverages	1.9	0.6
Food Producers	5.6	3.0
Household Goods and Home Construction	7.3	1.9
Leisure Goods	–	0.6
Personal Goods	3.2	2.0
Consumer Goods	**18.0**	**8.1**
Health Care, Equipment and Services	4.2	2.7
Pharmaceuticals and Biotechnology	3.7	2.9
Health Care	**7.9**	**5.6**
Food and Drug Retailers	–	0.9
General Retailers	5.6	8.1
Media	6.2	3.6
Travel and Leisure	8.6	7.3
Consumer Services	**20.4**	**19.9**
Fixed Line Telecommunications	–	0.9
Telecommunications	**–**	**0.9**
Electricity	–	0.9
Utilities	**–**	**0.9**
Banks	–	1.6
Life and Non-life Insurance	–	4.1
Real Estate/Real Estate Investment Trusts	12.2	10.4
Financial Services	8.0	7.7
Financials	**20.2**	**23.8**
Software and Computer Services	5.4	4.8
Technology Hardware and Equipment	–	1.9
Technology	**5.4**	**6.7**
Total	**100.0**	**100.0**

The investment portfolio comprises 45 listed UK equity holdings.

Directors' Report

Board of Directors

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

Kathryn Matthews – Board Chairman and Nomination Committee Chairman
Kathryn Matthews was appointed a Director on 1 April 2010 and became Chairman of MUSCIT on 27 July 2013. 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, JP Morgan Chinese Investment Trust Plc and Aperam. She is also a member of the Council of the Duchy of Lancaster and is on the board of trustees of the Nuffield Trust.

Kate Bolsover – Remuneration Committee Chairman
Kate Bolsover was appointed a Director on 17 October 2014. She is a non-executive director of JP Morgan American Investment Trust plc and chairman of Fidelity Asian Values plc. She is also chairman of Tomorrow's People Trust Limited and a director of a number of affiliated companies. She worked for Cazenove Group plc and JP Morgan Cazenove between 1995 and 2005 where she was managing director of the mutual fund business and latterly director of Corporate Communications. Prior to this, her work involved business development and mutual funds experience covering countries in the UK, Europe and the Far East.

Roger Cuming – Senior Independent Director
Roger Cuming was appointed a Director on 5 June 2009 and has been in the investment industry for over 35 years. He was head of investments for Reliance Mutual Insurance Society Limited prior to his retirement in December 2015, and was a significant investor in closed and open-ended investments of all types.

James Robinson – Audit and Management Engagement Committee Chairman
James Robinson was appointed a Director on 30 September 2013. He was chief investment officer (investment trusts) and director of hedge funds at Henderson Global Investors prior to his retirement in 2005. A chartered accountant, he has 34 years' investment experience and is a director of Aberdeen New Thai Investment Trust plc, Invesco Asia Trust plc, Fidelity European Values PLC and JP Morgan Elect plc. He is also chairman of Polar Capital Global Healthcare Growth and Income Trust plc and chairman of the investment committee of the British Heart Foundation.

DIRECTORS

The Directors in office at the date of this report are shown on page 16. All served throughout the year under review. Michael Moule was a Director until his resignation on 31 July 2015.

In accordance with the policy adopted by the Board, all Directors will stand for re-election at the forthcoming AGM.

As set out on page 21, the Board carries out an annual review of the performance of the Board, its Committees and the individual Directors. Following the performance review, the Board considers that all Directors contribute effectively, possess the necessary skills and experience and continue to demonstrate commitment to their roles. The Board therefore believes that it is in the best interests of shareholders that each Director is re-elected.

DIVIDEND

Details of the final dividend recommended by the Board are set out in the Strategic Report on page 10.

SHARE CAPITAL

There are currently 33,475,958 Ordinary 10p shares in issue (2015: 33,475,958), none of which are held in Treasury (2015: nil). Holders of Ordinary shares have unrestricted voting rights of one vote per share at all general meetings of the Company.

SECURITIES CARRYING VOTING RIGHTS

The following information is disclosed in accordance with the Large and Medium-Sized 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 above;
- details of the substantial shareholders in the Company are set out on this page;
- the Board's current powers to buy back and issue shares, and proposals for their renewal are disclosed on page 19; and
- 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 to which the Company is party that might affect its control following a successful takeover bid.

MANAGEMENT AGREEMENT

In order to comply with the AIFMD, the Company entered into a new Management Agreement with Montanaro dated 19 June 2014 under which the Manager was appointed by the Company to act as AIFM. Montanaro receives an ongoing fee of £50,000 per annum to act as the Company's AIFM.

The Manager receives a management fee of 0.85% per annum of gross assets and no performance fee.

Except in certain circumstances, the Management Agreement may only be terminated by the Manager on giving 12 months' notice in writing to the Company. The Company shall be entitled to terminate the Agreement by notice in writing to the Manager forthwith, or as at the date specified in such notice. On receiving such notice, the Manager will be entitled to a termination fee of 1% of the gross assets of MUSCIT at the close of business on the last day of the calendar month immediately preceding the effective date of termination of the Agreement.

CONTINUING APPOINTMENT OF MONTANARO

The Board, through the Audit and Management Engagement Committee, keeps under review the performance of the Manager and the level and terms of the management fee. 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 long-term 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.

SUBSTANTIAL SHAREHOLDINGS

At 31 March 2016, MUSCIT had been informed of the following notifiable interests in its voting rights:

Beneficial owner	Ordinary shares	% of voting rights
Derbyshire County Council	2,925,000	8.7
East Riding of Yorkshire Council	2,743,400	8.2
1607 Capital Partners LLC	1,764,000	5.3
Quilter Cheviot Limited	1,671,230	5.0
Newton Investment Management Limited	1,661,565	5.0
Jupiter Asset Management Limited	1,565,000	4.7
Royal London Asset Management Limited	1,534,839	4.6
Montanaro Asset Management Limited	1,300,000	3.9
City of Bradford Metropolitan District Council	1,228,500	3.7

The Company has not been notified of any changes between 31 March 2016 and the date of this report.

GOING CONCERN

The Company's Articles of Association ("Articles") contain a requirement for shareholders to vote on the continuation of the Company at regular intervals. At the Company's AGM held on 26 July 2013, shareholders voted to remove the obligation to convene a General Meeting during 2014 for the purpose of voluntarily winding up the Company.

Directors' Report continued

The Board intends to propose a resolution at the AGM in 2017 to remove the obligation to convene a General Meeting during 2018 for the purpose of voluntarily winding up the Company.

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.

VIABILITY STATEMENT

In accordance with the UK Corporate Governance Code, the Directors have assessed the prospects of the Company over a longer period than the twelve months required by the 'Going Concern' provision. The Board asked the Audit and Management Engagement Committee (the "Committee") to review this new requirement over a three-year period ending 31 March 2019. In the absence of any adverse change to the regulatory environment and to the treatment of UK investment trusts, a rolling three-year period represents the horizon over which the Directors do not expect there to be any significant change to the Company's principal risks or their mitigation and they believe they can form a reasonable expectation of the Company's prospects.

In its review, the Committee took into account the Company's current financial position, its ability to meet liabilities as they fall due and the principal risks as set out in the Strategic Report. The Board concluded that it had a reasonable expectation that the Company would be able to continue in operation during the period under review.

To provide this assessment, the Committee has considered the Company's financial position as described above and its ability to liquidate its portfolio and meet its expenses as they fall due:

- the portfolio comprises solely of cash balances and equity securities traded on the London Stock Exchange. The current portfolio could be liquidated to the extent of 70% within five trading days and there is no expectation that the nature of the investments held within the portfolio will be materially different in future;
- the portfolio currently has a small exposure to investments traded on AIM;
- the expenses and interest payments of the Company are predictable and modest in comparison with the assets;
- there are no expected capital outlays; and
- the Company has no employees, with only non-executive Directors and consequently does not have potential employment related liabilities.

The Committee, as well as considering the principal risks on page 11 and the financial position of the Company as set out above, has also taken account of the following assumptions in considering the Company's longer-term viability:

- the Board and the Manager will continue to adopt a long-term view when making investments, and anticipated holding periods can be at least five years;
- it is reasonable to believe that the Company will extend the loan facilities currently provided by ING Bank when they expire in December 2016 and February 2017 respectively;
- the Company invests principally in the securities of quoted UK smaller companies to which investors will wish to continue to have exposure;
- the Company has a large margin of safety over the covenants on its debt;
- there will continue to be demand for investment trusts;
- regulation will not increase to a level that makes the running of the Company uneconomical; and
- the performance of the Company will continue to be satisfactory.

Based on the results of this analysis, the Directors have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the three-year period of their detailed assessment.

FINANCIAL RISK MANAGEMENT

The principal financial risks and the Company's policies for managing these risks are set out in note 20 to the financial statements.

GLOBAL GREENHOUSE GAS EMISSIONS

The Company has no greenhouse gas emissions to report from the operations of the Company, nor does it have responsibility for any other emissions producing sources under the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013.

INFORMATION TO BE INCLUDED IN ANNUAL REPORT IN ACCORDANCE WITH LISTING RULE 9.8.4R

Listing Rule 9.8.4R requires the Company to include certain information in a single identifiable section of the Annual Report or a cross reference table indicating where the information is set out. The Directors confirm that there are no disclosures to be made in this regard.

AUDITOR

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/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the Company's Auditor is aware of that information.

As disclosed on page 4, the audit for the financial year ending 31 March 2017 was tendered during the year. Having not been invited to tender, KPMG intends to resign as the Company's Auditor at the conclusion of the AGM. Following a competitive tender process, and on the recommendation of the Audit and Management Engagement Committee, the Board intends to appoint Ernst & Young ("EY") as the Company's Auditor. Accordingly, a resolution to appoint EY and to authorise the Directors to agree its remuneration will be proposed at the forthcoming AGM.

ANNUAL GENERAL MEETING

The Notice of the AGM to be held on 22 July 2016 (the "Notice") is set out on pages 48 to 52. Resolutions 1 to 8, 10 and 12 will be proposed as Ordinary Resolutions and Resolutions 9, 11 and 13 will be proposed as Special Resolutions.

Purchase of Own Shares

At the Company's AGM held on 31 July 2015, the Company was granted authority to purchase up to 14.99% of the Company's Ordinary shares in issue at that date, amounting to 5,018,046 shares. No shares have been bought back under this authority.

A resolution to renew MUSCIT's authority to purchase (either for cancellation or for placing into Treasury) up to 5,018,046 Ordinary shares (being 14.99% of the issued Ordinary share capital as at the date of this report), will be put to shareholders as Resolution 9 at the AGM. Purchases will be made on the open market and prices will be in accordance with the terms laid out in Resolution 9. The authority will be used where the Directors consider it to be in the best interests of shareholders.

Authority to Issue Shares and Disapplication of Pre-Emption Rights

Resolution 10, if passed, will give the Directors the general authority (pursuant to paragraph (a) of the Resolution) to allot Ordinary shares up to an aggregate nominal amount of £1,115,865, representing approximately one-third of MUSCIT's issued Ordinary shares. Upon the passing of Resolution 10 the Directors will also 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. No shares are currently held in Treasury. The authority will be used where the Directors consider it to be in the best interests of shareholders.

Resolution 11, subject to the passing of Resolution 10, will give the Directors the general authority, in accordance with institutional guidelines, to allot Ordinary shares (including issues out of Treasury) for cash, up to an aggregate nominal amount of £167,380, representing approximately 5% of the issued Ordinary shares and at a price above net asset value per share, in respect of new issues of shares, without having to offer such shares to existing shareholders in proportion to their existing holdings. See Resolution 12 in relation to sales of Treasury Shares.

The authorities for the above Resolutions will expire at the conclusion of the Company's next AGM after the passing of the Resolutions.

Authority to Issue Treasury Shares at a Discount

Resolution 12, subject to the passing of Resolution 11, 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 weighted average discount than when they were originally purchased.

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

Notice Period for General Meetings

Resolution 13, if passed, will allow the Directors to hold a General Meeting, other than an AGM, on a minimum of 14 clear days' notice. The notice period for AGMs 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 expeditiously.

Full details of these Resolutions are provided in the Notice of AGM.

The Directors consider that all Resolutions to be proposed at the AGM 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
10 June 2016

Corporate Governance Statement

The Corporate Governance Statement forms part of the Directors' Report.

COMPLIANCE WITH THE PROVISIONS OF THE AIC CODE

The Board of MUSCIT has considered the principles and recommendations of the AIC Code issued in February 2015 by reference to the AIC Corporate Governance Guide for Investment Companies ("AIC Guide"). The AIC Code, as explained by the AIC Guide, addresses 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.

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.

During the year, the Company has complied with the recommendations of the AIC Code and the relevant provisions of the UK Corporate Governance Code 2014, 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 and executive directors' remuneration (there are no executive directors) 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.

ATTENDANCE AT BOARD AND COMMITTEE MEETINGS

The Company holds at least five Board meetings each year at which the Directors review MUSCIT's investments and all other important issues in relation to the Company's affairs. During the year ended 31 March 2016, six Board meetings were held, one of which was a full-day session devoted entirely to reviewing strategic matters. The number of scheduled Board and Committee meetings attended by each Director is set out below.

	Board		Audit and Management Engagement Committee		Remuneration 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
Kathryn Matthews	6	6	2	2	1	1	1	1
Kate Bolsover	6	6	2	2	1	1	1	1
Roger Cuming	6	6	2	2	1	1	1	1
Michael Moule*	3	3	1	1	1	1	1	1
James Robinson	6	6	2	2	1	1	1	1

* Resigned 31 July 2015.

THE BOARD

The Board consists of four non-executive Directors.

Kathryn Matthews is currently Chairman of MUSCIT. The Board considers her to be independent and to have no conflicting relationships.

Roger Cuming is currently the Senior Independent Director ("SID") of MUSCIT. The Board considers that Roger Cuming is ideally suited to perform the role of the SID.

As reported in the Chairman's Statement on page 4, following the conclusion of the forthcoming AGM, Roger Cuming will replace Kathryn Matthews as Chairman and Kate Bolsover will replace Roger Cuming as SID.

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 or since the year end.

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 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 recommendation of dividends, the approval of press releases and circulars, Board appointments and removals and the membership of Committees. Decisions regarding 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.

PERFORMANCE EVALUATION

The Directors conduct an annual review of the performance of the Board, its Committees and the individual Directors. 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. This process is comprised of the following:

1. a 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 each Directors' independence; and
5. an assessment of any required training.

Kathryn Matthews, 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. Roger Cuming, as the SID, leads the appraisal of the Chairman.

The Board has reviewed the time commitment required from all Directors and, noting their contributions and 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.

Following evaluation, the Board concluded that it had the appropriate balance of skills, experience, length of service and knowledge.

INDEPENDENCE OF DIRECTORS

The Board has considered the independent status of each Director under the AIC Code and has determined that all Directors are independent.

The Board has reviewed the fact that Roger Cuming was a senior member of a company that, until February 2015, had a shareholding in MUSCIT. The Board was satisfied that internal controls made sure that voting and control of this shareholding was not influenced by Roger Cuming. The Board believes that the contribution of Roger Cuming has always been entirely aligned to the overall success of the Company and therefore considers him to be independent.

ELECTION/RE-ELECTION OF DIRECTORS

Under the Company's Articles and in accordance with the AIC Code, Directors are required to retire at the first AGM following their appointment. Thereafter, one third of Directors shall be subject to retirement by rotation 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.

Beyond these requirements, the Board has agreed a policy whereby all Directors will seek annual re-election at the Company's AGMs. This is in line with the recommendations of the UK Corporate Governance Code for FTSE 350 companies, albeit the Company does not fall in this category.

The Board does not have a formal policy requiring Directors to stand down after a fixed period as it believes there are significant benefits to the Company in having a long serving Director.

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

STEWARDSHIP CODE

The Company has given discretionary voting powers to the Manager. AIC Code Principle 16 recommends that the Board should agree a policy regarding voting rights exercised by Montanaro. The Board has agreed that there is no need to set a written policy with Montanaro 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 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.

Corporate Governance Statement continued

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

Meetings	
Number of meetings voted at:	53
Number of meetings voted against management or abstained:	5
Resolutions	
Number of resolutions where voted with management:	819
Number of resolutions where abstained:	3
Number of resolutions where voted against management:	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.

Audit and Management Engagement Committee

The roles of the Audit Committee and Management Engagement Committee have been combined to form one Committee. This Committee is comprised of all Directors and is chaired by James Robinson, who is a Chartered Accountant. The Board is satisfied that James Robinson has recent and relevant financial experience to guide the Committee in its deliberations.

The report from this Committee is set out on pages 24 and 25.

Remuneration Committee

Following Michael's Moule's retirement on 31 July 2015, the Remuneration Committee is chaired by Kate Bolsover and is comprised of all Directors. The Committee meets as required for the purpose of considering levels of remuneration paid to the Directors and reviews the Directors' Remuneration Report and Remuneration Policy.

Nomination Committee

The Nomination Committee is comprised of all Directors and meets as required for the purpose of considering recruitment to, and removals from, the Board. Following the retirement of Michael Moule, this Committee is chaired by Kathryn Matthews. 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 Nomination Committee met to consider the re-appointment of each Director at the AGM. All of the Company's Directors will stand for re-election at the forthcoming AGM. The Committee considers that the performance of each of the Directors standing for re-election continues to be effective and that they each demonstrate commitment to their role, including commitment of time for Board and Committee meetings and any other duties.

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.

INTERNAL CONTROL AND FINANCIAL REPORTING

The Board is responsible for establishing and maintaining MUSCIT's risk management and internal control processes, and for monitoring their 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 that 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 principal risks faced by MUSCIT, which accords with guidance supplied by the Financial Reporting Council ("FRC") on risk management, internal control and related financial and business reporting. This is reviewed on a regular basis by the Board. Details of the principal risks are set out on page 11. The process involves reports from MUSCIT's Company Secretary and Manager as described below. In addition, the Audit and Management Engagement 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, the Board has carried out a review of the effectiveness of the Company's risk management and internal control processes operated since 1 April 2015. There were no matters arising from this review that required further investigation and no significant failings or weaknesses were identified; and
- a risk register has been produced against which the risks identified and the controls in place to mitigate those risks can be monitored. The risks are assessed on the basis of the likelihood of them happening, the impact on the business if they were to occur and the effectiveness of the controls in place to mitigate them. The risk register is reviewed at each meeting of the Audit and Management Engagement Committee and at other times as necessary.

Given the nature of the Company's activities and the fact that most functions are sub-contracted, the Board has concluded that there is no need for the Company to have an internal audit function. Instead, the Directors obtain information from key third party suppliers regarding the controls operated by them. The key procedures which have been established in relation to this are as follows:

- investment management is provided by Montanaro 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. Montanaro provides reports at these meetings, which cover investment performance and compliance issues;
- Capita Sinclair Henderson Limited ("CSH") 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 an independent third party;
- 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; and
- the Board reviews financial information produced by CSH in detail on a regular basis.

DIALOGUE WITH SHAREHOLDERS

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

The Annual and Half-Yearly Reports of the Company are prepared by the Board and its advisers to present a fair, balanced and understandable review of the Company's position and performance, business model and strategy.

All shareholders have the opportunity to attend and vote at the AGM during which the Board and Manager are available to discuss issues affecting MUSCIT. The Manager has signed up to the Stewardship Code and publishes its voting records on its website.

Report from the Audit and Management Engagement Committee

ROLE OF THE COMMITTEE

The primary responsibilities of the Committee are to:

- monitor the process for the production and integrity of the Company's accounts;
- consider compliance with regulatory and financial reporting requirements;
- review and monitor the effectiveness of the internal control and risk management systems;
- review annually the need for the Company to have its own internal audit function;
- consider the terms of appointment, remuneration, independence, objectivity and effectiveness of the Company's Auditor;
- make recommendations to the Board in relation to the appointment and remuneration of the Auditor;
- develop and implement a policy on the supply of non-audit services by the Auditor;
- review annually the performance of the Manager; and
- review annually the performance of other third party service providers.

MATTERS CONSIDERED IN THE YEAR

The Committee meets at least twice a year in conjunction with the annual and half-yearly financial results of MUSCIT.

The Committee has:

- reviewed the internal controls and risk management systems of the Company and its third party providers;
- reviewed the performance of the Company's third party service providers;
- agreed the audit fee and audit plan with the Auditor, including the principal areas of focus;
- received and discussed with the Auditor their report on the results of the audit;
- reviewed the Company's financial statements and advised the Board accordingly;
- reviewed the performance of the Manager and recommended to the Board that the Manager's appointment be continued; and
- reviewed and, where appropriate, updated the Company's risk register.

The key area of risk that had been determined by the Committee in relation to the business activities and financial statements of the Company, was the valuation of the listed investments. The Board relies on the Administrator to use correct listed prices and seeks comfort in the testing of this process through the internal control statements. This was discussed with the Administrator, Manager and Auditor at the conclusion of the audit of the financial statements.

The Committee assesses annually whether it is appropriate to prepare the Company's financial statements on a going concern basis, and makes its recommendations to the Board. The Board's conclusions are set out on pages 17 and 18.

The Committee considered the latest revisions to the Code, including the requirement to include a viability statement in the Annual Report. The statement is set out on page 18.

The Committee considers carefully the internal control systems. The Company relies heavily on third party suppliers. There were no significant matters of concern identified in the Committee's review of the internal controls of its third party suppliers. The Committee paid particular attention to the developing threat of cyber-crime.

It is considered that the Company does not require an internal audit function, principally because the Company delegates its day-to-day operations to third parties, which are monitored by the Committee, and provide control reports on their operations annually.

Following the consideration of the above, and its detailed review, the Committee was of the opinion that the Annual Report and Financial Statements, taken as a whole, are fair, balanced and understandable and provide the information necessary to assess to Company's position and performance, business model and strategy and advised the Board accordingly.

PERFORMANCE OF MONTANARO

The Committee considers the performance of Montanaro as AIFM and Manager by reference to obligations imposed under the terms of the Investment Management Agreement. The Committee makes recommendations to the Board on any variations to the terms of the Investment Management Agreement when it considers it necessary or desirable and on the continuing appointment of the Manager.

The Committee has considered the performance of Montanaro, their terms of engagement and their continued appointment as AIFM and Manager and made recommendations to the Board.

External Auditor

An audit fee of £21,500 (excluding expenses) has been agreed in respect of the audit for the year ended 31 March 2016 (2015: £20,500 (excluding expenses)).

The 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 reviewed the effectiveness of the external audit process during the year, considering performance, objectivity, independence and experience. The Committee has reviewed and accepted reports from KPMG on its procedures for ensuring that its independence and objectivity are safeguarded. Following review, the Committee concluded that the audit process was effective.

This is the second year with a new audit director, Peter Lomax. KPMG has been Auditor to the Company since incorporation in 1995. In response to shareholder concerns regarding the tenure of KPMG, the Committee conducted a formal tender process in November 2015. Having considered a range of alternative auditors, three firms were invited to tender. The Committee considered each of the tender submissions in detail and received presentations. As a result of this process, the Committee recommended to the Board the appointment of Ernst & Young in place of KPMG at the AGM.

JAMES ROBINSON
Audit and Management Engagement Committee Chairman
10 June 2016

Directors' Remuneration Report

The Board has prepared this Report in accordance with the requirements of the Large and Medium-Sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. An Ordinary Resolution for the approval of this report will be put to shareholders at the forthcoming AGM.

The law requires the Company's Auditor, KPMG LLP, to audit certain disclosures provided. Where disclosures have been audited, they are indicated as such. The Auditor's opinion is included in their report on pages 29 and 30.

ANNUAL STATEMENT FROM THE CHAIRMAN OF THE REMUNERATION COMMITTEE

I am pleased to present the Directors' Remuneration Report for the year ended 31 March 2016.

Having reviewed the current level of remuneration payable to Directors in accordance with the Remuneration Policy, the Committee has determined that there will be no increase in Directors' fees for the year ending 31 March 2017.

There is no significant change in the way the current, approved Remuneration Policy will be implemented during the course of the next financial year.

Remuneration Committee

The Remuneration Committee is comprised of all Directors and 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.

Directors' Fees

	2016	2015
	£	£
Chairman of the Board	**29,000**	29,000
Chairman of the Audit Committee	**23,000**	23,000
Senior Independent Director	**21,000**	21,000
Other Directors	**20,000**	20,000
	93,000	93,000

Directors' Emoluments for the Year (Audited)

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

	2016		2015	
	Fees	**Total**	Fees	Total
	£	**£**	£	£
Kathryn Matthews	**29,000**	**29,000**	29,000	29,000
Kate Bolsover*	**20,000**	**20,000**	9,140	9,140
Roger Cuming	**21,000**	**21,000**	21,000	21,000
Michael Moule**	**6,667**	**6,667**	20,661	20,661
James Robinson	**23,000**	**23,000**	22,008	22,008
	99,667	**99,667**	101,809	101,809

* Appointed 17 October 2014.
** Resigned 31 July 2015.

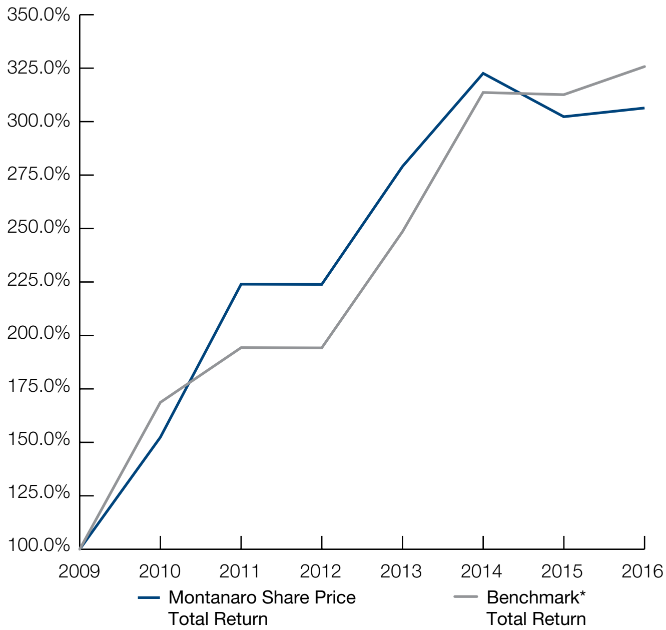
Michael Moule stepped down as Audit Committee Chairman on 30 July 2014 and James Robinson assumed the role on the same day. The above fees for 2015 for both Directors reflect this change.

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

Your Company's Performance

The following graph compares the total return (assuming all dividends are reinvested) over the past seven years to Ordinary shareholders to the total shareholder return of the NSCI. The NSCI was adopted as the new benchmark from 1 April 2013.

Total Return vs Benchmark* (rebased from March 2009)



Source: Capita Sinclair Henderson Limited.

* The Benchmark is a composite index comprising the FTSE SmallCap Index (excluding investment companies) until 31 March 2013 and the NSCI from 1 April 2013 onwards.

Voting at AGM

The Directors' Remuneration Report for the year ended 31 March 2015 and the Directors' Remuneration policy were approved by shareholders at the AGMs held on 31 July 2015 and 30 July 2014 respectively. The votes cast by proxy were as follows:

Directors' Remuneration Report (2015 AGM)

	Number of votes	% of votes cast
For	17,637,685	99.99%
Against	2,600	0.01%
At Chairman's discretion	0	0.00%
Total votes cast	17,640,285	100.00%
Number of votes withheld	388,795	

Directors' Remuneration Policy (2014 AGM)

	Number of votes	% of votes cast
For	16,915,915	100.00%
Against	0	0.00%
At Chairman's discretion	0	0.00%
Total votes cast	16,915,915	100.00%
Number of votes withheld	0	

Directors' Beneficial and Family Interests (Audited)

There is no requirement under the Articles for Directors to hold shares in the Company. The interests of the current Directors and their families in the voting rights in MUSCIT are set out below:

	As at 31 March 2016 No. of shares	As at 1 April 2015 (or date of appointment if later) No. of shares
Kathryn Matthews	**1,500**	1,500
Kate Bolsover	**1,669**	755
Roger Cuming	**5,000**	5,000
James Robinson	**8,000**	8,000

There have been no changes to the above holdings between 31 March 2016 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.

Relative Importance of Spend on Pay

The table below sets out, in respect of the financial year ended 31 March 2016 and the preceding financial year:

a) the remuneration paid to the Directors; and

b) the distributions made to shareholders by way of a dividend.

	Year ended 31 March 2016 £	Year ended 31 March 2015 £	Change %
Total remuneration	**99,667**	101,809	-2.1
Dividend paid	**2,979,360**	2,510,697	18.7

Remuneration Policy

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 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 AGM after appointment and at least every three years thereafter. The Board has agreed to a policy of annual re-election. The terms also provide that a Director may be removed without notice and that compensation will not be due on leaving office.

The fees of the existing or new Directors are determined within the limits set out in the Company's Articles. The maximum aggregate amount of Directors' fees in any one financial year shall not exceed £125,000. 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.

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.

	Expected fees for the year to 31 March 2017 (annualised) £	Fees for the year to 31 March 2016 £
Chairman	**29,000**	29,000
Chairman of the Audit Committee	**23,000**	23,000
Senior Independent Director	**21,000**	21,000
Non-executive Director	**20,000**	20,000

Fees for any new Director appointed will be on the above basis. Fees payable in respect of subsequent periods will be determined following an annual review.

Any views expressed by shareholders on the fees being paid to Directors would be taken into consideration by the Board when reviewing the Directors' Remuneration Policy and in the annual review of Directors' fees.

The Directors' Remuneration Policy will be put to shareholders' vote at least once every three years and in any year if there is to be a change in the Directors' Remuneration Policy.

Approval

The Directors' Remuneration Report was approved by the Board on 10 June 2016.

On behalf of the Board
KATE BOLSOVER
Remuneration Committee 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 Strategic Report, 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 Strategic 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.

In the opinion of the Board, the Annual Report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

On behalf of the Board
KATHRYN MATTHEWS
Chairman
10 June 2016

Independent Auditor's Report

to the Members of Montanaro UK Smaller Companies Investment Trust PLC only

OPINIONS AND CONCLUSIONS ARISING FROM OUR AUDIT

1. Our opinion on the financial statements is unmodified

We have audited the financial statements of Montanaro UK Smaller Companies Investment Trust plc for the year ended 31 March 2016 set out on pages 31 to 44. In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 March 2016 and of its profit for the year then ended;
- have been properly prepared in accordance with UK Accounting Standards, including FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

2. Our assessment of risks of material misstatement

In arriving at our audit opinion above on the financial statements, the risks of material misstatement that had the greatest effect on our audit were as follows:

Carrying value of listed investments £209,502,000 (2015: £198,575,000)

Refer to pages 24 and 25 (Report from the Audit and Management Engagement Committee), page 34 (accounting policy) and pages 37 and 38 (financial disclosures).

The risk: The Company's portfolio consists entirely of listed investments which are considered to be the key driver of the Company's operations and performance results. We do not consider there is a high risk of significant misstatement or a requirement for a significant level of judgement regarding listed investments as they are comprised of liquid, quoted instruments. However, due to their materiality in the context of the financial statements as a whole, they are considered to be the area which had the greatest effect on our overall audit strategy and allocation of resources in planning and completing our audit.

Our response: Our procedures included:

- documenting and assessing the processes in place to record investment transactions and to value the portfolio;
- verifying the valuation of 100% of portfolio investments by reference to externally quoted prices;
- assessing the liquidity of the investments and the impact of this on the valuations; and
- verifying 100% of portfolio investment holdings to independently received third party confirmations.

3. Our application of materiality and an overview of the scope of our audit

The materiality for the financial statements as a whole was set at £2,200,000 (2015: £4,154,000). This has been determined with reference to a benchmark of total assets of which it represents 1% (2015: 2%), reflecting industry consensus levels.

In addition, we applied materiality of £150,000 (2015: nil) to certain income statement accounts, primarily gains/losses on investments, management fee and other expenses for which we believe misstatements of lesser amounts than materiality for the financial statements as a whole could be reasonably expected to influence the members' assessment of the Company's financial performance.

We report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £110,000 (2015: £205,000) for the higher materiality and £8,000 (2015: nil) for certain income statement accounts which applied a lower materiality, in addition to other identified misstatements that warranted reporting on qualitative grounds.

Our audit of the Company was undertaken to the materiality level specified above and was performed at the office of the Administrator, Capita Sinclair Henderson Limited, in Exeter.

4. Our opinion on other matters prescribed by the Companies Act 2006 is unmodified

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006;
- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the information given in the Corporate Governance Statement set out on pages 22 and 23 with respect to internal control and risk management systems in relation to financial reporting processes is consistent with the financial statements.

5. We have nothing to report on the disclosures of principal risks

Based on the knowledge we acquired during our audit, we have nothing material to add or draw attention to in relation to:

- the Strategic Report on page 11, concerning the principal risks, their management, and, based on that, the directors' assessment and expectations of the Company's continuing operation over the three years to 2019; or
- the disclosures in note 1 of the financial statements concerning the use of the going concern basis of accounting.

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

6. We have nothing to report in respect of the matters on which we are required to report by exception

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the annual report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading.

In particular, we are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our audit and the Directors' statement that they consider that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy; or
- the Corporate Governance Statement does not appropriately address matters communicated by us to the Audit and Management Engagement Committee.

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; or
- a Corporate Governance Statement has not been prepared by the Company.

Under the Listing Rules we are required to review:

- the Directors' statements, set out on pages 17 and 18, in relation to going concern and longer-term viability; and
- the part of the Corporate Governance Statement on pages 20 to 23 relating to the Company's compliance with the eleven provisions of the 2014 UK Corporate Governance Code specified for our review.

We have nothing to report in respect of the above responsibilities.

Scope and responsibilities

As explained more fully in the Statement of Directors' Responsibilities set out on page 28, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. 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. This report is made solely to the Company's members as a body and is subject to important explanations and disclaimers regarding our responsibilities, published on our website at www.kpmg.com/uk/auditscopeukco2014a, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

PETER LOMAX (Senior Statutory Auditor)

for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
100 Temple Street
Bristol
BS1 6AG
10 June 2016

Income Statement
for the year to 31 March 2016

		Year to 31 March 2016			Year to 31 March 2015		
	Notes	**Revenue £'000**	**Capital £'000**	**Total £'000**	Revenue £'000	Capital £'000	Total £'000
Gains/(losses) on investments at fair value through profit or loss	10	**–**	**2,779**	**2,779**	–	(7,753)	(7,753)
Dividends	2	**5,249**	**–**	**5,249**	5,162	260	5,422
Management fee	3	**(480)**	**(1,439)**	**(1,919)**	(879)	(879)	(1,758)
Other expenses	4	**(515)**	**–**	**(515)**	(479)	–	(479)
Movement in fair value of derivative financial instruments	15	**–**	**123**	**123**	–	(81)	(81)
Net return/(loss) before finance costs and taxation		**4,254**	**1,463**	**5,717**	3,804	(8,453)	(4,649)
Interest payable and similar charges	6	**(187)**	**(562)**	**(749)**	(363)	(363)	(726)
Net return/(loss) before taxation		**4,067**	**901**	**4,968**	3,441	(8,816)	(5,375)
Taxation	7	**(3)**	**–**	**(3)**	(3)	–	(3)
Net return/(loss) after taxation		**4,064**	**901**	**4,965**	3,438	(8,816)	(5,378)
Return/(loss) per Ordinary share	9	**12.1p**	**2.7p**	**14.8p**	10.3p	(26.4)p	(16.1)p

The total column of this statement is the Statement of Total Comprehensive Income of the Company prepared in accordance with Financial Reporting Standards ("FRS 102"). The supplementary revenue return and capital return columns are prepared in accordance with the Statement of Recommended Practice issued in November 2014 by the AIC ("AIC SORP").

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 34 to 44 form part of these financial statements.

Statement of Changes in Equity
for the year to 31 March 2016

Year to 31 March 2016	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 2015		**3,348**	**19,307**	**1,362**	**4,642**	**154,842**	**5,522**	**189,023**
Fair value movement of investments	10	**–**	**–**	**–**	**–**	**2,779**	**–**	**2,779**
Costs allocated to capital		**–**	**–**	**–**	**–**	**(2,001)**	**–**	**(2,001)**
Dividends paid in the year	8	**–**	**–**	**–**	**–**	**–**	**(2,979)**	**(2,979)**
Movement in fair value of derivative financial instruments	15	**–**	**–**	**–**	**–**	**123**	**–**	**123**
Net revenue for the year		**–**	**–**	**–**	**–**	**–**	**4,064**	**4,064**
As at 31 March 2016		**3,348**	**19,307**	**1,362**	**4,642**	**155,743**	**6,607**	**191,009**

Year to 31 March 2015	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 2014		3,348	19,307	1,362	4,642	163,658	4,595	196,912
Fair value movement of investments	10	–	–	–	–	(7,753)	–	(7,753)
Capital dividend received	2	–	–	–	–	260	–	260
Costs allocated to capital		–	–	–	–	(1,242)	–	(1,242)
Dividends paid in the year	8	–	–	–	–	–	(2,511)	(2,511)
Movement in fair value of derivative financial instruments	15	–	–	–	–	(81)	–	(81)
Net revenue for the year		–	–	–	–	–	3,438	3,438
As at 31 March 2015		3,348	19,307	1,362	4,642	154,842	5,522	189,023

* These reserves are distributable, excluding any unrealised capital reserve. The special reserve can be used for the repurchase of the Company's own shares.

The notes on pages 34 to 44 form part of these financial statements.

Balance Sheet
as at 31 March 2016

	Notes	**31 March 2016** £'000	**31 March 2016** £'000	31 March 2015 £'000	31 March 2015 £'000
Fixed assets					
Investments at fair value	10		**209,502**		198,575
Current assets					
Debtors	12	**988**		1,281	
Cash at bank		**9,061**		7,847	
		10,049		9,128	
Creditors: amounts falling due within one year					
Other creditors	13	**(401)**		(416)	
Revolving credit facility	14	**(28,000)**		(18,000)	
Interest rate swap	15	**(141)**		–	
		(28,542)		(18,416)	
Net current liabilities			**(18,493)**		(9,288)
Total assets less net current liabilities			**191,009**		189,287
Creditors: amounts falling due after more than one year					
Interest rate swap	15		**–**		(264)
Net assets			**191,009**		189,023
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			**155,743**		154,842
Distributable revenue reserve			**6,607**		5,522
Total equity shareholders' funds			**191,009**		189,023
Net asset value per Ordinary share	19		**570.6p**		564.7p

These financial statements were approved by the Board of Directors on 10 June 2016.

KATHRYN MATTHEWS
Chairman

Company Registered Number: 3004101

The notes on pages 34 to 44 form part of these financial statements.

Notes to the Financial Statements
at 31 March 2016

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 November 2014. The financial statements have been prepared under FRS 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland'. There are no significant changes to the Company's accounting policies as a result of the adoption of FRS 102 which became mandatory for companies with a financial year beginning 1 January 2015. The Company has early adopted the amendments made in FRS 102 issued in March 2016, revising the fair value hierarchy disclosure requirements. Following the adoption of FRS 102, the Company has elected not to present the statement of cash flows. 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. With effect from 1 April 2015, management fees and finance costs were allocated 75% to the capital reserve and 25% to the revenue reserve. During the previous periods, the management fees and finance costs were allocated 50% to the capital reserve and 50% to the revenue reserve. This was changed in line with the expectations of long-term returns from the investment portfolio of the Company.

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 timeframe 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 102. 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 102 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 102, 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 AGM.

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 are recognised in the Income Statement over the period of the borrowings on an effective interest basis.

1 Accounting Policies continued

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 derivatives are recognised in the Income Statement and allocated to capital.

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 2016 £'000	Year to 31 March 2015 £'000
Income from investments	**5,249**	5,422
UK dividend income	**5,228**	5,079
UK capital dividend income*	**–**	260
Overseas dividend income	**21**	83
Total income	**5,249**	5,422
Total income comprises		
Dividends from financial assets at fair value	**5,249**	5,422
Dividends	**5,249**	5,422

* Capital dividends have been allocated to the capital reserve.

3 Management fee

	Year to 31 March 2016			Year to 31 March 2015		
	Revenue £'000	**Capital £'000**	**Total £'000**	Revenue £'000	Capital £'000	Total £'000
Management fee	**467**	**1,402**	**1,869**	849	849	1,698
AIFMD fee*	**13**	**37**	**50**	30	30	60
	480	**1,439**	**1,919**	879	879	1,758

The Manager received a monthly fee equivalent to 1/12 of 0.85% of the gross assets of the Company valued at the close of business on the last business day of each month.

At 31 March 2016, £160,000 (2015: £151,000) was due for payment to the Manager.

* Montanaro receives an ongoing fee of £50,000 per annum to act as the Company's AIFM. The 2015 fee had been pro-rated from 22 July 2014 and includes a one-off set up fee of £25,000.

Notes to the Financial Statements continued
at 31 March 2016

4 Other Expenses

	Year to 31 March 2016 £'000	Year to 31 March 2015 £'000
Administration and company secretarial fees	**113**	108
Directors' fees (see note 5)	**100**	102
Depositary fee	**71**	50
Registrar fee	**29**	24
Auditor's remuneration for:		
– audit	**22**	22
Custody and other bank charges	**21**	19
Legal fees	**8**	15
Other expenses (including VAT)	**151**	139
	515	479

5 Directors' Remuneration

	Year to 31 March 2016 £'000	Year to 31 March 2015 £'000
Total fees	**100**	102

A breakdown of the Directors' remuneration is set out in the Directors' Remuneration Report on page 26.
The Company has no employees.

6 Interest Payable and Similar Charges

	Year to 31 March 2016			Year to 31 March 2015		
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	**176**	**530**	**706**	349	349	698
Loan commitment fee	**11**	**32**	**43**	14	14	28
	187	**562**	**749**	363	363	726

7 Taxation

Analysis of charge in year	Year to 31 March 2016			Year to 31 March 2015		
	Revenue £'000	**Capital £'000**	**Total £'000**	Revenue £'000	Capital £'000	Total £'000
Current tax:						
Overseas tax suffered	**3**	**–**	**3**	3	–	3
	3	**–**	**3**	3	–	3

	Year to 31 March 2016			Year to 31 March 2015		
	Revenue £'000	**Capital £'000**	**Total £'000**	Revenue £'000	Capital £'000	Total £'000
Return on ordinary activities before taxation	**4,067**	**901**	**4,968**	3,441	(8,816)	(5,375)
Theoretical corporation tax at 20% (2015: 21%)	**814**	**180**	**994**	722	(1,851)	(1,129)
Effects of:						
– capital (gains)/losses that are not taxable	**–**	**(580)**	**(580)**	–	1,645	1,645
– overseas dividend income not liable to corporation tax	**(4)**	**–**	**(4)**	(17)	–	(17)
– UK dividend income not liable to corporation tax	**(1,001)**	**–**	**(1,001)**	(1,027)	(55)	(1,082)
– overseas tax suffered	**3**	**–**	**3**	3	–	3
– excess management expenses	**191**	**400**	**591**	322	261	583
	3	**–**	**3**	3	–	3

7 Taxation continued

At 31 March 2016, the Company had no unprovided deferred tax liabilities (2015: £nil). At that date, based on current estimates and including the accumulation of net allowable losses, the Company had unrelieved losses of £38,848,047 (2015: £35,886,762) that are available to offset future taxable revenue. A deferred tax asset of £7,769,609 has not been recognised because the Company is not expected to generate sufficient taxable income in future periods in excess of the available deductible expenses and accordingly, the Company is unlikely to be able to reduce future tax liabilities through the use of existing surplus losses.

Deferred tax is not provided on capital gains and losses arising on the revaluation or disposal of investments because the Trust meets (and intends to continue for the foreseeable future to meet) the conditions for approval as an Investment Trust company.

8 Dividends

	Year to 31 March 2016 £'000	Year to 31 March 2015 £'000
Paid		
2015 Final dividend of 8.90p (2014: 7.50p) per Ordinary share	**2,979**	2,511
Proposed		
2016 Final dividend of 10.00p (2015: 8.90p) per Ordinary share	**3,348**	2,979

9 Return per Ordinary Share

	Year to 31 March 2016			Year to 31 March 2015		
	Revenue	**Capital**	**Total**	Revenue	Capital	Total
Ordinary share	**12.1p**	**2.7p**	**14.8p**	10.3p	(26.4)p	(16.1)p

Revenue return per Ordinary share is based on the net revenue after taxation of £4,064,000 (2015: £3,438,000) and 33,475,958 (2015: 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 £901,000 (2015: £8,816,000 loss), and on 33,475,958 (2015: 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 2016 £'000	Year to 31 March 2015 £'000
Total investments at fair value	**209,502**	198,575

The investment portfolio comprises 45 listed UK equity holdings.

	Year to 31 March 2016 £'000	Year to 31 March 2015 £'000
Opening book cost	**150,527**	152,875
Opening investment holding gains	**48,048**	56,536
Opening valuation	**198,575**	209,411
Movements in the year		
Purchases at cost	**38,531**	36,124
Sales – proceeds	**(30,383)**	(39,207)
– realised (losses)/gains on sales	**(1,048)**	735
Increase/(decrease) in investment holding gains	**3,827**	(8,488)
Closing valuation	**209,502**	198,575
Closing book cost	**157,627**	150,527
Closing investment holding gains	**51,875**	48,048
	209,502	198,575

Notes to the Financial Statements continued
at 31 March 2016

10 Investments continued

FAIR VALUE HIERARCHY
In accordance with FRS 102, the Company must disclose the fair value hierarchy of financial instruments.

The fair value hierarchy consists of the following three levels:

- level 1 – The unadjusted quoted price in an active market for identical assets or liabilities that the entity can access at the measurement date;
- level 2 – Inputs other than quoted prices included within level 1 that are observable (i.e. developed using market data) for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- level 3 – Inputs are unobservable (i.e. for which market data is unavailable) for the asset or liability.

For financial instruments (within the scope of FRS 102), 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 102 fair value hierarchy system:

	31 March 2016			31 March 2015		
	Level 1 £'000	**Level 2 £'000**	**Total £'000**	Level 1 £'000	Level 2 £'000	Total £'000
Equity investments	**209,502**	**–**	**209,502**	198,575	–	198,575
	209,502	**–**	**209,502**	198,575	–	198,575

The table below sets out fair value measurements of financial liabilities in accordance with the FRS 102 fair value hierarchy system:

	31 March 2016			31 March 2015		
	Level 1 £'000	**Level 2 £'000**	**Total £'000**	Level 1 £'000	Level 2 £'000	Total £'000
Revolving Credit Loan Facility	**–**	**28,000**	**28,000**	–	18,000	18,000
Derivative financial instruments	**–**	**141**	**141**	–	264	264
	–	**28,141**	**28,141**	–	18,264	18,264

Details of the Revolving Credit Loan Facility are provided in note 14.

There were no level 3 investments.

TRANSACTION COSTS
During the year, the Company incurred transaction costs of £192,000 (2015: £182,000) and £24,000 (2015: £39,000) on purchases and sales of investments respectively. These amounts are deducted in determining gains/(losses) on investments at fair value as disclosed in the Income Statement.

	Year to 31 March 2016 £'000	Year to 31 March 2015 £'000
Net gains/(losses) on investments at fair value		
(Losses)/gains on sales	**(1,048)**	735
Changes in fair value	**3,827**	(8,488)
	2,779	(7,753)

A list of the investments by market value and an analysis of the investment portfolio by industrial or commercial sector are set on pages 14 and 15.

11 Significant Holdings

The Company has no holdings of 3% or more of the voting rights attached to shares that is material in the context of the financial statements.

12 Debtors

	Year to 31 March 2016 £'000	Year to 31 March 2015 £'000
Prepayments and accrued income	**31**	57
Due from brokers	**–**	520
Dividends receivable	**930**	679
Taxation recoverable	**27**	25
	988	1,281

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

	Year to 31 March 2016 £'000	Year to 31 March 2015 £'000
Accruals	**401**	416
	401	416

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

14 Revolving Credit Loan Facility

	Year to 31 March 2016 £'000	Year to 31 March 2015 £'000
Falling due within one year	**28,000**	18,000
	28,000	18,000

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.

This facility is available for a five-year term from 19 December 2011 to 19 December 2016. The loan was drawn down until 20 June 2016 and will be rolled over on a short-term basis. Interest is payable at LIBOR plus a margin and mandatory costs.

The Interest Rate Swap was originally entered into with the intention of hedging the £15,000,000 Floating Rate Revolving Credit Facility with ING Bank N.V. to a fixed rate.

On 10 February 2014, the Company agreed an additional £10,000,000 Floating Rate Revolving Credit Loan Facility with ING Bank N.V. This facility is available for a three-year term from 24 February 2014 to 24 February 2017. On 25 November 2015 the Company increased the Floating Rate Revolving Credit Loan Facility to £15,000,000. The loan was drawn down until 29 April 2016 and will be rolled over on a short-term basis. Interest is payable at LIBOR plus a margin and mandatory costs.

Interest is payable on each advance at LIBOR plus a margin and mandatory costs. A commitment fee is payable at the rate of 0.4% if the average utilisation is less than 50% of the facility during the quarter, or 0.35% if the average utilisation is 50% or more of the facility during the quarter.

The facilities contain covenants which require that total borrowings will not at any time exceed 30% of the adjusted net asset value, which itself shall not fall below £39,000,000 in respect of the original £15,000,000 facility, and £80,000,000 in respect of the additional £15,000,000 facility.

Notes to the Financial Statements continued
at 31 March 2016

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 on its £15,000,000 facility for a fixed rate until 19 December 2016.

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

	Year to 31 March 2016 £'000	Year to 31 March 2015 £'000
Opening valuation	**(264)**	(183)
Movement in fair value	**123**	(81)
Closing valuation	**(141)**	(264)

16 Share Capital

	31 March 2016 £'000	31 March 2015 £'000
Allotted, called-up and fully paid:		
33,475,958 (2015: 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 AGM on 31 July 2015, 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 AGM.

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 in the Strategic Report on page 9.

17 Duration of the Company
The Articles prescribe that shareholders should have the opportunity to consider the future of the Company at regular intervals. At the AGM held on 26 July 2013, shareholders voted to remove the obligation to convene a General Meeting during 2014 for the purpose of voluntarily winding up the Company. The Board intends to propose a resolution at the AGM in 2017 to remove the obligation to convene a General Meeting during 2018 for the purpose of voluntarily winding up the Company.

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 £191,009,000 (2015: £189,023,000) and on 33,475,958 (2015: 33,475,958) Ordinary shares, being the number of Ordinary shares in issue at the year-end.

20 Analysis of Financial Assets and Liabilities

As required by FRS 102, 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, 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 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;
- gearing; and
- use of derivatives.

(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 BONY, 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 within CREST, whereby the transaction will only settle if the Company and counterparty details are matching.

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

The maximum exposure to credit risk at 31 March 2016 was:

	31 March 2016 £'000	31 March 2015 £'000
Cash at bank	**9,061**	7,847
Debtors and prepayments	**988**	1,281
	10,049	9,128

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 9 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 2016

20 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 are set out on pages 12 and 13.

The maximum exposure to market price risk is the fair value of investments of £209,502,000 (2015: £198,575,000).

If the investment portfolio valuation fell by 1% from the amount detailed in the financial statements as at 31 March 2016, it would have the effect, with all other variables held constant, of reducing the net capital return before taxation by £2,095,000 (2015: £1,986,000). 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 Facilities with ING Bank N.V. are floating rate facilities (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 rate on £15,000,000 of its total borrowings of £28,000,000.

The Company did not receive any interest on cash deposits in the year (2015: £nil).

The interest rate risk profile of the Company is given below.

If interest rates had reduced by 1% from those paid as at 31 March 2016, 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 (2015: £30,000). If there was an increase in interest rates of 1%, the net revenue return before taxation on an annualised basis would have decreased by £150,000 (2015: £30,000). The calculations are based on cash at bank, short-term deposits and the Revolving Credit Loan Facilities as at 31 March 2016 and these may not be representative of the year as a whole.

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

(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 £10.0 million cash at bank and short-term debtors which can satisfy its creditors and that, as a closed-ended 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 level of gearing appropriate to its own risk profile.

The AIFM, in consultation with the Board, is responsible for determining the gearing levels of the Company. The Directors receive financial information on a monthly basis which is used to identify and monitor risk.

(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 £15,000,000 of its Revolving Credit Loan 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 2016 or at any time during the year. All financial assets are in sterling and disclosed at fair value through profit or loss.

20 Analysis of Financial Assets and Liabilities continued

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 2016 is as follows:

	Total £'000	**Weighted average interest rate %**	**Period until maturity Years**
Amounts drawn down under Revolving Credit Loan Facilities	**13,000**	**3.2**	**0.2**
Amounts drawn down under the additional Revolving Credit Loan Facilities	**15,000**	**1.9**	**0.1**
Derivative financial instruments	**141**	**1.0**	**0.7**
Financial liabilities upon which no interest is paid	**401**	**–**	**–**

The interest rate risk profile of the financial liabilities of the Company as at 31 March 2015 was as follows:

	Total £'000	Weighted average interest rate %	Period until maturity Years
Amounts drawn down under Revolving Credit Loan Facility	15,000	3.3	0.2
Amounts drawn down under the additional Revolving Credit Loan Facilities	3,000	1.9	0.1
Derivative financial instruments	264	1.0	1.7
Financial liabilities upon which no interest is paid	416	–	–

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

	31 March 2016 £'000	31 March 2015 £'000
In one year or less	**28,542**	18,416
In more than one year but not more than two years	**–**	264
	28,542	18,680

The Company had £2,000,000 undrawn under the floating rate Revolving Credit Loan Facility at 31 March 2016 (2015: fully drawn).

The Company had fully drawn down its facility under the additional floating rate Revolving Credit Loan Facility at 31 March 2016 (2015: £7,000,000).

The Company's Revolving Credit Loan Facilities are 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 facilities, cost approximates to fair value.

21 Capital Management Policies

The Investment 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 NSCI. 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; and pay dividends to shareholders out of distributable reserves.

Details of the Ordinary share capital are set out in note 16. Dividend payments are set out in note 8.

	31 March 2016 £'000	31 March 2015 £'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	**155,743**	154,842
Distributable revenue reserve	**6,607**	5,522
Total equity shareholders' funds	**191,009**	189,023

The Company's policies for managing capital are unchanged and have been complied with throughout the year.

Notes to the Financial Statements continued
at 31 March 2016

22 Commitments and Contingent Liabilities
At 31 March 2016, there were no capital commitments or contingent liabilities (2015: nil).

23 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 102, the Manager is not considered a related party. The relationship between the Company, its Directors and the Manager is disclosed in the Directors' Report.

AIFMD Disclosure (Unaudited)

In accordance with the AIFMD, Montanaro and the Company are required to make certain disclosures available to investors, in relation to the Company's leverage and the remuneration of the Company's AIFM. In accordance with the Directive, the AIFM's remuneration policy is available from Montanaro on request and the numerical remuneration disclosures in relation to the AIFM's first relevant accounting period will be made available in due course. The Company's maximum and average actual leverage levels at 31 March 2016 are shown below:

Leverage exposure

	Gross method	Commitment method
Maximum limit	200%	200%
Actual	117.5%	114.4%

For the purposes of the AIFMD, leverage is any method which increases the Company's exposure, including the borrowing of cash and the use of derivatives. It is expressed as a percentage of the Company's exposure to its net asset value and is calculated on both a gross and commitment method.

An explanation of the methods used can be found in the glossary of terms on page 47.

The leverage limits are set by the AIFM and approved by the Board and are in line with the maximum leverage levels permitted in the Company's Articles. The AIFM is also required to comply with the gearing parameters set by the Board in relation to borrowings. Detailed regulatory disclosures to investors in accordance with the AIFMD are contained on the Company's website.

The AIFM has sufficient capital and liquid assets to meet the requirements under AIFMD. In addition, the AIFM has extended its professional liability insurance cover to £5 million.

The periodic disclosures as required under the AIFMD to investors are made below:

- page 11 and note 20 to the financial statements set out the risk profile and risk management systems in place. There have been no changes to the risk management systems in place in the period under review and no breaches of any of the risk limits set, with no breach expected;
- information on the investment strategy, geographic and sector investment focus and stock exposures are included on pages 6 to 9 and 14 and 15; and
- none of the Company's assets are subject to special arrangements arising from their illiquid nature.

Company Summary

Investment Objective
MUSCIT's investment objective is 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 NSCI.

No unquoted investments are permitted.

Investment Policy
The Company seeks to achieve its objective and to manage risk by investing in a diversified portfolio of quoted UK small companies. At the time of initial investment, a potential investee company must be profitable and no bigger than the largest constituent of the NSCI, which represents the smallest 10% of the UK Stock Market by value. At the start of 2016, this was any company below £1.3 billion in size. The Manager focuses on the smaller end of this Index.

In order to manage risk the Manager limits any one holding to a maximum of 4% of the Company's investments at the time of initial investment. 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 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.

The AIFM, in consultation with the Board, is responsible for determining the gearing levels of the Company and has determined that the Company's borrowings should be limited to 25% of shareholders' funds. Gearing is used to enhance returns when the timing is considered appropriate. The Company currently has credit facilities of £30 million with ING Bank N.V., of which £28 million was drawn down as at 31 March 2016 (amounting to net gearing of 9.9%).

Benchmark (capital return)
For the year under review, the benchmark was the NSCI. Prior to 1 April 2013, the benchmark was the FTSE SmallCap.

Gross Assets
£219,551,000 as at 31 March 2016.

Shareholders' Funds
£191,009,000 as at 31 March 2016.

Market Capitalisation
£154,324,000 as at 31 March 2016.

Capital Structure
As at 31 March 2016 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, an ordinary resolution can be put to shareholders at the AGM in 2017 to release the Directors from the obligation to convene a General Meeting in 2018 for the purpose of winding up the Company.

Management Fee
The Manager is entitled to receive 0.85% of the gross assets with no performance fee. 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 £113,000 were paid in the year to 31 March 2016 and are subject to an annual RPI uplift.

Glossary of Terms

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

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.

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

Montanaro, AIFM or Manager
Montanaro Asset Management Limited.

MUSCIT
Montanaro UK Smaller Companies Investment Trust PLC.

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.

NSCI
Numis Smaller Companies Index (excluding investment companies).

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

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 method of calculating leverage
Represents the sum of the Company's positions after deduction of cash balances, without taking account of any hedging or netting arrangements.

Commitment method of calculating leverage
Exposure is calculated without the deduction of cash balances and after certain hedging and netting positions are offset against each other.

Shareholder Information

Sources of Further Information
Information on the Company is available on the Company's website: www.montanarouksmaller.co.uk (please note that this will be changing to www.montanaro.co.uk/muscit during the financial year) and the Manager's website www.montanaro.co.uk.

Key Dates

31 March 2016	Company year end
June 2016	Annual results
1 July 2016	Record date for dividend
22 July 2016	Annual General Meeting
10 August 2016	Dividend payable
November 2016	Half-yearly 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.

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.

Notice of Annual General Meeting

Notice is hereby given that the twenty-first 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, 22 July 2016 at 12 noon for the following purposes:

RESOLUTION 1 – ORDINARY RESOLUTION
To receive and, if thought fit, to accept the Strategic Report, the Directors' Report, the Auditor's Report and the audited financial statements for the year ended 31 March 2016.

RESOLUTION 2 – ORDINARY RESOLUTION
To receive and approve the Directors' Remuneration Report for the year ended 31 March 2016.

RESOLUTION 3 – ORDINARY RESOLUTION
To declare a final dividend of 10.0p per Ordinary share for the year ended 31 March 2016.

RESOLUTION 4 – ORDINARY RESOLUTION
To re-elect Kathryn Matthews as a Director of the Company.

RESOLUTION 5 – ORDINARY RESOLUTION
To re-elect Kate Bolsover as a Director of the Company.

RESOLUTION 6 – ORDINARY RESOLUTION
To re-elect Roger Cuming as a Director of the Company.

RESOLUTION 7 – ORDINARY RESOLUTION
To re-elect James Robinson as a Director of the Company.

RESOLUTION 8 – ORDINARY RESOLUTION
To appoint Ernst & Young LLP 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 before the Company and to authorise the Directors to determine their remuneration.

RESOLUTION 9 – 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 quotation of the Ordinary shares in the Company as derived from the Daily Official List of the London Stock Exchange, 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 Stabilisation Regulation 2003;

(iv) the authority hereby conferred shall expire at the conclusion of the Annual General Meeting of the Company in 2017, 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 10 – 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 approximately 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 11 – SPECIAL RESOLUTION

THAT, subject to the passing of Resolution 10 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 10 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 10, 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 approximately 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 12 – ORDINARY RESOLUTION

THAT, subject to the passing of Resolution 11 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 approximately 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 11 set out above.

RESOLUTION 13 – 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
10 June 2016

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 Asset Services, PXS1, 34 Beckenham Road, Beckenham, Kent BR3 4ZF, 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 that Note can only be exercised by registered members of the Company.

Note 4: As at 9 June 2016 (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 9 June 2016 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 20 July 2016 (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 Notice 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.

Note 10: None of the Directors has a contract of service with the Company. A copy of the letters of appointment of the Directors will be available for inspection at the registered office of the Company during usual business hours on any weekday (except weekends and public holidays) until the date of the meeting and at the place of the meeting for a period of fifteen minutes prior to and during the meeting.

Registered in England and Wales No. 3004101.

Notes

Notes

Form of Proxy

for use at the Twenty-first 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 twenty-first 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, 22 July 2016 at 12 noon and at any adjournment thereof.

Signature ______________________________

Dated ______________________________ 2016

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 and accept the Strategic Report, the Directors' Report, the Auditor's Report and the audited financial statements for the year ended 31 March 2016.			
RESOLUTION 2	To receive and approve the Directors' Remuneration Report for the year ended 31 March 2016.			
RESOLUTION 3	To declare a final dividend of 10.0p per Ordinary share for the year ended 31 March 2016.			
RESOLUTION 4	To re-elect Kathryn Matthews as a Director of the Company.			
RESOLUTION 5	To re-elect Kate Bolsover as a Director of the Company.			
RESOLUTION 6	To re-elect Roger Cuming as a Director of the Company.			
RESOLUTION 7	To re-elect James Robinson as a Director of the Company.			
RESOLUTION 8	To appoint Ernst & Young LLP as Auditor and to authorise the Directors to determine their remuneration.			
RESOLUTION 9	That the Company be authorised to make market purchases of up to 14.99% of its Ordinary shares.			
RESOLUTION 10	To allot relevant securities in accordance with Section 551 of the Companies Act 2006.			
RESOLUTION 11	To allot equity securities for cash and to disapply pre-emption rights, in accordance with Sections 570 and 573 of the Companies Act 2006.			
RESOLUTION 12	To issue shares held in Treasury at a discount to net asset value.			
RESOLUTION 13	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 (calls cost 12p per minute plus your phone company's access charge. Calls outside the UK will be charged at the applicable international rate). Lines are open between 9.00am – 5.30pm, Monday to Friday, excluding public holidays in England and Wales. 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 Asset Services, PXS1, 34 Beckenham Road, Beckenham, Kent BR3 4ZF or by hand during normal business hours to Capita Asset Services, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4ZF, 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.

Principal Advisers

AIFM and Manager
MONTANARO ASSET MANAGEMENT LIMITED
53 Threadneedle Street
London EC2R 8AR
Tel: 020 7448 8600
Fax: 020 7448 8601
www.montanaro.co.uk
enquiries@montanaro.co.uk

Company Secretary, Administrator and Registered Office
CAPITA SINCLAIR HENDERSON LIMITED
Beaufort House
51 New North Road
Exeter EX4 4EP
Tel: 01392 477 500
Fax: 01392 253 282

Registrar
CAPITA ASSET SERVICES
Shareholder Services Department
The Registry
34 Beckenham Road
Beckenham
Kent BR3 4TU
Tel: 0871 664 0300
(calls will cost 12p per minute plus network charges)
ssd@capitaregistrars.com
www.capitaregistrars.com

Depositary
BNY MELLON TRUST & DEPOSITARY (UK) LIMITED
BNY Mellon Centre
160 Queen Victoria Street
London EC4V 4LA

Custodian
BANK OF NEW YORK MELLON SA/NV
London Branch
One Canada Square
London E14 5AL

Banker
ING BANK N.V.
London Branch
60 London Wall
London EC2M 5TQ

Financial Adviser
CANTOR FITZGERALD EUROPE
One Churchill Place
Canary Wharf
London E14 5RB

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.

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