MONTANARO

European Smaller Companies Trust plc

Annual Report and Accounts 2010

The investment objective of **Montanaro European Smaller Companies Trust plc** (the 'Company') is to achieve capital growth by investing principally in European quoted smaller companies.

The Company's benchmark index is the MSCI Europe SmallCap (ex UK) Index (in sterling terms).

The Company was launched in May 1981. Its current objective and investment policy were adopted in September 2006. It is listed on the London Stock Exchange.

This document is important and relates to certain matters on which voting action is required. Shareholders who are in any doubt as to what action to take should consult an appropriate independent adviser immediately.

If any shareholder has sold or transferred all their shares in the Company, he or she should pass this document to the purchaser or transferee or to the person through whom the transfer or sale was effected for onward transmission to the transferee or purchaser.

Highlights
for the year ended 31 March 2010

Results

> Net asset value ('NAV') per Ordinary Share +67%

> Share price +69%

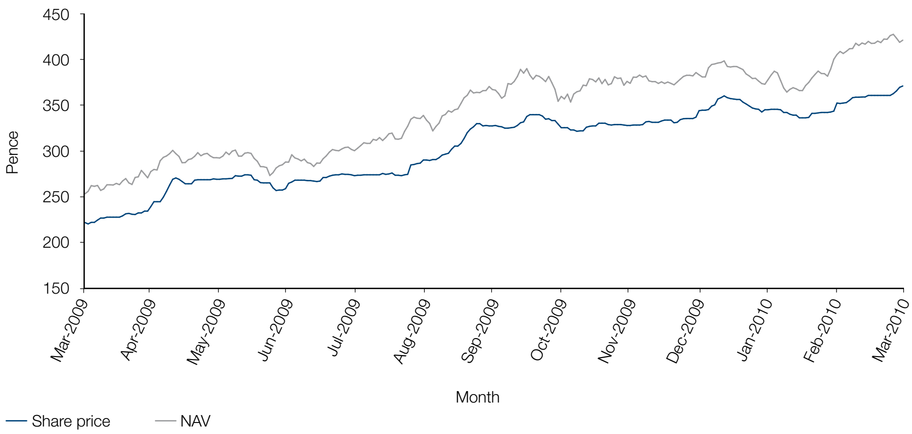
> Benchmark index +71%

> Total assets +78% (£81.1 million)

	As at 31 March 2010	As at 31 March 2009
Net assets ('000s)	**£71,059**	£42,653
NAV per Ordinary Share	**428.76p**	257.36p
Ordinary Share price	**373.00p**	220.75p
Discount	**13%**	14%
Dividend per Ordinary Share – Basic	**4.50p**	4.50p
– Special	**–**	2.83p
Net cash*	**(11.3)%**	4.7%

*(Current assets – current liabilities)/net assets.

NAV and Share Price for the year to 31 March 2010



Historic Record

	Net assets £'000s	NAV per share	Ordinary share price	Discount	Dividends per share
5 September 2006*	60,022	344.00p	322.00p	6.4%	n/a
31 March 2007	74,447	426.67p	404.00p	5.3%	4.00p
31 March 2008	69,061	401.56p	340.00p	15.3%	4.00p
31 March 2009	42,653	257.36p	220.75p	14.2%	7.33p**
31 March 2010	71,059	428.76p	373.00p	13.0%	4.50p

* Date of commencement of current management arrangements.

** Includes special dividends of 2.83p per share.

Chairman's Statement

"Following two years of losses, European Stock markets performed strongly during the year ended 31 March 2010. It is pleasing to report a significant increase in the Company's share price and net asset value ('NAV') per share over the period."

Highlights 2010

- NAV per share increased by 67% to 428.76p
- Share price increased by 69% to 373p
- Share price total return of 74%
- Maintained basic dividend of 4.5p per share

During the year ended 31 March 2010, the Company's NAV per share increased by 67% to 428.76p. This compares to an increase of 71% in the benchmark index, which at the end of the year was the MSCI Europe SmallCap (ex UK) Index (in sterling terms). The share price increased by 69% to 373p per share, reflecting a narrowing of the discount to 13% at the end of the year.

European stock markets performed strongly over the year as investors' risk appetite returned and there was evidence of improving economic conditions and corporate profitability. However, investors remain concerned over fiscal deficits and sovereign credit risk. The final quarter of the year was dominated by concerns over the stability of the Euro.

It is worth noting that, despite the problems of the Euro, currency changes did not have a material impact on the returns for the year (which are expressed in sterling) because the Pound was also weak during the year. It is not the Company's normal policy to hedge currency exposure, although currency hedging is permitted by the investment policy as contained on pages 13 and 14.

The principal reason for the underperformance of the Company against the benchmark index was the strong rally in the share prices of low quality companies, in particular in the first half of the financial year. The Company enjoyed good relative performance in the second half of the year as higher quality, less leveraged companies began to outperform.

Realignment of Portfolio

As set out in my statement last year, since the change of Manager in 2006 the Company has invested in quoted companies both within Continental Europe and in the United Kingdom. As at 31 March 2009, 18% of the Company's portfolio was invested in UK quoted companies.

After discussions with advisers and shareholders, the Board decided that it would be more appropriate for the Company to be invested exclusively in Continental European quoted companies. During the year, the Manager therefore realigned the portfolio, selling all the positions in UK quoted small companies.

To reflect this change, with effect from 1 June 2009, the Company's benchmark changed to the MSCI Europe SmallCap (ex UK) Index (in sterling terms), which comprises only small companies in Continental Europe.

Share Buy-Backs and Discount Management Policy

The discount of share price to NAV as at 31 March 2010 was 13%.

Since September 2006, the Board's stated intention has been to apply an active discount management policy. During this period, the Company has purchased 875,000 ordinary shares at discounts of between 7% and 17% and at a weighted average discount of 10%. All shares bought back are held in treasury for subsequent re-issue or cancellation in accordance with the Company's policy on treasury shares.

The Board remains committed to an active discount management policy, but the abnormal market conditions and significant stock market volatility since 2008 made it difficult to maintain the discount at the previous targeted level of 5%. Therefore, following consultation with a number of the Company's shareholders, the Board announced a change to the Company's discount management policy during the year, such that the Board will in future consider a buy back of shares if the discount of share price to NAV is greater than a target of 10% for a sustained period of time.

The Company will seek to renew its share buy back authority at the Annual General Meeting (see Resolution 11 set out in the notice of Annual General Meeting on pages 45 to 50). Shares which are bought back by the Company may be cancelled or held in treasury.

The making and timing of any share buy-backs will continue to be at the absolute discretion of the Board.

Earnings and Dividends

Revenue earnings per share for the year were 4.77p (2009: 8.82p). The decrease for the year is due principally to the absence of recoveries associated with VAT on investment management fees. Special dividends of 2.83p per share were paid in respect of VAT related recoveries during the year ended 31 March 2009. As previously reported, those special dividends were of an exceptional nature and will therefore not be repeated in future years.

A first interim dividend of 1.75p per Ordinary Share was paid on 8 January 2010 and a second interim dividend of 2.75p per Ordinary Share was paid on 1 April 2010. This brings the total dividend for the year to 4.50p per share, unchanged from the level of basic dividend paid in respect of the previous year.

Borrowings

As a reflection of a more optimistic outlook by the Manager during the earlier part of the financial year, the Company's borrowings increased from £2.5 million to £9.8 million.

The Board reviews borrowings on a regular basis and receives recommendations from the Manager on gearing levels. The Company's borrowings are represented by a flexible revolving credit facility, which enables gearing to be increased or decreased as considered appropriate.

Outlook

Although there have been signs of improving economic conditions in Europe, there are still significant uncertainties ahead, with governments needing to address debt levels, and concerns over the stability of the Euro due to the poor economic health of some of the weaker countries in the EU.

Stock market levels should, however, continue to be supported by improved corporate profitability and easy monetary conditions. Smaller companies traditionally outperform their larger counterparts during a period of recovery and, with the Manager continuing to focus on high quality companies with strong management teams, the Board believes that the Company is well placed to take advantage of attractive investment opportunities.

A R IRVINE
Chairman
9 June 2010

Manager's Report

"Equity Bull markets in Small Cap last on average 54 months and outperform Large Cap by over 7% per annum. We feel that there is a still a long way to go."

"We expect takeover activity to pick up markedly this year as better capitalised companies, particularly in the United States, take advantage of attractive valuations."

"Not all companies emerged from the recession in good shape, indeed not all survived. Those that did should now be stronger, leaner and well placed to gain market share."

The Attractions of Quoted Small Companies ('Small Cap')

The key attraction of Small Cap is that, over the long-term, investors make more money than from investing in large companies. It is easier for small companies to grow faster than large companies; hence they offer investors the potential for higher returns. Taking UK Small Cap as a proxy for Europe (because the data goes back much further), since 1954 Small Cap equities have outperformed Large Cap by an average of 3.2% per annum (the 'Small Cap Effect') which, when compounded over time, has produced returns almost five times greater.

We believe that the Small Cap Effect is more marked in Europe outside the UK, where markets can be even less efficient as a result of language, cultural and geographical barriers, where there are many more companies to choose from and where there is often far less research available.

The Small Cap market gives investors access to world leading companies managed by dynamic entrepreneurs operating in attractive niche markets. However, due to lack of broker research and the illiquidity of their shares, they require a lot of time and a level of in-house resources beyond the scope of most institutions. This is why many institutions are attracted to the asset class and equally why they will outsource the day-to-day investment decisions to dedicated specialists such as Montanaro.

A good investment manager doing its own detailed and thorough research can take advantage of the inefficiencies created by the lack of generally available research and thereby outperform the asset class. Thus investors can receive not only the benefits of the Small Cap Effect, but also a further uplift to their returns through the added value that a dedicated investment manager can bring.

Montanaro

Montanaro was established in 1991. We have the largest and most experienced specialist teams in the UK dedicated exclusively to researching and investing in quoted European small companies. Our team of 24 continues to grow as we have invested further in our research capabilities. The team is both multi-lingual and multi-national (with no less than seven nationalities), ensuring that we have the benefit of local contacts and knowledge that is so essential.

At 31 March 2010, funds under management were €1 billion.

Our clients are mainly leading international financial institutions (insurance companies, pension funds and fund of fund managers). We launched our first European fund, the open-ended Montanaro European Smaller Companies plc, in December 2000. In March 2009 it was announced that the Fonds de reserve pour les retraites ('FRR', the French national pension reserve system) had decided to appoint Montanaro to manage a substantial portfolio investing in European Smaller Companies.

Investment Philosophy and Approach

Montanaro specialises in quoted European small companies with a particular focus on those with a Stock market value below €3 billion. In Stock market parlance, we are 'bottom up' stock pickers. As an independent quoted small company specialist, we have the resources and skills to complete due diligence ourselves on companies we consider to be undervalued. Investment ideas typically are generated internally – rather than through brokers – and are researched in detail using our own information resources. With over 6,000 companies currently within our universe, we are spoiled for choice. There is never a shortage of exciting new ideas. Before 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. We also identify long-term investment themes.

Investments are focused on companies that are profitable and where there are sufficient shares in public hands to enable us to establish a holding. We are mindful of our 'circle of competence' – complicated, technology, or 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 normally invest in the market leader. We prefer companies that can demonstrate self-funded organic growth rather than those on the acquisition treadmill.

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 an economic downturn. We assess carefully 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 taking 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.

To ensure that we remain well informed, we regularly visit the companies in which we invest. 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. The track record of executives is examined in detail along with board structure, the level of insider ownership and the emphasis paid by management on sound corporate governance. Good communication and regular dialogue with management is important.

In summary, we focus on well-managed, high quality companies in growth markets adopting an investment philosophy akin to that of Warren Buffett. We share his belief that the key ingredient of a good business is management. We aim as far as possible to invest for the longer term: to 'buy and hold'. We thus keep turnover and transaction costs low and ensure we follow the companies in which we invest very closely over many years. We would rather pay more for a higher quality, more predictable company that can be valued with greater certainty. We are more interested in where an industry and a specific company will be in five to ten years than its next set of figures. We are genuine long-term investors, seemingly an increasing rarity these days.

Manager's Report continued

The Portfolio

At 31 March 2010, the portfolio consisted of 51 companies of which the top ten holdings represented 28.8%. Since our appointment in September 2006, the focus has been on companies with a market capitalisation of less than €3 billion.

Sector distribution in 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 is perceived to be.

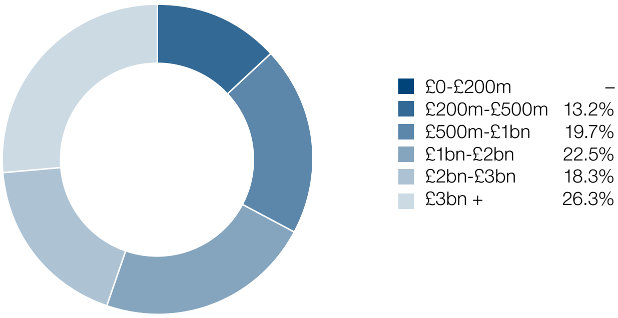
Country distribution is also driven by stock selection. In accordance with the investment policy, following consultation with a number of the Company's shareholders, the portfolio no longer invests in the United Kingdom and the benchmark was modified accordingly.

Portfolio Strategy

The two key developments last year related to the level of gearing and country allocation. The Board determines the level of borrowing within the Company in consultation with the Manager. Montanaro turned positive on European Small Cap in April 2009, having been cautious during the recession. As a result, the Board agreed to move from a net cash position to gearing within the portfolio of around 10%. This proved beneficial to investors.

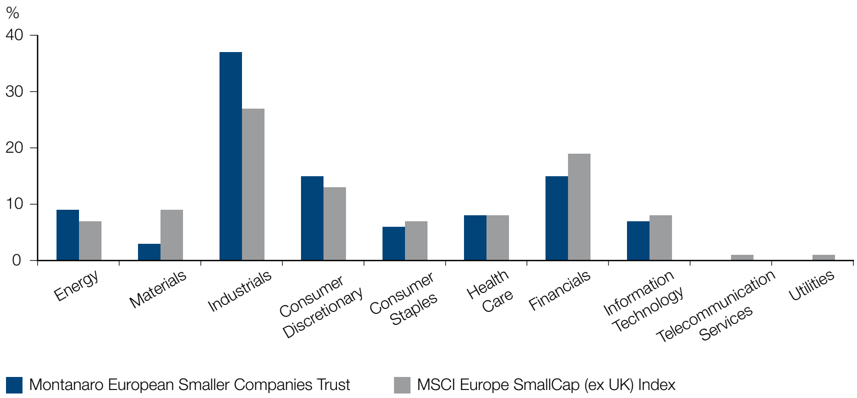
Secondly, the number of holdings in UK companies was reduced to nil during the year.

Market Capitalisation of Holdings by Value (31 March 2010)

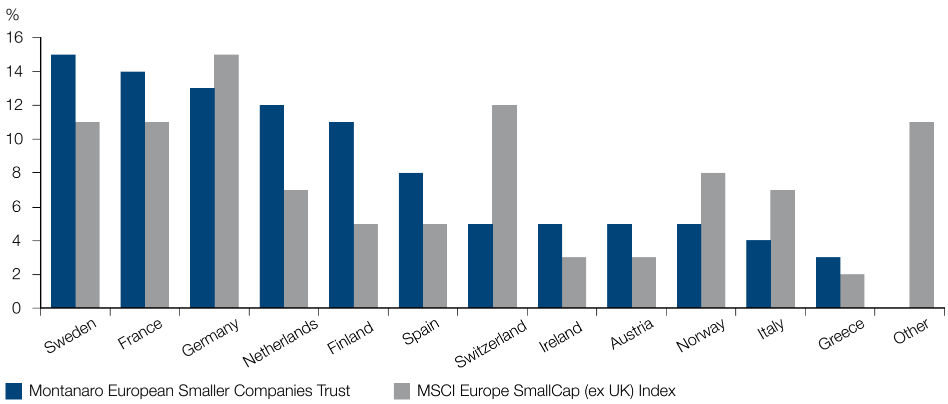


Source: Montanaro Asset Management Limited

Sector Distribution vs Index (31 March 2010)



Geographical Analysis vs Index (31 March 2010)



Source: Montanaro Asset Management Limited

Outlook

Montanaro remains optimistic about the outlook for equities, and European Small Cap in particular. Emerging market economies are in good shape and many smaller companies are benefitting from the growth there. Germany is the fifth largest trade partner of China and is benefitting from strong demand. Euro and Sterling interest rates are likely to remain low for longer than many had previously expected. The strength in the US dollar and recent weakness of the Euro will be helpful for exporters.

However, investor sentiment is still generally cautious and many investors still hold significant amounts of cash, having largely missed out on the rally in 2009. The asset class of choice last year for UK investors was high grade corporate bonds – a sensible strategy – but they were net sellers of European Small Cap (a less prescient move). We expect takeover activity to pick up markedly this year as better capitalised companies, particularly in the United States, take advantage of attractive valuations. This may well have a positive influence on sentiment.

Montanaro believes that earnings will continue to exceed analyst expectations for the rest of 2010. Both stock market analysts and companies themselves have been and probably remain too cautious about this earnings recovery. Furthermore, Stock markets – including Small Cap equities – are good value by long-term historic standards. We hold the view that a significant Bull market began in March 2009. Equity Bull markets in Small Cap last on average 54 months and outperform Large Cap by over 7% per annum. We feel that there is a still a long way to go.

2010 should be a year for stock pickers when high quality companies do well. Not all companies emerged from the recession in good shape, indeed not all survived. Those that did should now be stronger, leaner and well placed to gain market share. It is these high quality companies with experienced management teams who should do particularly well, the type of companies in which we invest.

CHARLES MONTANARO
Montanaro Asset
Management Limited
9 June 2010

Twenty Largest Holdings
as at 31 March 2010

1. AF Group
is a leader in technical consulting, offering services and solutions for infrastructure development projects, services in the pulp and paper industry as well as in the fields of energy and the environment, and the development of products and high-tech IT applications.

2. Prosegur Seguridad
provides guarding, alarm systems and security for cash in transit and operates principally in Europe and Latin America.

3. Fugro
is based in the Netherlands and comprises three divisions: Geotechnical (advice on the physical characteristics of soil, foundation design and construction), Survey (supplies precise positioning and mapping services for onshore and offshore construction services) and Geoscience (acquires and processes geophysical and geological data).

4. Andritz
is an Austrian-based global supplier of systems, machinery and services for the pulp and paper industry, the hydropower industry, the steel industry, the environment and process industry and the feed and biofuel industry.

5. Azimut
is the 6th largest Italian asset gatherer which manages and distributes a range of investment products to wealthy individuals. The group manages around EUR 15bn of client assets in in-house mutual funds, hedge funds and funds of hedge funds, and operates a small life insurance operation.

6. Virbac
which is based in France, researches, develops and manufactures pharmaceuticals for companion and food producing animals and is the largest pure-play animal pharma company in the world and 8th alongside the animal pharma divisions of the global human pharma businesses.

7. Fuchs Petrolub
is the world's largest independent manufacturer of lubricants and sells into industrial, agricultural, pharmaceutical, mining and top-end automotive markets.

8. Frigoglass
is a global corporation, specialising in the design, manufacture and marketing of Ice Cold Merchandisers ('ICMs') and the production of glass containers primarily targeting the beverage industry. It has production facilities in 10 countries on four continents and customers in more than 100 countries worldwide.

9. Viscofan
is the global market leader in the manufacture and distribution of sausage skins for the meat industry. Casing types include Skinless, Collagen, Fibrous and Plastics. Viscofan also has a market leading position in the Spanish tinned vegetable market through its IAN business.

10. GFK
is a global market research company specialising in retail, technology and media research.

11. TGS Nopec Geophysical
specialises in the acquisition and processing of 2D and 3D seismic surveys. The data is stored in a comprehensive library and provided on a multi-client basis.

12. Arcadis
is an environmental consultant offering services in contaminated land, waste management, remediation, audit, water, air and environmental management.

13. Vopak
is an energy and chemical products storage business. Vopak is the global market leader with a 12% market share.

14. Skistar
is the largest ski resort operator in the Nordic region, operating three resorts in Sweden (head office) (Sälen, Vemdalen and Åre), and two in Norway (Hemsedal and Trysil).

15. Poyry
is a global engineering consultant, specialising in the energy, forestry, infrastructure and environment sectors.

16. Vacon
is a Finnish company involved in the design and manufacture of variable speed AC drives.

17. Wincor Nixdorf
is one of the leading global suppliers of hardware and software solutions for the banking and retail industries within the areas of automated teller machines ('ATMs') and point-of-sales ('POS').

18. Rational
is the dominant global market leader in manufacturing 'combi-steamer' units for industrial and commercial kitchens with a 50% market share.

19. Aryzta
is a global leader in specialty bakery with geographic reach from North America through Europe to South East Asia and Australia. Brands include Cuisine de France, Délice de France, Otis Spunkmeyer and La Brea Bakery.

20.BTS Group
is a management training company that uses board games and computer-based simulations to facilitate 'learning by doing'. BTS delivers customised training which is designed to help managers deliver on specific businesses strategies, KPIs, efficiency improvements, leadership or sales development programmes.

Holding	Country	**31 March 2010 Value £'000**	31 March 2009 Value £'000	% of portfolio	Market cap £m
AF Group	Sweden	**2,411**	1,123	3.0	3,655
Prosegur Seguridad	Spain	**2,378**	1,333	3.0	2,059
Fugro	Netherlands	**2,374**	1,396	3.0	3,812
Andritz	Austria	**2,347**	1,786	3.0	2,280
Azimut	Italy	**2,299**	697	2.9	1,342
Virbac	France	**2,260**	1,224	2.9	684
Fuchs Petrolub	Germany	**2,229**	1,046	2.8	845
Frigoglass	Greece	**2,176**	323	2.8	392
Viscofan	Spain	**2,168**	–	2.7	907
GFK	Germany	**2,153**	1,574	2.7	967
TGS Nopec Geophysical	Norway	**2,096**	1,028	2.7	13,138
Arcadis	Netherlands	**2,093**	1,323	2.6	1,059
Vopak	Netherlands	**2,080**	–	2.6	3,727
Skistar	Sweden	**2,009**	1,082	2.5	5,116
Poyry	Finland	**1,985**	1,377	2.5	633
Vacon	Finland	**1,842**	1,218	2.3	456
Wincor Nixdorf	Germany	**1,788**	–	2.3	1,659
Rational	Germany	**1,782**	642	2.3	1,476
Aryzta	Switzerland	**1,713**	775	2.2	2,613
BTS Group	Sweden	**1,699**	669	2.1	815
Twenty Largest Holdings		**41,882**		**52.9**	

Analysis of Investment Portfolio by Industrial or Commercial Sector
as at 31 March 2010

Sector	% of portfolio	% of MSCI Europe SmallCap (ex UK) Index
Energy Equipment and Services	7.4	4.5
Oil, Gas and Consumable Fuels	1.6	2.3
Energy	**9.0**	**6.8**
Chemicals	2.8	4.6
Other	–	4.5
Materials	**2.8**	**9.1**
Building Products	1.3	1.8
Construction and Engineering	8.6	5.3
Electrical Equipment	2.3	2.8
Machinery	7.2	6.7
Commercial Services and Supplies	3.0	0.6
Professional Services	12.1	2.0
Transportation Infrastructure	2.6	1.4
Other	–	6.1
Industrials	**37.1**	**26.7**
Auto Components	1.9	1.4
Household Durables	4.1	2.0
Leisure Equipment and Products	1.1	0.5
Textiles, Apparel and Luxury Goods	1.2	1.3
Hotels, Restaurants and Leisure	2.5	1.8
Media	2.9	3.5
Speciality Retail	1.3	2.0
Other	–	0.7
Consumer Discretionary	**15.0**	**13.2**
Food Products	5.6	4.3
Other	–	2.3
Consumer Staples	**5.6**	**6.6**
Health Care Equipment and Supplies	2.8	1.7
Health Care Technology	1.3	0.2
Pharmaceuticals	4.1	2.2
Other	–	4.2
Health Care	**8.2**	**8.3**
Commercial Banks	2.8	3.9
Diversified Financial Services	2.0	2.4
Capital Markets	6.0	2.7
Insurance	1.2	2.2
Real Estate Investment Trusts	2.0	2.5
Real Estate Management and Development	1.9	5.2
Other	–	0.2
Financials	**15.9**	**19.1**
Internet Software and Services	2.0	0.3
Computers and Peripherals	2.2	1.2
Electronic Equipment, Instruments and Components	0.9	0.8
Office Electronics	1.3	–
Other	–	5.6
Information Technology	**6.4**	**7.9**
Telecommunications	**–**	**0.9**
Utilities	**–**	**1.4**
Total	**100.0**	**100.0**

Advisers

Manager
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Fax: 020 7448 8601
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Tel: 0871 384 2030

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Montanaro European Smaller Companies Trust plc
Registered in Scotland No. SC074677

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

Board of Directors

1. Andrew Irvine – Chairman
Andrew Irvine was appointed in 1992 and is Chairman of Jones Lang LaSalle (Scotland) Limited. He is also a director of Fidelity Special Values plc and Securities Trust of Scotland plc. He is Chairman of The British and Irish Lions and a past President of Scottish Rugby Union plc.

2. Bruce Graham
Bruce Graham was appointed in 2003 and was previously a partner at PricewaterhouseCoopers. Since leaving PricewaterhouseCoopers he has provided forensic accounting services to third parties. He is Chairman of the Audit Committee.

3. Alex Hammond-Chambers
Alex Hammond-Chambers was appointed in 2004. He is Chairman of Fidelity Special Values plc, Hansa Trust plc, Aurora Investment Trust plc and a director of International Biotechnology Trust plc. He is Chairman of the Nomination Committee.

4. John Lumsden
John Lumsden was appointed in 1998 and was, until December 2002, Group Chief Executive of Motherwell Bridge Holdings Limited. He is Chairman of the Remuneration Committee.

5. Richard Martin
Richard Martin was appointed in 2006. He is an adviser to various family groups, Chairman of F&C Managed Portfolio Trust plc and a director of Invesco Perpetual Aim VCT plc.

Report of the Directors

The Directors submit the Annual Report and Accounts of the Company and of the Group for the year ended 31 March 2010.

Results and Dividends

The results for the year are set out in the attached accounts.

An interim dividend of 1.75p per Ordinary Share was paid on 8 January 2010 and a second interim dividend of 2.75p per Ordinary Share was paid on 1 April 2010. The Board does not recommend the payment of a final dividend.

Principal Activity and Status

The Company is registered as a public limited company in Scotland (registered number SC074677) and is an investment company within the terms of Section 833 of the Companies Act 2006. Its shares are quoted on the main market of the London Stock Exchange.

The Company has been approved by HM Revenue and Customs as an investment trust under Section 842 of the Income and Corporation Taxes Act 1988 for the year ended 31 March 2009. As a result, it is not liable to corporation tax on capital gains. In the opinion of the Directors, the Company has subsequently conducted its affairs so as to enable it to continue to obtain approval as an investment trust.

The Company is required to comply with company law, the rules of the UK Listing Authority, the Admission and Disclosure Standards of London Stock Exchange plc, International Financial Reporting Standards, and its Articles of Association.

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

Capital Structure

The Company's capital structure is composed solely of Ordinary Shares. All shares rank equally for dividends and entitlement to capital, and at a general meeting of the Company every shareholder who is present in person or by proxy shall have one vote for all of the shares of which he is the holder on a show of hands, and one vote for each share on a poll.

Business Review

The Board of Directors is responsible for the overall stewardship of the Company, including investment and dividend policies, corporate strategy, corporate governance and risk management. Biographical details of the Directors, all of whom are non-executive, can be found on page 12.

Objective

The Company's objective is to achieve capital growth by investing principally in European quoted smaller companies.

Investment Policy

The Company invests principally in quoted smaller companies within the European Union, Iceland, Norway and Switzerland (but is not restricted from investing in smaller companies quoted on other European stock exchanges). In addition, the Company may invest in:

- Companies listed on non-European stock exchanges that derive significant revenues or profits from Europe;
- European securities, such as global depositary receipts, listed on other international stock exchanges; and
- Debt issued by European governments or denominated in European currencies.

The Company's investment policy is flexible, enabling it to invest in all types of securities of companies, including (but not limited to) equities, preference shares, debt, convertible securities, warrants and other equity-related securities. The Company may also invest, where appropriate, in open-ended collective investment schemes and closed-ended funds that invest in Europe.

It is not intended that the Company will acquire securities that are unquoted or unlisted at the time of investment (with the exception of securities which are about to be listed or traded on a stock exchange). However, the Company may continue to hold securities that cease to be quoted or listed if the Manager considers this to be appropriate.

Investment risk is spread through holding a range of securities in different countries and industrial sectors. Investments are not limited as to country or sector weightings, but no investment in the portfolio may exceed 10% of the Company's total assets at the time of investment.

Report of the Directors continued

The Company may invest in derivatives, financial instruments, money market instruments and currencies solely for the purpose of efficient portfolio management (i.e. solely for the purpose of reducing, transferring or eliminating investment risk in the Company's investments, including any technique or instrument used to provide protection against currency and credit risks).

The Company borrows funds for investment to enhance returns over the long term and may borrow in sterling, euros or other currencies. The Board has set a maximum limit on gearing, net of cash, of 30% of shareholders' funds at the time of borrowing. The Company's portfolio will normally be fully invested. However, during periods in which changes in economic conditions or other factors so warrant, the Company may reduce its exposure to securities and increase its position in cash and money market instruments.

The Company will not invest more than 10%, in aggregate, of the value of its total assets at the time of investment in other investment trusts or investment companies admitted to the Official List of the UK Listing Authority.

Investment of Assets

At each Board Meeting, the Board receives a detailed presentation from the Manager together with a comprehensive analysis of the performance of the Company and compliance with investment restrictions during the reporting period. An analysis of how the portfolio was invested as at 31 March 2010 is contained on page 10 and the 20 largest holdings are shown on pages 8 and 9. Borrowings, net of cash, as at 31 March 2010 were 11.3% of shareholders' funds.

Strategy

As part of its strategy, the Board has contractually delegated the management of the investment portfolio to Montanaro Asset Management Limited ('Montanaro'), which was appointed as Manager on 5 September 2006. Established in 1991, Montanaro is a highly experienced specialist investor in UK and Continental European quoted smaller companies. It has the largest team in the UK researching and investing exclusively in quoted European smaller companies and currently manages €1 billion, mainly on behalf of leading financial institutions.

The Company's performance in pursuing its objective is measured against key performance indicators as set out on page 16. A review of the Company's returns during the financial year, the position of the Company at the year end and the outlook for the coming year is contained within the Chairman's Statement on pages 2 and 3 and the Manager's Report on pages 4 to 7.

Principal Risks and Risk Mitigation

The Board carefully considers the Company's principal risks and seeks to mitigate these risks through continued 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 and recommendations of the Combined Code on Corporate Governance and the AIC's Code of Corporate Governance as described on pages 18 and 19. It also applies the principles detailed in the internal control guidance issued by the Financial Reporting Council. Details of the Company's internal controls are described in more detail on pages 19 and 20.

The principal risk faced by the Company is that it fails to produce the capital appreciation stated as its objective, and the Company's net asset value ('NAV') does not rise over the longer-term. The risks which might give rise to this event are summarised below. Mitigation of these risks is sought and achieved in many ways as described in italics below.

External: events such as terrorism, disease, protectionism, inflation or deflation, changes in taxation, excessive stock market speculation, economic recessions, political instability and movements in interest rates and exchange rates could affect share prices in particular markets.

Portfolio diversification, both geographical and sectoral, can mitigate the consequences of risky events. It is also possible to raise the level of cash, thereby reducing the risk of declining share prices and the effect of gearing on lower portfolio valuations. However, the portfolio's liquidity is not managed on the basis of market timing short term fluctuations.

Manager: should the Manager not be in a position to continue to manage the Company, performance may be impacted.

Montanaro has the largest specialist European smaller company team in the UK. The Manager keeps the Board informed of developments within its business.

Investment and strategy: inappropriate strategy, including country and sector allocation, stock selection and the use of gearing could all lead to poor returns for shareholders.

At each Board Meeting the Manager discusses portfolio performance and strategy with the Directors and provides the Board and shareholders with monthly reports. The portfolio is well diversified with typically 50-60 holdings, thereby reducing stock-specific risk. The Board formally reviews the performance of the Manager and its terms of appointment annually.

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

One of the benefits of an investment trust is that the Manager is not forced to buy or sell individual holdings at inopportune times. The Manager constantly reviews the underlying liquidity of the portfolio, which is well-diversified, and deals with a wide range of brokers to enhance its ability to execute and minimise liquidity risk.

Gearing: one of the benefits of an investment trust is its ability to use borrowings, which can enhance returns to shareholders in a rising stock market. However, gearing exacerbates movements in the NAV both positively and negatively and will exaggerate declines in NAV when share prices of investee companies are falling.

The Board is responsible for setting the gearing range within which the Manager may operate. It receives recommendations on gearing levels from the Manager, and monitors and discusses with the Manager the appropriate level of gearing at each Board Meeting.

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

The Manager is encouraged by the Board to market the Company to private client wealth managers and other potential new investors. The goal is to widen the shareholder base to enhance liquidity. In addition, the ability to buy back shares to be held in treasury for subsequent re-issue may enhance the liquidity of the Company's shares.

Discount volatility: as with all small company investment trusts, discounts can fluctuate significantly both in absolute terms and relative to their peer group.

The Board and Manager actively monitor the discount of share price to NAV per share and seek to manage this through liaising closely with the Company's Broker, share buy-backs and effective marketing. The Board has stated its commitment to an active discount management policy, such that it will consider a buy back of shares if the discount of share price to NAV is greater than a target of 10% for a sustained period of time. The Board encourages the Manager to market the Company to new investors to increase demand for the Company's shares, which may help to reduce the discount.

Regulatory: breach of regulatory rules could lead to suspension of the Company's Stock Exchange listing, financial penalties or a qualified audit report. Breach of Section 842 of the Income and Corporation Taxes Act 1988 could lead to the Company being subject to tax on chargeable gains.

The Administrator monitors the Company's compliance with the Listing Rules of the UK Listing Authority and Section 842 of the Income and Corporation Taxes Act 1988. Compliance with the principal rules is reviewed by the Directors at each Board Meeting.

Report of the Directors continued

Operational: failure of the Manager's or Administrator's systems, or those of third party service providers could lead to an inability to provide accurate reporting and monitoring or a breach of Section 842 of the Income and Corporation Taxes Act 1988.

The Board reviews operational issues in detail at each Board Meeting and the Audit Committee receives reports on the operation of internal controls, as explained in more detail within Internal Control on pages 19 and 20.

Financial: inadequate controls by the Manager or Administrator or other third party service providers could lead to misappropriation of assets or a breach of Section 842 of the Income and Corporation Taxes Act 1988. Inappropriate accounting policies or failure to comply with accounting standards could lead to misreporting or breaches of regulations.

The Board reviews financial reports in detail at each Board Meeting.

Banking: a breach of the Company's loan covenants might lead to funding being summarily withdrawn.

At each Board Meeting the Board reviews compliance with the banking covenants.

Reputational: inadequate or deficient controls of the Manager or Administrator or other third party providers might result in breaches of regulations and damage the trust and confidence of shareholders in the Company and lead to an increase in the discount.

The Board continually monitors and reviews issues that may impact the standing of the Company and lead to an increase in the discount.

Key Performance Indicators

The Board uses a number of performance measures to assess the Company's success in pursuing its objectives. The key performance indicators are as follows:

- Total return of the share price against that of a risk-free investment.
- Attribution of share price total return.
- NAV total return against the benchmark index.
- Discount of share price to NAV.
- Total expense ratio.

The share price total return for the year ended 31 March 2010 was 74.2% (source: Datastream), which compares to a return of 1.0% from a risk free investment (represented by a Moneyfacts average 90 day notice account). The estimated attribution of the share price total return for the year is as follows:

Change in NAV	66.6%
Dividends	5.1%
Narrowing of discount	2.5%
Share price total return	74.2%

The change in NAV for the year ended 31 March 2010 and the movement in the discount during the year are referred to in the Highlights on page 1 and the Chairman's Statement on pages 2 and 3.

The total expense ratio for the year ended 31 March 2010 (excluding the recovery of VAT on management fees and associated interest) was 1.7% (2009: 1.6%).

Subsidiary Undertaking

The Company has a 100% holding in MESCT Securities Limited, a non-trading company. In the year to 31 March 2010, MESCT Securities Limited made a profit before and after taxation of £20 (2009: £200).

The Board does not expect the subsidiary to trade in the foreseeable future.

Directors

The Directors who held office at the end of the year and their interests in the shares of the Company were:

		31 March 2010 Ordinary Shares	31 March 2009 Ordinary Shares
A R Irvine	Beneficial	**50,000**	40,000
R B M Graham	Beneficial	**34,600**	34,600
R A Hammond-Chambers	Beneficial	**8,000**	8,000
	Non-beneficial	**4,000**	4,000
J Lumsden	Beneficial	**25,000**	25,000
R M Martin	Beneficial	**8,000**	8,000

No Director has an interest in the share capital of the subsidiary undertaking. There have been no changes in the Directors' interests in the shares of the Company between 31 March 2010 and 9 June 2010.

As explained in more detail under Corporate Governance on pages 18 and 19, the Board has agreed that all Directors will retire annually. Accordingly, Mr A R Irvine, Mr R B M Graham, Mr R A Hammond-Chambers, Mr J Lumsden and Mr R M Martin will retire at the Annual General Meeting and, being eligible, offer themselves for re-election.

The Board confirms that, following formal performance evaluations, the performance of each of the Directors seeking re-election continues to be effective and demonstrates commitment to the role, and believes that it is therefore in the interests of shareholders that these Directors are re-elected.

No Director has a contract of service with the Company and no Director has any material interest in any contract to which the Company is a party.

Directors' Indemnities

As at the date of this report, indemnities are in force between the Company and each of its Directors under which the Company has agreed to indemnify each Director, to the extent permitted by law, in respect of certain liabilities incurred as a result of carrying out his role as a Director of the Company. The Directors are also indemnified against the costs of defending any criminal or civil proceedings or any claim by the Company or a regulator as they are incurred provided that where the defence is unsuccessful the Director must repay those defence costs to the Company. The indemnities are qualifying third party indemnity provisions for the purposes of the Companies Act 2006.

A copy of each deed of indemnity is available for inspection at the Company's registered office during normal business hours and will be available for inspection at the Annual General Meeting.

Conflicts of Interest

Each Director has a statutory duty to avoid a situation where he has, or could have, a direct or indirect interest which conflicts, or may conflict with the interests of the Company. A Director will not be in breach of that duty if the relevant matter has been authorised in accordance with the Company's Articles of Association.

The Board has approved a protocol for identifying and dealing with conflicts and has resolved to conduct a regular review of actual or possible conflicts and any authorised conflicts. No conflicts or potential conflicts were identified during the year.

Substantial Interests in Share Capital

As at 9 June 2010, the Company had received notification of the following holdings of voting rights (under the FSA's Disclosure and Transparency Rules):

	Number of shares held	Percentage held
Newton Investment Management Ltd	2,239,850	13.5
South Yorkshire Pensions Authority	2,000,000	12.1
Henderson Global Investors Ltd	1,180,000	7.1
Jupiter Asset Management Ltd	880,000	5.3
JP Morgan Asset Management (UK) Ltd	815,000	4.9

As at 9 June 2010, the Manager had a beneficial interest in 432,000 Ordinary Shares.

Management and Management Fees

Montanaro is entitled to receive a basic management fee of 1.0% per annum of the Company's market capitalisation (payable monthly in arrears). Montanaro is also entitled to receive an annual performance fee equal to 15% of the amount by which the increase in the NAV per share in any accounting period (adjusted for dividends paid or payable and the impact of accruing any performance fee) exceeds the total return on the Company's benchmark index plus 2.0 percentage points.

The payment of the performance fee is subject to a high water mark test and a cap of 2.0% of the Company's net assets at the end of the relevant accounting period. The performance fee is payable annually in arrears. 50% of any performance fee is payable in cash, with the balance being settled by the issue of new shares to Montanaro, although the Board may (in its absolute discretion) determine to pay the whole of the performance fee in cash in respect of any accounting period.

Montanaro's appointment may be terminated by either party giving to the other not less than six months' notice. The investment management agreement may be terminated earlier provided that a payment in lieu of notice, equivalent to the amount the Manager would otherwise have received during the notice period, is made.

Since the year end, the Board has reviewed the appropriateness of the Manager's continuing engagement. In carrying out its review, the Board considered the skills, experience, resources and commitment of the Manager together with the investment performance during the year and since its appointment. It also considered the

Report of the Directors continued

length of the notice period of the investment management agreement and the fees payable to the Manager. Following this review, it is the Directors' opinion that the continuing engagement of the Manager on the terms agreed is in the interests of shareholders as a whole.

Corporate Governance

Arrangements in respect of corporate governance, appropriate to an investment trust, have been made by the Board. The Board has considered the principles and recommendations of the AIC's Code of Corporate Governance ('AIC Code') by reference to the AIC Corporate Governance Guide for Investment Companies ('AIC Guide'). The AIC Code, as explained by the AIC Guide, addresses all the principles set out in Section 1 of the Combined Code on Corporate Governance issued by the Financial Reporting Council ('Combined Code'), as well as setting out additional principles and recommendations on issues which are of specific relevance to the Company.

The Board considers that it is appropriate to report against the principles and recommendations of the AIC Code, and by reference to the AIC Guide (which incorporates the Combined Code).

Except as disclosed in the following paragraph, the Company complied throughout the year with the recommendations of the AIC Code and the relevant provisions of Section 1 of the Combined Code. Since all the Directors are non-executive, the provisions of the Combined Code in respect of the role of the chief executive are not relevant to the Company and, likewise, the provisions of the Combined Code relating to Directors' remuneration are not relevant except in so far as they relate specifically to non-executive Directors. For the reasons set out in the AIC Guide, and in the preamble to the Combined Code, the Board considers that these provisions are not relevant to the Company, being an externally managed investment trust. The Company has therefore not reported further in respect of these provisions.

In view of its non-executive nature, and the requirement of the Articles of Association that all Directors retire by not later than the third Annual General Meeting after they were last elected, the Board considers that it is not appropriate for the Directors to be appointed for a specified term as recommended by provision A.7.2 of the Combined Code and principle 3 of the AIC Code. However, the Board has agreed that all Directors will retire annually and, if appropriate, seek re-election. Nor, due to the size of the Board, do the Directors consider it appropriate to appoint a Senior Independent Director as recommended by provision A.3.3 of the Combined Code.

The Board consists solely of non-executive Directors. Mr A R Irvine is the Chairman. All Directors are considered by the Board to be independent of the Manager. New Directors receive an induction from the Manager and Company Secretary on joining the Board, and all Directors are made aware of appropriate training courses.

Messrs Irvine and Lumsden have served on the Board for more than nine years. However, the Board subscribes to the view expressed within the AIC Code that long-serving Directors should not be prevented from forming part of an independent majority. It does not consider that a Director's tenure necessarily reduces his ability to act independently and, following a formal performance evaluation, has determined that Messrs Irvine and Lumsden are independent in character and judgement and that there are no relationships or circumstances which are likely to affect their judgement. The Board's policy on tenure is that continuity and experience are considered to add significantly to the strength of the Board and, as such, no limit on the overall length of service of any of the Company's Directors, including the Chairman, has been imposed.

Messrs Irvine and Hammond-Chambers are both non-executive directors of Fidelity Special Values plc. The Board does not consider that this relationship affects their judgement or independence in any way.

The Company has no executive Directors or employees. A management agreement between the Company and

	Board of Directors		Audit Committee		Remuneration Committee		Nomination Committee	
	Held	Attended	Held	Attended	Held	Attended	Held	Attended
A R Irvine	4	4	3	3	1	1	1	1
R B M Graham	4	4	3	3	1	1	1	1
R A Hammond-Chambers	4	4	3	3	1	1	1	1
J Lumsden	4	4	3	3	1	1	1	1
R M Martin	4	4	3	3	1	1	1	1

the Manager sets out the matters over which the Manager has authority and the limits beyond which Board approval must be sought. All other matters, including strategy, investment and dividend policies, gearing and corporate governance procedures, are reserved for the approval of the Board of Directors. The Board currently meets four times a year and, in addition, informally on a frequent basis. It receives full information on the Company's investment performance, assets, liabilities and other relevant information in advance of Board meetings. The Manager, in the absence of explicit instructions from the Board, is empowered to exercise discretion in the use of the Company's voting rights. Throughout the year a number of committees have been in operation, namely the Audit Committee, the Remuneration Committee and the Nomination Committee. The full terms of reference are available on request from the Company.

The Audit Committee, chaired by Mr R B M Graham, operates within clearly defined terms of reference and comprises all of the Directors. The duties of the Audit Committee include reviewing the annual and interim financial statements; the system of internal controls; and the terms of appointment of the Auditors together with their remuneration. It is also the forum through which the Auditors report to the Board of Directors and meets at least twice yearly. The objectivity and independence of the Auditors is reviewed by the Audit Committee, which also reviews the terms under which the Auditors are appointed to perform non-audit services. The Committee reviews the scope and results of the audit, its cost effectiveness and the independence and objectivity of the Auditors, with particular regard to non-audit fees. Such fees amounted to £7,000 for the year ended 31 March 2010 (2009: £9,000) and related to the provision of taxation services. Notwithstanding such services, the Audit Committee considers Ernst & Young LLP to be independent of the Company and that the provision of such non-audit services is not a threat to the objectivity and independence of the conduct of the audit.

The Remuneration Committee, chaired by Mr J Lumsden, comprises the full Board and reviews the appropriateness of the Manager's continuing appointment together with the terms and conditions thereof on a regular basis, and the level of Directors' fees.

The Nomination Committee, chaired by Mr R A Hammond-Chambers, comprises the full Board and is convened for the purpose of considering the appointment of additional Directors as and when considered appropriate.

In considering appointments to the Board, the Nomination Committee takes into account the ongoing requirements of the Company and the need to have a balance of skills and experience within the Board.

During the year, in accordance with the guidance issued by the AIC, the performance of the Board, its committees and individual Directors was evaluated through a formal interview-based assessment process led by the Chairman. The performance of the Chairman was evaluated by the other Directors.

The table on the previous page sets out the number of scheduled Board and Committee meetings held during the year ended 31 March 2010 and the number of meetings attended by each Director.

Individual Directors may, at the expense of the Company, seek independent professional advice on any matter that concerns them in the furtherance of their duties. The Company maintains appropriate directors' and officers' liability insurance.

Going Concern

The Company's investment policy, which is described on pages 13 and 14 and which is subject to regular Board monitoring processes, is designed to ensure that the Company is invested mainly in liquid, listed securities. The Company retains title to all assets held by its custodian, and has agreements relating to its borrowing facility with which it has complied during the year.

Notes 15 to 20 to the accounts set out the financial risk profile of the Company and indicate the effect on its assets and liabilities of falls and rises in the value of securities, market rates of interest and changes in exchange rates.

The Directors believe, in the light of the controls and review processes noted above and, bearing in mind the nature of the Company's business and assets, that the Company has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Internal Control

The Board is responsible for the Company's system of internal control and for reviewing its effectiveness. The Board confirms there is an ongoing process designed to meet the particular needs of the Company in managing the risks to which it is exposed, consistent with the internal control guidance issued by the Financial Reporting Council.

Report of the Directors continued

The key procedures which have been established to provide an effective internal control environment are as set out below:

- Investment management services are provided by Montanaro, which is regulated by the Financial Services Authority. At each Board Meeting the Board monitors the investment performance of the Company in comparison to its stated investment objective, the benchmark index and comparable investment trusts. The Board also reviews the Company's activities since the last Board Meeting to ensure that the Manager adheres to the agreed investment policy and approved investment guidelines. The Audit Committee receives reports on the operation of internal controls operated by the Manager.
- F&C Investment Business Limited ('FCIB') is responsible for the provision of company secretarial, accounting, and administration services to the Company. On an annual basis, FCIB produces an AAF 01/06 Report on internal controls, which is reviewed by a firm of reporting accountants, for consideration by the Audit Committee.
- JPMorgan Chase Bank is responsible for the custody of the Company's investments. Lists of investments held are reconciled to the Company's records on a regular basis and a SAS 70 Report, which is reviewed by a firm of reporting accountants, is produced annually for consideration by the Audit Committee.
- The Board reviews contracts with other third party service providers, including the standard of services provided, on a regular basis.
- Board procedures are set within clearly defined parameters.
- The Board receives regular financial information including management accounts and forecasts of income and expenditure.

A formal annual review of these procedures is carried out by the Audit Committee. The review meeting is attended by the Company's Auditors. A second meeting during the year receives updates on any material changes in the risk environment and the action taken.

These procedures have been in place up to the date of approval of the Annual Report and the Board is satisfied with their effectiveness. The procedures are designed to manage rather than eliminate risk and, by their nature, can only provide reasonable, but not absolute, assurance against material misstatement or loss.

The Board has reviewed the need for an internal audit function. It has decided that the systems and procedures employed by the Manager and the Administrator provide sufficient assurance that a sound system of internal control, which safeguards shareholders' investment and the Company's assets, is maintained. An internal audit function, specific to the Company, is therefore considered unnecessary.

Relations with Shareholders and Annual General Meeting

The Company welcomes the views of shareholders and places great importance on communication with its shareholders. The Manager holds meetings with the Company's largest shareholders and reports back to the Board on these meetings. The Chairman and other Directors meet significant shareholders every year and are available to meet other shareholders if required. The Annual General Meeting of the Company provides a forum, both formal and informal, for shareholders to meet and discuss issues with the Directors and the Manager of the Company. The notice of the forthcoming Annual General Meeting, to be held on 27 July 2010, is set out on pages 45 to 50.

Directors' Authority to Allot Shares

The Company's Articles of Association empower the Directors to allot unissued shares. In accordance with section 551 of the Companies Act 2006, such allotments must be authorised by shareholders in general meeting. Resolution 9 to be proposed at the forthcoming Annual General Meeting renews the Directors' authority, granted by shareholders at last year's Annual General Meeting, to allot new shares under section 551 of the Companies Act 2006. This authority will allow the Directors to allot shares up to an aggregate nominal amount of £828,663, representing an amount equal to approximately 10% of the Company's total issued ordinary share capital as at 9 June 2010 (being the latest practicable date before the publication of the Annual Report and Accounts) excluding shares held in treasury. This authority will expire at the conclusion of the Company's next Annual General Meeting, to be held in 2011 or, if earlier, on 30 September 2011.

Directors' Authority to Allot Shares other than on a Pre-emptive Basis

Resolution 10 to be proposed at the Annual General Meeting grants the Directors authority to allot new shares for cash and to dispose of treasury shares, up to an aggregate nominal amount of £828,663, representing an amount equal to approximately 10% of the Company's issued ordinary share capital as at 9 June 2010, without having to first offer such shares to existing shareholders pro rata to their existing holdings. The authority also allows the Directors to take such steps as they consider necessary in relation to the treatment of overseas shareholders, treasury shares and fractional entitlements on pre-emptive share issues. This authority will expire at the conclusion of the Company's next Annual General Meeting to be held in 2011 or, if earlier, on 30 September 2011 and will enable the Company to issue new shares and to dispose of treasury shares at any price for cash, including where shares are being issued from treasury at a price representing a discount to the NAV per share at the time of issue.

The Directors will only allot new shares pursuant to the authorities proposed to be conferred by Resolutions 9 and 10 if they believe it is advantageous to the Company's shareholders to do so and in no circumstances would result in an overall dilution of NAV per share. The Board's policy regarding the issue of shares from treasury is described below. The Directors consider that the authorities proposed to be conferred by Resolutions 9 and 10 are necessary to retain flexibility, although they do not have any intention of exercising such authorities at the present time.

Directors' Authority to Buy Back Shares

The Company did not buy back any shares during the year.

The current authority of the Company to make market purchases of up to 14.99% of the issued Ordinary Shares expires at the end of the Annual General Meeting and Resolution 11, as set out in the notice of the Annual General Meeting, seeks renewal of such authority. The renewed authority to make market purchases will be in respect of a maximum of 14.99% of the issued Ordinary Shares of the Company as at the date of the passing of the resolution (approximately 2.5 million Ordinary Shares). The price paid for shares (exclusive of expenses) will not be less than the nominal value of 50p per share nor more than 105% of the average of the middle market quotations (as derived from the Daily Official List of the London Stock Exchange) for the shares for the five business days immediately preceding the date of purchase. This power will only be exercised if, in the opinion of the Directors, a purchase would result in an increase in NAV per share and be in the best interests of the shareholders as a whole.

Treasury Shares

Shares which are bought back by the Company pursuant to the share buy-back authority may be cancelled or held by the Company in treasury and subsequently re-issued, subject to a maximum of 10% of the Company's issued share capital being held in treasury at any time. Shares held in treasury will effectively be in a state of limbo; they will not carry any voting rights, dividends payable in respect of them will be suspended and they will have no entitlements on a winding-up of the Company.

It is the Board's policy that shares will only be re-issued from treasury either at a price representing a premium to the NAV per share at the time of re-issue, or at a discount to the NAV per share provided that such discount is lower than the weighted average discount to the NAV per share when they were bought back by the Company.

It is also the Board's policy that, subject to the 10% limit referred to above, shares may be held in treasury indefinitely.

The Board believes that the treasury shares policy will improve liquidity in the shares and help to maintain the size of the Company. Furthermore, the Board believes that the re-issuance of shares from treasury at a discount to the NAV per share within the parameters described above will, in conjunction with the Company's share buy-back policy, ensure that the overall effect of the 'round trip' of repurchasing shares and subsequently re-issuing them from treasury will be an enhancement to the NAV per share.

There were 17,448,260 Ordinary Shares in issue as at 9 June 2010, including 875,000 Ordinary Shares held in treasury (which represented 5.0% of the total issued ordinary share capital as at 9 June 2010).

It is the Board's intention that any further shares bought back by the Company will be held in treasury.

Report of the Directors continued

Amendments to the Company's Articles of Association

The law in relation to companies has undergone a number of changes since the Company's current articles of association (the 'Current Articles') were last updated. The Board has decided that it is in the best interests of the Company to adopt new articles of association (the 'New Articles'). Accordingly, Resolution 12 is a special resolution relating to the adoption of the New Articles. The principal changes introduced by the New Articles are summarised in the Appendix on pages 51 to 52. The changes are being made as a consequence of the implementation of the final parts of the Companies Act 2006 in October 2009 and the implementation of the Companies (Shareholders' Rights) Regulations 2009 (the 'Regulations') in August 2009. Whilst the majority of the changes brought about as a result of the Companies Act 2006 and the Regulations applied automatically to the Company, it is best practice to reflect the new law in the Company's articles of association. Other changes, which are of a minor, technical or clarifying nature, are proposed to be made although are not summarised in the Appendix as they are not considered to be of material importance. A copy of the New Articles marked to show the changes being proposed by Resolution 12 is on display at the address of the Registered Office on page 11.

Financial Instruments

The Company's financial instruments comprise its investment portfolio, cash balances, bank debt and debtors and creditors that arise directly from its operations, such as sales and purchases awaiting settlement and accrued income. The financial risk management objectives and policies arising from its financial instruments and the exposure of the Company to risk are disclosed in Note 15 to the Accounts.

Auditors and Disclosure of Relevant Audit Information

Having made the requisite enquiries, so far as the Directors are aware, there is no relevant audit information (as defined by Section 418(3) of the Companies Act 2006) of which the Company's Auditors are unaware and each Director has taken all steps that ought to have been taken to make himself aware of any relevant audit information and to establish that the Company's Auditors are aware of that information.

Auditors

Ernst & Young LLP have expressed their willingness to continue in office as Auditors and a resolution proposing their re-appointment will be proposed at the Annual General Meeting.

Individual Savings Accounts ('ISAs')

The Company's shares are qualifying investments as defined by HM Revenue and Customs' regulations for ISAs. It is the current intention of the Directors that the Company will continue to conduct its affairs to satisfy this requirement.

Creditor Payment Policy

The Company's payment policy is to settle investment transactions in accordance with market practice and to ensure settlement of supplier invoices in accordance with stated terms. The Company did not have any trade creditors at the year end.

Recommendation

The Directors consider that the passing of the resolutions to be proposed at the Annual General Meeting is in the best interests of the Company and its shareholders as a whole and they unanimously recommend that all shareholders vote in favour of these resolutions.

By order of the Board

F&C INVESTMENT BUSINESS LIMITED
Company Secretary
9 June 2010

Directors' Remuneration Report

The Board has prepared this report in accordance with the requirements of the Companies Act 2006. An Ordinary Resolution for the approval of this report will be put to shareholders at the forthcoming Annual General Meeting.

The law requires the Company's Auditors to audit certain of the disclosures provided. Where disclosures have been audited, they are indicated as such. The Auditors' opinion is included in their report on pages 25 and 26.

The Remuneration Committee consists solely of independent non-executive Directors and determines the level of the Directors' fees in accordance with the Combined Code. The Administrator provides information on comparative levels of directors' fees to the Remuneration Committee in advance of each review.

The Remuneration Committee comprises A R Irvine, R B M Graham, R A Hammond-Chambers, J Lumsden (Chairman of the Committee) and R M Martin. As the Company has no executive Directors, the Committee meets at least annually to review the remuneration and terms of appointment of the Manager and to determine the level of Directors' fees.

Policy on Directors' Fees

The Board's policy is that the remuneration of non-executive Directors should reflect the responsibilities of being a Director, including the potential liabilities associated with the position, and the time committed by them to these responsibilities including, where appropriate, Board committee duties. It is intended that this policy will continue for the year ending 31 March 2011 and subsequent years.

The fees for the non-executive Directors are determined within the limits set out in the Company's Articles of Association. The present limit is £200,000 in aggregate per annum. Non-executive Directors are not eligible for bonuses, pension benefits, share options, long-term incentive schemes or other benefits.

Directors' Emoluments for the Year (audited)

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

	2010 **£**	2009 £
A R Irvine	**26,000**	26,000
R B M Graham	**21,000**	21,000
R A Hammond-Chambers*	**17,500**	17,500
J Lumsden	**17,500**	17,500
R M Martin	**17,500**	17,500
Total	**99,500**	99,500

* Includes fees of £11,500 (2009: £17,000) paid to Alex Hammond-Chambers and Company.

Directors' Service Contracts

It is the Board's policy that Directors do not have service contracts, but new Directors are provided with a letter of appointment.

Director	Date of appointment	Due date for re-election
A R Irvine	10/01/1992	AGM 2010
R B M Graham	24/06/2003	AGM 2010
R A Hammond-Chambers	22/06/2004	AGM 2010
J Lumsden	24/07/1998	AGM 2010
R M Martin	01/02/2006	AGM 2010

The terms of Directors' appointments provide that Directors should retire and be subject to re-election at the first Annual General Meeting after their appointment. Directors are obliged to offer themselves for re-election by shareholders by not later than the third Annual General Meeting after they were last elected. However, the Board has agreed that all Directors will retire annually. There is no notice period and no provision for compensation upon early termination of appointment.

The Company's policy when determining the duration of, and any notice periods and termination payments under, letters of appointment is to follow prevailing best practice and be comparable to those of other relevant investment trusts that are similar in size and have similar investment objectives and structures.

Directors' Remuneration Report continued

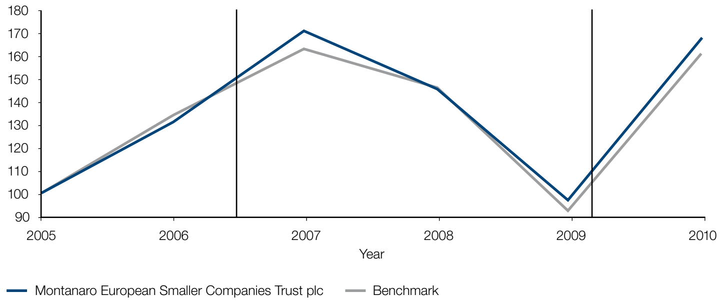
Company Performance

The Board is responsible for the Company's investment strategy and performance, although the management of the Company's investment portfolio is delegated to the Manager through the investment management agreement, as referred to in the Report of the Directors on page 17.

The graph below compares, for the five financial years ended 31 March 2010, the share price total return (assuming all dividends are reinvested) to shareholders compared to the total shareholder return from the benchmark index.

An explanation of the performance of the Company for the year ended 31 March 2010 is given in the Chairman's Statement and the Manager's Report.

Total Return vs Benchmark* (rebased from March 2005)



* Until 4 September 2006: Hoare Govett Smaller Companies (ex Investment Companies) Index. From 5 September 2006: MSCI Europe SmallCap Index. The benchmark was changed as a result of changes in management arrangements. It was changed again on 1 June 2009 to the MSCI Europe SmallCap (ex UK) Index.

On behalf of the Board

A R IRVINE
Director
9 June 2010

Management Report, Directors' Responsibilities Statement and Independent Auditor's Report

Management Report

Listed companies are required by the FSA's Disclosure and Transparency Rules (the 'Rules') to include a management report in their annual financial statements. The information required to be in the management report for the purpose of the Rules is included in the Chairman's Statement (pages 2 to 3), the Manger's Report (pages 4 to 7) and the Business Review contained in the Report of the Directors (pages 13 to 16). Therefore a separate management report has not been included.

Statement of Directors' Responsibilities in Relation to the Group Financial Statements

The Directors are responsible for preparing the Annual Report and the Group financial statements in accordance with applicable United Kingdom law and those International Financial Reporting Standards as adopted by the European Union.

Under Company Law the Directors must not approve the Group financial statements unless they are satisfied that they present fairly the financial position, financial performance and cash flows of the Group for that period. In preparing the Group financial statements the Directors are required to:

- select suitable accounting policies in accordance with IAS 8: *Accounting Policies, Changes in Accounting Estimates and Errors* and then apply them consistently;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's financial position and financial performance;
- state that the Group has complied with IFRSs, subject to any material departures disclosed and explained in the financial statements; and
- make judgements and estimates that are reasonable and prudent.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the Group financial statements comply with the Companies Act 2006 and Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

On behalf of the Board

A R IRVINE
Director
9 June 2010

Independent Auditors' Report to the Members of Montanaro European Smaller Companies Trust plc

We have audited the financial statements of Montanaro European Smaller Companies Trust plc for the year ended 31 March 2010 which comprise the Consolidated Statement of Comprehensive Income, the Group and Parent Company Balance Sheets, the Group and Parent Company Statements of Changes in Equity, the Consolidated Cash Flow Statement and the related notes 1 to 20. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards ('IFRSs') as adopted by the European Union and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

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

Respective Responsibilities of Directors and the Auditors

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

Management Report, Directors' Responsibilities Statement and Independent Auditor's Report continued

Scope of the Audit of the Financial Statements
An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the financial statements.

Opinion on Financial Statements
In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 March 2010 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Opinion on Other Matters Prescribed by the Companies Act 2006
In our opinion:

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

Matters on Which We Are Required to Report by Exception
We have nothing to report in respect of the following:

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

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

Under the Listing Rules we are required to review:

- the Directors' statement, set out on page 19, in relation to going concern; and
- the part of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the June 2008 Combined Code specified for our review.

SUE DAWE
(Senior statutory auditor)
For and on behalf of Ernst & Young LLP,
Statutory Auditor
Edinburgh
9 June 2010

Consolidated Statement of Comprehensive Income

for the year ended 31 March 2010

	Notes	2010 Revenue £'000	2010 Capital £'000	2010 Total £'000	2009 Revenue £'000	2009 Capital £'000	2009 Total £'000
Capital gains/(losses) on investments							
Gains/(losses) on investments held at fair value	9	–	29,246	29,246	–	(26,364)	(26,364)
Exchange (losses)/gains		–	(135)	(135)	–	880	880
		–	29,111	29,111	–	(25,484)	(25,484)
Revenue							
Investment income	2	1,747	–	1,747	2,005	–	2,005
Other income	2	13	–	13	403	–	403
Total income		1,760	29,111	30,871	2,408	(25,484)	(23,076)
Expenditure							
Management expenses	3	(176)	(328)	(504)	88	164	252
Other expenses	4	(497)	–	(497)	(433)	–	(433)
Total expenditure		(673)	(328)	(1,001)	(345)	164	(181)
Profit/(loss) before finance costs and taxation		1,087	28,783	29,870	2,063	(25,320)	(23,257)
Finance costs	5	(68)	(126)	(194)	(82)	(153)	(235)
Profit/(loss) before taxation		1,019	28,657	29,676	1,981	(25,473)	(23,492)
Taxation	6	(229)	–	(229)	(494)	322	(172)
Total comprehensive income		790	28,657	29,447	1,487	(25,151)	(23,664)
Return/(loss) per share	8	4.77p	172.91p	177.68p	8.82p	(149.16)p	(140.34)p

The total column of this statement represents the Group's Income Statement and Statement of Comprehensive Income, prepared in accordance with IFRS. The supplementary revenue return and capital return columns are both prepared under guidance published by the Association on Investment Companies.

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

No operations were acquired or discontinued in the year.

All of the profit/(loss) and total comprehensive income for the year is attributable to the owners of the Company.

The accompanying notes are an integral part of this statement.

Balance Sheets
as at 31 March 2010

		Company		Group	
	Notes	**2010 £'000**	2009 £'000	**2010 £'000**	2009 £'000
Non-current assets					
Investments held at fair value through profit and loss	9	**79,576**	41,341	**79,114**	40,655
Current assets					
Other receivables	10	**375**	393	**375**	393
Cash and cash equivalents	10	**1,562**	4,484	**1,563**	4,491
		1,937	4,877	**1,938**	4,884
Total assets		**81,513**	46,218	**81,052**	45,539
Current liabilities					
Other payables	11	**(10,454)**	(3,565)	**(9,993)**	(2,886)
Total liabilities		**(10,454)**	(3,565)	**(9,993)**	(2,886)
Net assets		**71,059**	42,653	**71,059**	42,653
Capital and reserves					
Called-up share capital	12	**8,724**	8,724	**8,724**	8,724
Share premium account		**3,935**	3,935	**3,935**	3,935
Capital redemption reserve		**2,212**	2,212	**2,212**	2,212
Capital reserve		**54,316**	25,784	**53,855**	25,198
Revenue reserve		**1,872**	1,998	**2,333**	2,584
Shareholders' funds		**71,059**	42,653	**71,059**	42,653
Net asset value per share	13	**428.76p**	257.36p	**428.76p**	257.36p

The financial statements on pages 27 to 42 were approved by the Board of Directors and authorised for issue on 9 June 2009 and signed on its behalf by:

A R IRVINE
Director

The accompanying notes are an integral part of this statement.

Company Statement of Changes in Equity
for the year ended 31 March 2010

	Notes	Share Capital £'000	Share Premium Account £'000	Capital Redemption Reserve £'000	Capital Reserve £'000	Revenue Reserve £'000	Total £'000
Balance at 1 April 2009		8,724	3,935	2,212	25,784	1,998	42,653
Total comprehensive income		–	–	–	28,532	915	29,447
Dividends paid	7	–	–	–	–	(1,041)	(1,041)
Balance at 31 March 2010		**8,724**	**3,935**	**2,212**	**54,316**	**1,872**	**71,059**

	Share Capital £'000	Share Premium Account £'000	Capital Redemption Reserve £'000	Capital Reserve £'000	Revenue Reserve £'000	Total £'000
Balance at 1 April 2008	8,724	3,935	2,212	52,824	1,366	69,061
Total comprehensive income	–	–	–	(25,151)	1,487	(23,664)
Ordinary Shares purchased to be held in treasury	–	–	–	(1,889)	–	(1,889)
Dividends paid (Note 7)	–	–	–	–	(855)	(855)
Balance at 31 March 2009	**8,724**	**3,935**	**2,212**	**25,784**	**1,998**	**42,653**

Consolidated Statement of Changes in Equity
for the year ended 31 March 2010

	Notes	Share Capital £'000	Share Premium Account £'000	Capital Redemption Reserve £'000	Capital Reserve £'000	Revenue Reserve £'000	Total £'000
Balance at 1 April 2009		8,724	3,935	2,212	25,198	2,584	42,653
Total comprehensive income		–	–	–	28,657	790	29,447
Dividends paid	7	–	–	–	–	(1,041)	(1,041)
Balance at 31 March 2010		**8,724**	**3,935**	**2,212**	**53,855**	**2,333**	**71,059**

	Share Capital £'000	Share Premium Account £'000	Capital Redemption Reserve £'000	Capital Reserve £'000	Revenue Reserve £'000	Total £'000
Balance at 1 April 2008	8,724	3,935	2,212	52,238	1,952	69,061
Total comprehensive income	–	–	–	(25,151)	1,487	(23,664)
Ordinary Shares purchased to be held in treasury	–	–	–	(1,889)	–	(1,889)
Dividends paid (Note 7)	–	–	–	–	(855)	(855)
Balance at 31 March 2009	**8,724**	**3,935**	**2,212**	**25,198**	**2,584**	**42,653**

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

Consolidated Cash Flow Statement
for the year ended 31 March 2010

	2010 £'000	2009 £'000
Cash flows from operating activities		
Profit/(loss) before finance costs and taxation	**29,870**	(23,257)
Investments (gains)/losses	**(29,246)**	26,364
Withholding tax	**(199)**	(172)
Exchange losses/(gains)	**135**	(880)
Operating cash flows before investments in working capital	**560**	2,055
(Increase)/decrease in receivables	**(154)**	30
Decrease in payables	**(12)**	(85)
Net cash from operating activities	**394**	2,000
Cash flows from investing activities		
Purchases of investments	**(34,217)**	(20,143)
Sales of investments	**24,971**	20,651
Net cash (outflow)/inflow in investing activities	**(9,246)**	508
Cash flows from financing activities		
Dividends paid	**(1,041)**	(855)
Interest paid	**(212)**	(231)
Own shares purchased to be held in treasury	**–**	(1,889)
Drawdowns/(repayments) of borrowings	**7,056**	(8,015)
Net cash inflow/(outflow) from financing activities	**5,803**	(10,990)
Net decrease in cash and cash equivalents	**(3,049)**	(8,482)
Realised exchange gains	**121**	737
Decrease in cash and cash equivalents	**(2,928)**	(7,745)
Cash and cash equivalents at beginning of year	**4,491**	12,236
Cash and cash equivalents at end of year	**1,563**	4,491

The accompanying notes are an integral part of this statement.

Notes to the Accounts
for the year ended 31 March 2010

1 Accounting Policies
A summary of the principal accounting policies is set out below.

BASIS OF ACCOUNTING
The financial statements of the Group have been prepared in accordance with the Companies Act 2006, International Financial Reporting Standards ('IFRS'), which comprise standards and interpretations approved by the International Accounting Standards Board ('IASB'), and International Accounting Standards and Standing Interpretations Committee interpretations approved by the International Accounting Standards Committee ('IASC') that remain in effect, and to the extent that they have been adopted by the European Union.

The financial statements have been prepared on a going concern basis. The principal accounting policies adopted are set out below. Where presentational guidance set out in the Statement of Recommended Practice ('SORP') for investment companies issued by the Association of Investment Companies ('AIC') in January 2009 is consistent with the requirements of IFRS, the Directors have sought to prepare the financial statements on a basis compliant with the recommendations of the SORP.

The notes and financial statements are presented in pounds sterling (functional and presentational currency) and are rounded to the nearest thousand except where otherwise indicated.

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts reported for assets and liabilities as at the balance sheet date and the amounts reported for revenue and expenses during the year. The nature of the estimation means that actual outcomes could differ from those estimates.

The following new standards have been adopted in the current year:

- On 6 September 2007, the IASB issued an amendment to IAS 1 '*Presentation of Financial Statements (Amendment)*', which became effective for periods commencing on or after 1 January 2009. The revised standard separates owner and non-owner changes in equity. The statement of changes in equity includes only details of transactions with owners, with non-owner changes, if any, disclosed in a single line.

  In addition, the standard introduces the Statement of Comprehensive Income. It presents all items of recognised income and expense either in a single statement, or in two linked statements. The Group has elected to present one single statement, entitled the Consolidated Statement of Comprehensive Income.
- On 5 March 2009, the IASB issued an amendment to IFRS 7 *'Financial Instruments: Disclosures'*, which became effective for periods commencing on or after 1 January 2009. The amendments are intended to enhance disclosure about fair value measurement.
- On 30 November 2006, the IASB issued IFRS 8 *'Operating Segments'*, which became effective for periods commencing on or after 1 January 2009. The Directors consider that the Group operates one segment, being investment principally in European quoted smaller companies, in accordance with IFRS 8.

The following new standards have been issued but are not effective for this accounting period and have not been adopted early:

- In January 2008, the IASB issued IAS 27 *'Consolidated and Separate Financial Statements'* which becomes effective for accounting periods commencing on or after 1 July 2009. The objective of this standard is to enhance the relevance, reliability and comparability of the information that a parent entity provides in its separate financial statements and in its consolidated financial statements for a group of entities under its control.

Notes to the Accounts continued
for the year ended 31 March 2010

- In November 2009, the IASB issued IFRS 9 *'Financial instruments'* which becomes effective for accounting periods commencing on or after 1 January 2013. This represents the first of a three part project to replace IAS 39 *'Financial Instruments: Recognition and Measurement'*. The objective of the standard is to enhance the ability of investors and other users of financial information to understand the accounting of financial assets and to reduce complexity,

The Board does not consider that the future adoption of any new standards, in the form currently available, will have any material impact on the financial statements as presented.

BASIS OF CONSOLIDATION
The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 March each year. Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

No Statement of Comprehensive Income is presented for the Company, as permitted by Section 408 of the Companies Act 2006.

OPERATING SEGMENTS
The Board has considered the requirements of IFRS 8 '*Operating Segments*'. The Board is of the view that the Group is engaged in a single segment of business, of investing in European quoted smaller companies, and that therefore the Group has only a single operating segment. The Board of Directors, as a whole, has been identified as constituting the chief operating decision maker of the Group. The key measure of performance used by the Board to assess the Group's performance is the total return on the Group's net asset value, as calculated under IFRS, and therefore no reconciliation is required between the measure of profit or loss used by the Board and that contained in the financial statements.

PRESENTATION OF INCOME STATEMENT
In order to better reflect the activities of an investment trust company and in accordance with guidance issued by the AIC, supplementary information which analyses the Income Statement between items of a revenue and capital nature has been presented alongside the Income Statement. In accordance with the Company's status as a UK investment company under Section 833 of the Companies Act 2006, net capital returns may not be distributed by way of dividend. Additionally, the net revenue is the measure the Directors believe appropriate in assessing the Company's compliance with certain requirements set out in Section 842 of the Income and Corporation Taxes Act 1988.

INCOME
Dividends are recognised as income on the date that the related investments are marked ex-dividend.

Dividends receivable on equity shares where no ex-dividend date is quoted are recognised when the Company's right to receive payment is established.

Where the Group has elected to receive its dividends in the form of additional shares rather than cash, the amount of the cash dividend is recognised as income.

Interest income is accounted for on an accruals basis.

EXPENSES AND INTEREST
All expenses and interest are accounted for on an accruals basis and are charged against revenue, except where incurred in connection with the maintenance or enhancement of the value of the Group's assets and taking account of the expected long-term returns as follows:

- loan interest payable is allocated 35% to revenue and 65% to capital.
- basic management fees payable are allocated 35% to revenue and 65% to capital.
- performance fees payable are allocated 100% to capital.

TAXATION

The tax expense represents the sum of the tax currently payable and deferred tax. Tax payable is based on the taxable profit for the year. Taxable profit differs from profit before tax as reported in the Statement of Comprehensive Income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

In line with the recommendations of the SORP, the allocation method used to calculate tax relief on expenses presented against capital returns in the supplementary information in the Statement of Comprehensive Income is the 'marginal basis'. Under this basis, if taxable income is capable of being offset entirely by expenses presented in the revenue return column of the Statement of Comprehensive Income, then no tax relief is transferred to the capital return column.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the Statement of Comprehensive Income, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Investment trusts which have approval under Section 842 of the Income and Corporation Taxes Act 1988 are not liable to taxation on capital gains.

INVESTMENTS

Investments are recognised and derecognised on the trade date where a purchase or sale is under a contract whose terms require delivery within a timeframe established by the market concerned, and are initially measured at fair value. Investments are classified as fair value through profit or loss. As the Group's business is investing in financial assets with a view to profiting from their total return in the form of interest, dividends or increases in fair value, listed equities and fixed income securities are designated as fair value through profit or loss on initial recognition. The Group manages and evaluates the performance of these investments on a fair value basis in accordance with its investment strategy, and information about the investments is provided internally on this basis to the entity's key management personnel.

Financial assets designated as at fair value through profit or loss are measured at subsequent reporting dates at fair value, which is the bid price.

Where securities are designated upon initial recognition as fair value through profit or loss, gains and losses arising from changes in fair value are included in the net profit or loss for the period as a capital item and transaction costs on acquisition or disposal of the security are expensed.

MESCT Securities Limited is valued at net asset value, being fair value, in the parent company accounts.

CASH AND CASH EQUIVALENTS

Cash comprises cash on hand and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Notes to the Accounts continued
for the year ended 31 March 2010

CAPITAL RESERVE
The following are accounted for in this reserve:

- gains and losses on the realisation of investments.
- increases and decreases in the valuation of investments held at the year end.
- exchange differences of a capital nature.
- special dividends of a capital nature.
- expenses and finance costs, together with the related taxation effect, charged in accordance with the above policies.
- cost of purchasing Ordinary Shares to be held in treasury or cancelled.

FINANCIAL INSTRUMENTS
Financial assets and financial liabilities are recognised on the Group's Balance Sheet when the Group becomes a party to the contractual provisions of the instrument. The Group shall offset financial assets and financial liabilities if it has a legally enforceable right to set off the recognised amounts and interests and intends to settle on a net basis.

FOREIGN CURRENCIES
Overseas assets and liabilities are translated at the bid price rate ruling at the balance sheet date. Profits or losses on retranslation of investments at the year end are included within unrealised appreciation/depreciation of investments and are taken to the capital reserve. Exchange gains and losses of a revenue nature are taken to the revenue reserve.

Rates of exchange	31 March 2010	31 March 2009
Euro	**1.12**	1.08
Norwegian Krone	**9.00**	9.68
Swedish Krona	**10.92**	11.85
Swiss Franc	**1.60**	1.63

2 Income

	2010 £'000	2009 £'000
Investment income		
UK dividend income	**34**	214
Overseas dividend income	**1,713**	1,791
	1,747	2,005
Other operating income		
Deposit interest	**13**	183
Interest on VAT recovered	**–**	220
	13	403
Total	**1,760**	2,408

3 Management Expenses

	2010 Revenue £'000	**2010 Capital £'000**	**2010 Total £'000**	2009 Revenue £'000	2009 Capital £'000	2009 Total £'000
Investment management fee	**176**	**328**	**504**	163	303	466
VAT recovered	**–**	**–**	**–**	(251)	(467)	(718)
	176	**328**	**504**	(88)	(164)	(252)

Details of the management arrangements during the year are contained within the Report of the Directors on page 17.

4 Expenses

	2010 Revenue £'000	**2010 Capital £'000**	**2010 Total £'000**	2009 Revenue £'000	2009 Capital £'000	2009 Total £'000
Directors' fees	**100**	**–**	**100**	100	–	100
Auditors' remuneration for:						
– audit	**16**	**–**	**16**	16	–	16
– taxation	**7**	**–**	**7**	9	–	9
Secretarial and administration fee	**130**	**–**	**130**	129	–	129
Other	**244**	**–**	**244**	179	–	179
	497	**–**	**497**	433	–	433

5 Finance Costs

	2010 Revenue £'000	**2010 Capital £'000**	**2010 Total £'000**	2009 Revenue £'000	2009 Capital £'000	2009 Total £'000
Interest payable on bank loans	**68**	**126**	**194**	82	153	235

6 Tax

	2010 Revenue £'000	**2010 Capital £'000**	**2010 Total £'000**	2009 Revenue £'000	2009 Capital £'000	2009 Total £'000
Corporation tax	**–**	**–**	**–**	494	(494)	–
Overseas tax	**229**	**–**	**229**	172	–	172
Double taxation relief	**–**	**–**	**–**	(172)	172	–
	229	**–**	**229**	494	(322)	172

As at 31 March 2010, the Company had unutilised management expenses for taxation purposes of £9,695,000 (2009: £9,531,000). No deferred tax asset has been recognised on the unutilised expenses as it is unlikely that there will be suitable taxable profits from which the future reversal of the deferred tax could be deducted. In addition, as at 31 March 2010, the Company had eligible unutilised foreign taxation of £546,000 (2009: £317,000).

Notes to the Accounts continued
for the year ended 31 March 2010

FACTORS AFFECTING TAX CHARGE FOR THE YEAR

The revenue account tax charge for the year is lower than the standard rate of corporation tax in the UK for an investment company (28%). The differences are explained below:

	2010 £'000	2009 £'000
Profit/(loss) on ordinary activities before taxation	**29,676**	(23,492)
Corporation tax at standard rate of 28%	**8,309**	(6,578)
Effects of:		
(Gains)/losses on investments	**(8,189)**	7,382
Movement in unutilised expenses	**86**	(498)
Non-taxable overseas income	**(234)**	–
Exchange losses/(gains)	**38**	(246)
Non-taxable UK dividend income	**(10)**	(60)
Overseas tax	**(229)**	(172)
Total tax charge for the year	**(229)**	(172)

7 Dividends

	2010 £'000	2009 £'000
Amounts recognised as distributions to equity holders in the year:		
Interim dividend for the year ended 31 March 2009 of 1.75p per share	**–**	294
Special interim dividend for the year ended 31 March 2009 of 1.05p per share	**–**	176
Final dividend for the year ended 31 March 2008 of 2.25p per share	**–**	385
Interim dividend for the year ended 31 March 2010 of 1.75p per share	**290**	–
Special final dividend for the year ended 31 March 2009 of 1.78p per share	**295**	–
Final dividend for the year ended 31 March 2009 of 2.75p per share	**456**	–
	1,041	855

8 Earnings Per Share

	2010 Revenue	**2010 Capital**	**2010 Total**	2009 Revenue	2009 Capital	2009 Total
Basic	**4.77p**	**172.91p**	**177.68p**	8.82p	(149.16)p	(140.34)p

Basic revenue return per Ordinary Share is based on the net revenue return on ordinary activities after taxation of £790,000 (2009: £1,487,000), and on 16,573,260 (2009: 16,861,863) Ordinary Shares, being the weighted average number of Ordinary Shares in issue during the year, excluding those shares bought back and held in treasury.

Basic capital return per Ordinary Share is based on the net capital gain for the financial year of £28,657,000 (2009: loss of £25,151,000), and on 16,573,260 (2009: 16,861,863) Ordinary Shares, being the weighted average number of Ordinary Shares in issue during the year, excluding those shares bought back and held in treasury.

9 Investments at Fair Value Through Profit and Loss

	Company		Group	
	2010 £'000	2009 £'000	**2010 £'000**	2009 £'000
Equity investments listed on recognised investment exchanges	**79,114**	40,655	**79,114**	40,655
Unlisted investments	**462**	686	**–**	–
	79,576	41,341	**79,114**	40,655

	Company				Group		
	Listed in UK £'000	Listed overseas £'000	Unlisted £'000	Total £'000	Listed in UK £'000	Listed overseas £'000	Total £'000
Opening cost	9,081	46,807	100	55,988	9,081	46,807	55,888
Holding (losses)/gains	(1,896)	(13,337)	586	(14,647)	(1,896)	(13,337)	(15,233)
Opening fair value	7,185	33,470	686	41,341	7,185	33,470	40,655
Purchases at cost	–	34,042	–	34,042	–	34,042	34,042
Sales – proceeds	(8,278)	(16,551)	–	(24,829)	(8,278)	(16,551)	(24,829)
– losses on sales	(803)	(3,008)	(100)	(3,911)	(803)	(3,008)	(3,811)
Holding gains/(losses)	1,896	31,161	(124)	32,933	1,896	31,161	33,057
Closing fair value	–	79,114	462	79,576	–	79,114	79,114
Closing cost	–	61,290	–	61,290	–	61,290	61,290
Holding gains	–	17,824	462	18,286	–	17,824	17,824
Closing valuation	**–**	**79,114**	**462**	**79,576**	**–**	**79,114**	**79,114**

TRANSACTION COSTS

The Group incurred transaction costs of £100,000 on the purchase and sale of investments (2009: £75,000).

	Company 2010 £'000	**Group 2010 £'000**
Losses on sales	**(3,911)**	**(3,811)**
Increase in holding gains	**32,933**	**33,057**
Gains on investments held at fair value	**29,022**	**29,246**

10 Current Assets

	Company		Group	
	2010 £'000	2009 £'000	**2010 £'000**	2009 £'000
Amounts due from brokers	**58**	200	**58**	200
Prepayments and accrued income	**317**	193	**317**	193
	375	393	**375**	393

CASH AND CASH EQUIVALENTS

These comprise bank balances and cash held by the Group including short-term bank deposits with an original maturity of three months or less. The carrying amount of these assets approximates to their fair value.

Notes to the Accounts continued
for the year ended 31 March 2010

11 Current Liabilities

	Company		Group	
	2010 £'000	2009 £'000	**2010 £'000**	2009 £'000
Amounts due to brokers	**–**	175	**–**	175
Loan from subsidiary undertaking	**462**	680	**–**	–
Revolving credit facility	**9,812**	2,500	**9,812**	2,500
Other creditors	**180**	210	**181**	211
	10,454	3,565	**9,993**	2,886

The Company has an unsecured €14 million revolving credit facility of which a sterling equivalent of £9,812,000 was drawn down as at 31 March 2010. £8,920,000 is repayable on 9 June 2010 and £892,000 is repayable on 30 July 2010 (2009: £2,500,000, repayable on 2 April 2009). The facility as a whole matures on 30 July 2010 and it is the Board's intention to renew it on a similar basis.

Under the bank covenants relating to the facility, the Company is to ensure that at all times the total borrowings of the Company do not exceed 40% of the Adjusted Net Asset Value and that the Adjusted Net Asset Value does not fall below £32 million. The Company met all covenant conditions during the year.

12 Share Capital

	Company and Group	
	2010 £'000	2009 £'000
Authorised:		
30,000,000 Ordinary Shares of 50p each	**15,000**	15,000
Issued and fully paid:		
17,448,260 Ordinary Shares of 50p each at 31 March 2010 (2009: 17,448,260)	**8,724**	8,724

Of the above shares in issue, the movements in Ordinary Shares held in treasury are:

	2010	2009
As at 1 April	**875,000**	250,000
Purchased during the year	**–**	625,000
As at 31 March	**875,000**	875,000

The cost of purchasing shares held for treasury during the year was £nil (2009: £1,889,000).

CAPITAL MANAGEMENT

The Group's capital is represented by the issued share capital, Share Premium Account, Capital Redemption Reserve, Capital Reserve and Revenue Reserve.

The Group's capital is managed in accordance with its investment policy, in pursuit of its investment objective, both of which are detailed in the Report of the Directors.

13 Net Asset Values

	Company and Group Net asset value per share		Company and Group Net asset value	
	2010 p	2009 p	**2010 £'000**	2009 £'000
Net asset value per Ordinary Share	**428.76**	257.36	**71,059**	42,653

The net asset value per share is based on net assets at the year end and on 16,573,260 (2009: 16,573,260) Ordinary Shares, being the number of Ordinary Shares in issue at the year end, excluding those shares bought back and held in treasury.

14 Significant Interests

Name	Country of incorporation or registration	Class of capital	Share capital and reserves £'000	Profit for the year £'000	Percent of class held	Percent of equity held	Valuation at 31 March 2010 £'000
MESCT Securities Limited	Scotland	Ordinary	462	–	100	100	462

On 31 March 2010 MESCT Securities Limited repaid £99,999 of share capital to Montanaro European Smaller Companies Trust plc. On the same date MESCT Securities Limited paid a dividend of £125,000 to Montanaro European Smaller Companies Trust plc.

15 Financial Instruments

The Group's financial instruments comprise its investment portfolio, cash balances, bank loan, and debtors and creditors that arise directly from its operations. As an investment trust the Company holds a portfolio of financial assets in pursuit of its investment objective. The Group makes use of borrowings, as detailed in Note 11 and the Chairman's Statement, to achieve improved performance in rising markets. The downside risk of borrowings may be reduced by raising the level of cash balances held.

Listed fixed asset investments held (see Note 9) are valued at fair value. For listed securities this is either bid price or the last traded price depending on the convention of the exchange on which the investment is listed. The fair value of all other financial assets and liabilities is represented by their carrying value in the Balance Sheet shown on page 28. The fair value of the loan is not materially different from the carrying value in the Balance Sheet.

Qualitative risks are discussed in the Report of the Directors on pages 14 to 16.

Quantitive risks arising from the Group's financial instruments are:

(i) market price risk, being the risk that the value of investment holdings will fluctuate as a result of changes in market prices caused by factors other than interest rate or currency rate movements;

(ii) interest rate risk, being the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates;

(iii) foreign currency risk, being the risk that the value of investment holdings, investment purchases, investment sales, bank loans and income will fluctuate because of movements in currency rates;

(iv) credit risk, being the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Group; and

(v) liquidity risk, being the risk that the Group may not be able to liquidate quickly its investments to meet obligations associated with its financial liabilities.

Notes to the Accounts continued
for the year ended 31 March 2010

The Group held the following categories of financial instruments as at 31 March 2010:

	Level 1 £'000	Level 2 £'000	Level 3 £'000	2010 £'000	Level 1 £'000	Level 2 £'000	Level 3 £'000	2009 £'000
Financial instruments (Group)								
Investments	**79,114**	**–**	**–**	**79,114**	40,655	–	–	40,655
Cash	**1,563**	**–**	**–**	**1,563**	4,491	–	–	4,491
Financial instruments (Company)								
Investments	**79,114**	**462**	**–**	**79,576**	40,655	686	–	41,341
Cash	**1,562**	**–**	**–**	**1,562**	4,484	–	–	4,484

The above table provides an analysis of investments based on the fair value hierarchy described below and which reflects the reliability and significance of the information used to measure their fair value. The levels are determined by the lowest (that is the least reliable or least independently observable) level of impact that is significant to the fair value measurement for the individual investment in its entirety as follows:

Level 1 reflects financial instruments quoted in an active market.

Level 2 reflects financial instruments whose fair value is evidenced by comparison with other observable current market transactions in the same instrument or based on a valuation technique whose variables includes only data from observable markets.

Level 3 reflects financial instruments whose fair value is determined in whole or in part using a valuation technique based on assumptions that are not supported by prices from observable market transactions in the same instrument and not based on available observable market data.

16 Market Price Risk
Mitigation of market price risk is part of the fund management process and is typical of equity investment. The portfolio is managed with an awareness of the effects of adverse price movements through detailed and continuing analysis with an objective of maximising overall returns to shareholders. Further information on the investment portfolio is set out on pages 8 to 10.

If the investment portfolio valuation had fallen by 10% at 31 March 2010, the impact on the profit or loss and the net asset value would have been negative £7.9 million (2009: negative £4.1 million). If the investment portfolio valuation had risen by 10% at 31 March 2010, the impact on the profit or loss and the net asset value would have been positive £7.9 million (2009: positive £4.1 million). The calculations are based on the portfolio valuation as at the respective balance sheet dates and are not representative of the year as a whole.

17 Interest Rate Risk
FLOATING RATE

When the Group retains cash balances, the majority of the cash is held in deposit accounts. As at 31 March 2010, the cash position of the Group was £1.6 million (31 March 2009: £4.5 million). The benchmark rate which determines the interest payments received on cash balances is the bank base rate for the relevant currency for each deposit.

The Group has floating rate liabilities that are denominated in Euros. The benchmark rate which determines the interest payments made on the revolving credit facility is based on the rate set by the European Central Bank.

The Company has entered into a €14 million multi currency revolving credit facility with ING Bank N.V., of which a sterling equivalent of £9.8 million was drawn down at 31 March 2010 at a rate of interest of 2.15% pa. As at 31 March 2009 a sterling equivalent of £2.5 million was drawn down at a rate of interest of 6.94% pa.

If the bank base rate had increased by 1.0%, the impact on the profit or loss would have been negative £82,000 (2009: positive £20,000). If the bank base rate had decreased by 1.0%, the impact on the profit or loss would have been positive £82,000 (2009: negative £20,000). The calculations are based on the cash and loan balances as at the respective balance sheet dates and are not representative of the year as a whole.

18 Foreign Currency Risk

The Group invests in overseas securities and holds foreign currency cash balances which give rise to currency risks. It is not the Group's policy to hedge this risk on a continuing basis but it may do so from time to time.

Foreign currency exposure:

	2010 Investments £'000	**2010 Cash £'000**	**2010 Loans £'000**	2009 Investments £'000	2009 Cash £'000	2009 Loans £'000
Euro	**58,555**	**734**	**(9,812)**	26,404	3,581	–
Norwegian Krone	**3,573**	**–**	**–**	1,029	–	–
Swedish Krona	**11,469**	**–**	**–**	4,225	7	–
Swiss Franc	**5,517**	**–**	**–**	1,812	–	–
Total	**79,114**	**734**	**(9,812)**	33,470	3,588	–

In addition, the following currency amounts are included within current assets: dividends receivable in Euros of £295,000 and withholding tax recoverable in Euros of £20,000. As at 31 March 2009, the Group had dividends receivable in Euros of £124,000 and withholding tax recoverable in Euros of £45,000, and Swiss Francs of £5,000.

As at 31 March 2010, the Group had loan interest payable in Euros of £67,000 included within current liabilities (2009: £82,000).

If the value of sterling had weakened by 5% against each of the currencies in the portfolio, the impact on the profit or loss and the net asset value would have been negative £478,000 (2009: positive £189,000). If the value of sterling had strengthened by 5% against each of the currencies in the portfolio, the impact on the profit or loss and the net asset value would have been positive £432,000 (2009: negative £171,000). The calculations are based on cash and loan balances only as at the respective balance sheet dates and are not representative of the year as a whole.

19 Credit Risk

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Group. The Group has in place a monitoring procedure in respect of counterparty risk which is reviewed on an ongoing basis. The carrying amounts of financial assets best represent the maximum credit risk exposure at the balance sheet date.

The Group had the following categories of financial assets exposed to credit risk as at 31 March 2010:

	2010 £'000	2009 £'000
Cash and cash equivalents	**1,563**	4,491
Amounts due from brokers	**58**	200
Interest, dividends and other receivables	**315**	193
	1,936	4,884

Notes to the Accounts continued
for the year ended 31 March 2010

Credit risk arising on transactions with brokers relates to transactions awaiting settlement. Risk relating to unsettled transactions is considered to be small due to the short settlement period involved and the high credit quality of the brokers used. The Manager monitors the quality of service provided by the brokers used to further mitigate this risk.

There were no significant concentrations of credit risk to counterparties at 31 March 2010 or 31 March 2009. No individual investment exceeded 3.0% of the investment portfolio at 31 March 2010 (2009: 4.4%).

A significant majority of the assets of the Company which are traded on a recognised exchange are held in segregated accounts on behalf of the Company by JPMorgan Chase Bank ('JPM'), the Company's custodian. Bankruptcy or insolvency of this or other custodians may cause the Company's rights with respect to securities held by the custodians to be delayed. The Board monitors the Company's risk by reviewing the custodians' internal control reports.

The Company's cash balances are held by a number of counterparties. Bankruptcy or insolvency of these counterparties may cause the Company's rights with respect to the cash balances to be delayed or limited. The Manager and Administrator monitor the credit quality of the relevant counterparties and should the credit quality or the financial position of these counterparties deteriorate significantly the cash holdings will be moved to another bank.

20 Liquidity Risk

The Group does not hold unlisted securities (31 March 2009: £nil). The Group's listed securities are considered to be readily realisable.

As with all small company investment trusts, there are times when the liquidity of the underlying portfolio is poor, such as when smaller companies are out of favour or during periods of adverse economic conditions. The Manager focuses on smaller companies where the opportunities may be more attractive but this can decrease overall underlying liquidity. This may result in the Manager being unable to buy or sell individual holdings within the portfolio. The Manager constantly reviews the underlying liquidity of the portfolio and deals with a wide range of brokers to enhance its ability to execute and minimise liquidity risk. The Company's overall liquidity risks are monitored on a regular basis by the Board.

The Group maintains sufficient investments in cash and readily realisable securities to pay accounts payable and accrued expenses. Short term flexibility is achieved, where necessary, through the use of overdraft facilities.

CONTRACTUAL MATURITY ANALYSIS FOR FINANCIAL LIABILITIES

	Within one month £'000	Between one and three months £'000	Between three and twelve months £'000	Between one and five years £'000	After five years £'000	Total £'000
Current liabilities						
Other creditors	3	111	–	–	–	114
Revolving credit facility	–	9,028	900	–	–	9,928
Total liabilities	**3**	**9,139**	**900**	**–**	**–**	**10,042**

Shareholder Information

Annual General Meeting

The Annual General Meeting of Montanaro European Smaller Companies Trust plc will be held at 53 Threadneedle Street, London EC2R 8AR, on Tuesday 27 July 2010 at 12 noon.

Key Dates

31 March 2010	Company year end
1 April 2010	Payment of second interim dividend
June 2010	Annual results announced
27 July 2010	Annual General Meeting
November 2010	Interim results announced
January 2011	Payment of expected interim dividend

Dividends

Shareholders who wish to have dividends paid directly into a bank account rather than by cheque to their registered address can complete a Mandate Form for this purpose. Mandates can be obtained from Equiniti Limited on request at the address shown on page 11.

Change of Address

Communications with shareholders are mailed to the address held on the share register. In the event of a change of address or other amendment this should be notified to Equiniti Limited under the signature of the registered holder.

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 ('AIC').

Share Savings Scheme

UK residents can invest in the Company's shares through savings plans which are administered by Alliance Trust Savings ('ATS'). ATS provides and administers a range of self-select investment plans, including tax-advantaged ISAs and SIPPs, and First Steps, an investment plan for children. More information can be obtained by contacting ATS on 08000 326 323 or visiting www.alliancetrust.co.uk.

Sources of Further Information

The Company's share price is listed in the *Financial Times* under Investment Companies, and in other newspapers. Information on the Company is also available on the Manager's website: www.montanaro.co.uk.

Glossary of Terms

Association of Investment Companies ('AIC')
The Association of Investment Companies is the trade body for investment trusts (www.theaic.co.uk).

Benchmark
This is a measure against which an investment trust's performance is compared. The benchmark of the Company is the MSCI Europe SmallCap (ex UK) Index (in sterling terms).

Discount
If the share price of an investment trust is less than its net asset value per share, the shares are trading at a discount.

Dividend
The income from an investment. Some investment trusts pay dividends on a quarterly or monthly basis. The majority, including the Company, pay dividends twice yearly.

Gearing
Unlike open-ended investment companies ('OEICs') and unit trusts, investment trusts have the ability to borrow to invest. This term is used to describe the level of borrowings that an investment trust has undertaken, and is stated as a percentage of shareholders' funds. The higher the level of borrowings, the higher the gearing ratio.

Investment Trust
An investment company which satisfies the requirements of Section 842 of the Income and Corporation Taxes Act 1988. Companies which meet these criteria are exempt from having to pay tax on the capital gains they realise from sales of the investments within their portfolios.

Market Capitalisation
The stock market value of a company as determined by multiplying the number of shares in issue by the market price of the shares.

Net Assets
This is calculated as the value of the investments and other assets of an investment trust plus cash and debtors less borrowings and any other creditors. It represents the underlying value of an investment trust at a point in time.

Net Asset Value ('NAV') per Share
This is calculated as the net assets of an investment trust divided by the number of shares in issue.

Ordinary Shares
The main type of equity capital issued by conventional investment trusts. Shareholders are entitled to their share of both income, in the form of dividends paid by the investment trust, and any capital growth. This Company has only ordinary shares in issue.

Premium
If the share price of an investment trust is greater than its net asset value per share, the shares are trading at a premium. It is more common for an investment trust's shares to trade at a discount than a premium.

Shareholders' Funds
See Net Assets.

Share Price
The value of a share at a point in time as quoted on a stock exchange. The shares of the Company are quoted on the London Stock Exchange.

Total Assets
For an investment trust, this figure would give an indication of the value of all the company's investments before deducting any borrowings.

Total Expense Ratio ('TER')
This is a measure of the level of expenses incurred by an investment trust during a reporting period. It is calculated as the sum of the investment management fee and other expenses divided by the average net assets during the period.

Total Return
This is a measure of return on an investment. For a given period it will include both the movement in the market value of an investment and any income received from it.

Notice of Annual General Meeting

Notice is hereby given that the twenty-ninth Annual General Meeting of Montanaro European Smaller Companies Trust plc (the 'Company') will be held at 53 Threadneedle Street, London, EC2R 8AR, on Tuesday 27 July 2010 at 12 noon for the purposes of considering and, if thought fit, passing the following resolutions, of which resolutions 1 to 9 will be proposed as ordinary resolutions and resolutions 10 to 12 will be proposed as special resolutions.

Ordinary Resolutions

RESOLUTION 1 – REPORT AND ACCOUNTS

That the Report and Accounts of the Company for the year ended 31 March 2010 be received.

RESOLUTION 2 – DIRECTORS' REMUNERATION REPORT

That the Directors' Remuneration Report for the year ended 31 March 2010 be approved.

RESOLUTION 3 – RE-ELECTION OF DIRECTOR

That Mr R B M Graham, who retires annually, be re-elected as a Director.

RESOLUTION 4 – RE-ELECTION OF DIRECTOR

That Mr R A Hammond-Chambers, who retires annually, be re-elected as a Director.

RESOLUTION 5 – RE-ELECTION OF DIRECTOR

That Mr J Lumsden, who retires annually, be re-elected as a Director.

RESOLUTION 6 – RE-ELECTION OF DIRECTOR

That Mr R M Martin, who retires annually, be re-elected as a Director.

RESOLUTION 7 – RE-ELECTION OF DIRECTOR

That Mr A R Irvine, who retires annually, be re-elected as a Director.

RESOLUTION 8 – RE-APPOINTMENT OF AUDITORS

That Ernst & Young LLP be re-appointed as the Company's Auditors, to hold office until the conclusion of the next general meeting at which accounts are laid before the Company, and that the Directors be authorised to determine their remuneration.

RESOLUTION 9 – AUTHORITY TO ALLOT SHARES

That, in substitution for any existing authority under section 80 of the Companies Act 1985 but without prejudice to the exercise of any such authority prior to the date of the passing of this resolution, the board of directors of the Company (the 'Board') be and is hereby generally and unconditionally authorised pursuant to and in accordance with section 551 of the Companies Act 2006 (the 'Act') to exercise all the powers of the Company to allot shares in the Company and to grant rights to subscribe for or to convert any security into shares in the Company up to an aggregate nominal amount of £828,663 provided that this authority shall expire at the conclusion of the annual general meeting of the Company to be held in 2011 or, if earlier, 30 September 2011 save that the Company may before such expiry make an offer or agreement which would or might require shares to be allotted, or rights to subscribe for or to convert securities into shares to be granted, after such expiry and the Board may allot shares or grant such rights in pursuance of such an offer or agreement as if the authority conferred hereby had not expired.

Notice of Annual General Meeting continued

Special Resolutions

RESOLUTION 10 – AUTHORITY TO ALLOT SHARES OTHER THAN ON A PRE-EMPTIVE BASIS

That, subject to the passing of resolution 9 and in substitution for any existing authority under section 95 of the Companies Act 1985 but without prejudice to the exercise of any such authority prior to the date of the passing of this resolution, the board of directors of the Company (the 'Board') be and is hereby generally empowered pursuant to sections 570 and 573 of the Companies Act 2006 (the 'Act') to allot equity securities (within the meaning of section 560 of the Act) (including the grant of rights to subscribe for, or to convert any securities into, ordinary shares of 50 pence each in the capital of the Company ('Ordinary Shares') for cash either pursuant to the authority conferred on them by such resolution 9 or by way of a sale of treasury shares (within the meaning of section 560(3) of the Act) as if section 561(1) of the Act did not apply to any such allotment, provided that this power shall be limited to:

(i) the allotment of equity securities in connection with a rights issue, open offer or other pre-emptive offer in favour of the holders of Ordinary Shares who are on the register of members on a date fixed by the Board where the equity securities respectively attributable to the interests of all such ordinary shareholders are proportionate (as nearly as may be practicable) to the respective numbers of Ordinary Shares held by them on that date (subject to such exclusions or other arrangements in connection with the rights issue, open offer or other offer as the Board deem necessary or expedient to deal with shares held in treasury, fractional entitlements to equity securities and to deal with any legal or practical problems or issues arising in any overseas territory or under the requirements of any regulatory body or stock exchange); and

(ii) the allotment (otherwise than pursuant to sub-paragraph (i) above) of equity securities up to an aggregate nominal amount of £828,663,

and shall expire (unless previously renewed, varied or revoked by the Company in general meeting) at the conclusion of the annual general meeting of the Company to be held in 2011 or, if earlier, 30 September 2011 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 Board may allot equity securities in pursuance of such an offer or agreement as if the authority conferred hereby had not expired. This power shall authorise the Board to issue equity securities at such issue price as the Board may determine (including, without limitation, where equity securities are being issued from treasury at a price below the net asset value per ordinary share of the Company at the time of the relevant issue).

RESOLUTION 11 – AUTHORITY TO BUY BACK SHARES

That, in substitution for any existing authority under section 166 of the Companies Act 1985 but without prejudice to the exercise of any such authority prior to the date of the passing of this resolution, the Company be and is hereby generally and unconditionally authorised for the purposes of section 701 of the Companies Act 2006 (the 'Act') to make one or more market purchases (as defined in section 693(4) of the Act) of ordinary shares of 50 pence each in the capital of the Company ('Ordinary Shares') on such terms and in such manner as the board of directors may determine provided that universally:

(i) the maximum aggregate number of Ordinary Shares which may be purchased is 14.99 per cent of the number of Ordinary Shares in issue immediately prior to the passing of this resolution;

(ii) the minimum price which may be paid for an Ordinary Share is 50 pence (exclusive of associated expenses);

(iii) the maximum price which may be paid for an Ordinary Share (exclusive of associated expenses) shall not be more than the higher of: (a) an amount equal to 105 per cent of the average of the middle market quotations for an Ordinary Share as derived from the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the Ordinary Share is purchased; and (b) the higher of the last independent trade and the highest current independent bid on the London Stock Exchange for an Ordinary Share; and

(iv) unless previously renewed, varied or revoked, this authority shall expire at the conclusion of the annual general meeting of the Company to be held in 2011 or, if earlier, 30 September 2011 save that the Company may before such expiry enter into a contract to purchase Ordinary Shares which will or may be completed wholly or partly after such expiry and a purchase of Ordinary Shares may be made pursuant to any such contract.

RESOLUTION 12 – ADOPTION OF NEW ARTICLES OF ASSOCIATION

That:

(i) the articles of association of the Company be amended by deleting all of the provisions of the Company's memorandum of association which, by virtue of section 28 of the Companies Act 2006, are treated as part of the Company's articles of association;

(ii) the articles of association of the Company be amended by deleting all of the provisions referred to in paragraph 42 of schedule 2 of the Companies Act 2006 (Commencement No. 8, Transitional Provisions and Savings) Order 2008 (Statutory Instrument 2008 No. 2860); and

(iii) the draft regulations produced at the meeting and initialled by the chairman of the meeting for the purposes of identification be adopted as the articles of association of the Company in substitution for, and to the entire exclusion of, the articles of association of the Company existing at the date of the meeting.

By order of the Board

F&C INVESTMENT BUSINESS LIMITED
Company Secretary
9 June 2010

Notice of Annual General Meeting continued

Notes

1. **Attending the Annual General Meeting in Person**
   If you wish to attend the Annual General Meeting in person, you should arrive at the venue for the Annual General Meeting in good time to allow your attendance to be registered. It is advisable to have some form of identification with you as you may be asked to provide evidence of your identity to the Company's registrar, Equiniti Limited (the 'Registrar') prior to being admitted to the Annual General Meeting.

2. **Appointment of Proxies**
   Members are entitled to appoint one or more proxies to exercise all or any of their rights to attend, speak and vote at the Annual General Meeting. A proxy need not be a member of the Company but must attend the Annual General Meeting to represent a member. To be validly appointed a proxy must be appointed using the procedures set out in these notes and in the notes to the accompanying proxy form.

   If members wish their proxy to speak on their behalf at the meeting, members will need to appoint their own choice of proxy (not the chairman of the Annual General Meeting) and give their instructions directly to them.

   Members can only appoint more than one proxy where each proxy is appointed to exercise rights attached to different shares. Members cannot appoint more than one proxy to exercise the rights attached to the same share(s). If a member wishes to appoint more than one proxy, they should contact the Registrar on 0871 384 2030. Calls to this number are charged at 8p per minute from a BT landline. Other telephony providers' costs may vary. Lines are open from 8.30 a.m. to 5.30 p.m. Monday to Friday. If calling from overseas please call +44 121 415 7047.

   A member may instruct their proxy to abstain from voting on any resolution to be considered at the meeting by marking the 'vote withheld' option when appointing their proxy. It should be noted that an abstention is not a vote in law and will not be counted in the calculation of the proportion of votes 'for' or 'against' the resolution.

   The appointment of a proxy will not prevent a member from attending the Annual General Meeting and voting in person if he or she wishes.

   A person who is not a member of the Company but who has been nominated by a member to enjoy information rights does not have a right to appoint any proxies under the procedures set out in these notes and should read Note 8 below.

3. **Appointment of a Proxy Using a Proxy Form**
   A proxy form for use in connection with the Annual General Meeting is enclosed. To be valid any proxy form or other instrument appointing a proxy, together with any power of attorney or other authority under which it is signed or a certified copy thereof, must be received by post or (during normal business hours only) by hand by the Registrar at Equiniti Limited, Freepost 10850, Aspect House, Spencer Road, Lancing, West Sussex, BN99 6ZR no later than 48 hours (excluding non-working days) before the time of the Annual General Meeting or any adjournment of that meeting.

   If you do not have a proxy form and believe that you should have one, or you require additional proxy forms, please contact the Registrar on 0871 384 2030. Calls to this number are charged at 8p per minute from a BT landline. Other telephony providers' costs may vary. Lines are open from 8.30 a.m. to 5.30 p.m. Monday to Friday. If calling from overseas please call +44 121 415 7047.

4. **Appointment of a Proxy Through CREST**
   CREST members who wish to appoint a proxy or proxies through the CREST electronic proxy appointment service may do so by using the procedures described in the CREST Manual and by logging on to the following website: www.euroclear.com/CREST. 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 using the CREST service 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 instruction, as described in the CREST Manual. The message, regardless of whether it constitutes the appointment of a proxy or is an amendment to the instruction given to a previously appointed proxy, must in order to be valid, be transmitted so as to be received by the Registrar (ID RA19) no later 48 hours (excluding non-working days) before the time of the Annual General Meeting or any adjournment of that meeting. 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 Application Host) from which the Registrar 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 provider(s) should note that Euroclear UK & Ireland Limited does not make available special procedures in CREST for any particular message. 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 system 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.

5. Appointment of Proxy by Joint Holders

In the case of joint holders, where more than one of the joint holders purports to appoint one or more proxies, only the purported appointment submitted by the most senior holder will be accepted. Seniority is determined by the order in which the names of the joint holders appear in the Company's register of members in respect of the joint holding (the first named being the most senior).

6. Corporate Representatives

Any corporation which is a member can appoint one or more corporate representatives. Members can only appoint more than one corporate representative where each corporate representative is appointed to exercise rights attached to different shares. Members cannot appoint more than one corporate representative to exercise the rights attached to the same share(s).

7. Entitlement to Attend and Vote

To be entitled to attend and vote at the Annual General Meeting (and for the purpose of determining the votes they may cast), members must be registered in the Company's register of members at 6.00 p.m. on 23 July 2010 (or, if the Annual General Meeting is adjourned, at 6.00 p.m. on the day two days prior to the adjourned meeting). Changes to the register of members after the relevant deadline will be disregarded in determining the rights of any person to attend and vote at the Annual General Meeting.

8. Nominated Persons

Any person to whom this notice is sent who is a person nominated under section 146 of the Companies Act 2006 (the '2006 Act') to enjoy information rights (a 'Nominated Person') may, under an agreement between him/her and the member 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 member as to the exercise of voting rights.

Notice of Annual General Meeting continued

9. Website Giving Information Regarding the Annual General Meeting
Information regarding the Annual General Meeting, including information required by section 311A of the 2006 Act, and a copy of this notice of Annual General Meeting is available from www.montanaro.co.uk.

10. Audit Concerns
Members should note that it is possible that, pursuant to requests made by members of the Company under section 527 of the 2006 Act, the Company may be required to publish on a website a statement setting out any matter relating to: (a) 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 (b) any circumstance 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 2006 Act. 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 2006 Act. Where the Company is required to place a statement on a website under section 527 of the 2006 Act, 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 2006 Act to publish on a website.

11. Voting Rights
As at 9 June 2010 (being the latest practicable date prior to the publication of this notice) the Company had 17,448,260 Ordinary Shares in issue, including 875,000 Shares held in treasury. Each Ordinary Share (other than those held in treasury) carries one vote. The total voting rights in the Company as at 9 June 2010 were 16,573,260 votes.

12. Notification of Shareholdings
Any person holding 3 per cent or more of the total voting rights of the Company who appoints a person other than the Chairman of the General Meeting as his proxy will need to ensure that both he, and his proxy, comply with their respective disclosure obligations under the UK Disclosure and Transparency Rules.

13. Further Questions and Communication
Under section 319A of the 2006 Act, the Company must cause to be answered any question relating to the business being dealt with at the Annual General Meeting put by a member attending the meeting unless answering the question would interfere unduly with the preparation for the meeting or involve the disclosure of confidential information, or the answer has already been given on a website in the form of an answer to a question, or it is undesirable in the interests of the Company or the good order of the meeting that the question be answered.

Members who have any queries about the Annual General Meeting should contact the Company Secretary at 80 George Street, Edinburgh EH2 3BU.

Members may not use any electronic address provided in this notice or in any related documents (including the accompanying circular and proxy form) to communicate with the Company for any purpose other than those expressly stated.

14. Documents Available for Inspection
The following documents will be available for inspection at the registered office of the Company and 53 Threadneedle Street, London EC2R 8AR during normal business hours on any weekday (Saturdays, Sundays and English public holidays excepted) from the date of this notice until the conclusion of the Annual General Meeting:

14.1 a copy of the proposed new articles of association of the Company;

14.2 copies of the Directors' letters of appointment; and

14.3 copies of the Directors' deeds of indemnity.

Appendix to Notice of Annual General Meeting

Summary of the Proposed Material Amendments to the Articles of Association of the Company

The material amendments to the Company's existing articles of association arising from the proposed adoption of the New Articles are summarised below.

This Appendix to the Notice of Annual General Meeting does not summarise non-material changes and in particular it does not summarise changes of a minor, technical or clarifying nature. A copy of the New Articles will be available for inspection at the registered office of the Company and at the offices of Montanaro Asset Management Limited, 53 Threadneedle Street, London EC2R 8AR during normal business hours on any weekday (Saturdays, Sundays and public holidays excepted) from the date of the notice of the AGM until the conclusion of the Annual General Meeting.

Repeal of the Companies Act 1985

On 1 October 2009 those provisions of the Companies Act 2006 which had not yet been brought in to force (which affect the articles of association of the Company) came into force with the effect that the Companies Act 1985 is no longer relevant to the Company's articles of association. The New Articles will therefore not contain references to the Companies Act 1985 and any consequential drafting changes have been made.

Provisions of the Company's Memorandum of Association (the 'Memorandum')

The Companies Act 2006 significantly reduces the constitutional significance of a company's memorandum. The Companies Act 2006 provides that a memorandum will record only the names of subscribers and the number of shares each subscriber has agreed to take in the Company. Under the Companies Act 2006, the objects clause and all other provisions contained in a company's memorandum were, from 1 October 2009, deemed to be contained in a company's articles of association but the Company can remove these provisions by special resolution.

In addition, the Companies Act 2006 states that unless a company's articles of association provide otherwise, a company's objects are unrestricted. This abolishes the need for companies to have an objects clause. For this reason, the Company is proposing to remove its objects clause together with all other provisions of its Memorandum which, by virtue of the Companies Act 2006, were treated as forming part of the Current Articles from 1 October 2009. Resolution 12 confirms the removal of these provisions for the Company. As the effect of this resolution will be to remove the statement currently in the Memorandum regarding shareholders' limited liability, the New Articles also contain an express statement regarding the limited liability of shareholders. The New Articles also contain an express statement that the Company's objects are unlimited to allow it to have the widest possible scope of activities.

Change of Name

Under the Companies Act 1985 a company can only change its name by special resolution. Under the Companies Act 2006, a company is able to change its name by other means provided for by its articles of association. To take advantage of this provision, the New Articles enable the Directors to pass a resolution to change the Company's name. The Directors have no current intention to use this power.

Authorised Share Capital and Unissued Shares

The Companies Act 2006 abolishes the requirement for a company to have an authorised share capital. The Company is proposing changes to the Current Articles to reflect this abolition. The Directors will still be limited as to the number of shares they can allot at any time because allotment authority from shareholders continues to be required under the Companies Act 2006 save in respect of employee share schemes.

Provisions of the Current Articles which are no longer relevant as a result of this change to the law have been deleted from the New Articles.

Appendix to Notice of Annual General Meeting continued

Redeemable Shares
Under the Companies Act 1985, if a company wished to issue redeemable shares it was required to include in its articles of association the terms and manner of redemption. The Companies Act 2006 enables directors to determine such matters instead provided they are so authorised by the articles. The New Articles contain such an authorisation. The Company has no plans to issue redeemable shares but if it did so the Directors would need shareholders' authority to issue new shares in the usual way.

Share Warrants to Bearer
The New Articles provide the Company with the ability to issue warrants to bearer (a 'Share Warrant') stating that the bearer of the Share Warrant is entitled to the shares specified in it. The Board may determine and vary the conditions upon which Share Warrants shall be issued.

Suspension of Registration of Share Transfers
The Current Articles permit the Directors to suspend the registration of transfers. Under the Companies Act 2006, share transfers must be registered as soon as practicable. The power in the Current Articles to suspend the registration of transfers is inconsistent with this requirement. Accordingly, this power has been removed in the New Articles.

Corporate Representatives
The Companies Act 2006 has been amended to clarify that where a shareholder appoints more than one corporate representative in respect of its shareholding, but in respect of different shares, those corporate representatives can act independently of each other, and validly vote in different ways. The New Articles reflect this matter.

Multiple Proxies
The Companies Act 2006 has been amended to clarify the position concerning the rights of proxies when voting on a show of hands in the event that a proxy has been appointed for the same meeting by more than one member and where a member appoints more than one proxy in respect of different shares within the same holding. The New Articles reflect the revised position under the Companies Act 2006.

Vacation of Office by Directors
The Current Articles specify the circumstances in which a Director must vacate office. The New Articles update these provisions to reflect the approach taken on mental and physical incapacity in the model articles for public companies produced by the Department for Business, Innovation and Skills.

Chairman's Casting Vote
Provisions in Current Articles giving the chairman a casting vote at shareholders' meetings became ineffective from 1 October 2007, but companies with a casting vote provision in their articles of association on that date were, broadly, allowed to keep it. However, the EU Shareholder Rights Directive (which are implemented by the Regulations) requires that all shareholders be treated equally and therefore this saving provision for UK traded companies has been removed, such that the casting vote provision in the Current Articles became redundant in August 2009.

Provisions No Longer Required
Under the Companies Act 1985 a company wishing to transact certain business, such as making alterations to its share capital, was required to have an authority in its articles of association in order to do so. The 2006 Act does not require such an authority in the articles of association and so the provisions in the existing articles of association dealing with the increase, consolidation, sub-division and cancellation of shares have been deleted.

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