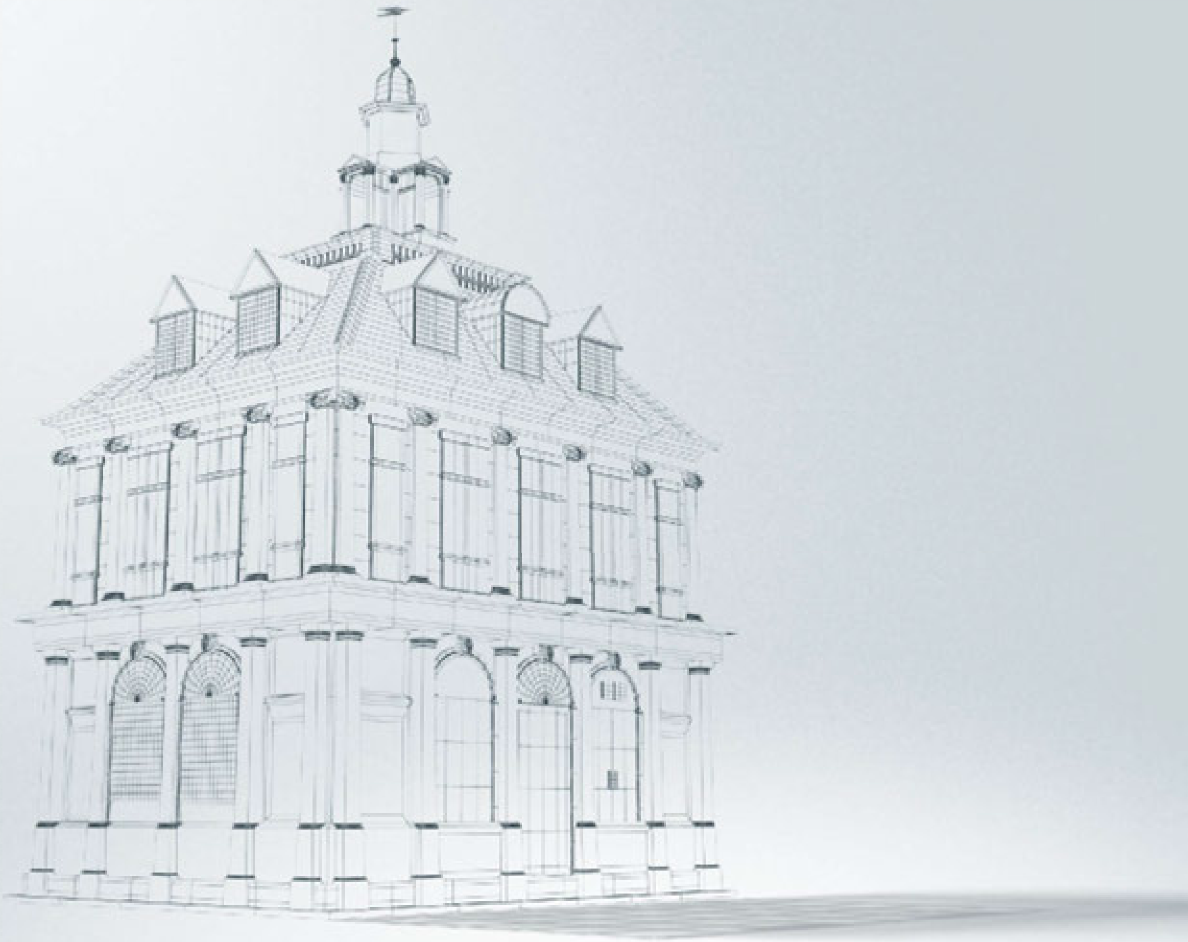
THE HENDERSON SMALLER COMPANIES INVESTMENT TRUST PLC

Annual Report 2016



MANAGED BY
Henderson
GLOBAL INVESTORS

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Moneywise Investment Trust awards 2016 WINNER
UK SMALLER COMPANIES
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Investors Chronicle FT Investment and Wealth Management Awards 2015 Winner
Best UK Growth Fund
Henderson Smaller Companies Investment Trust

Investment Week Investment Company of the Year Awards 2015 WINNER
UK SMALLER COMPANIES

The image on the front cover is based on Custom House in King's Lynn.

Strategic Report

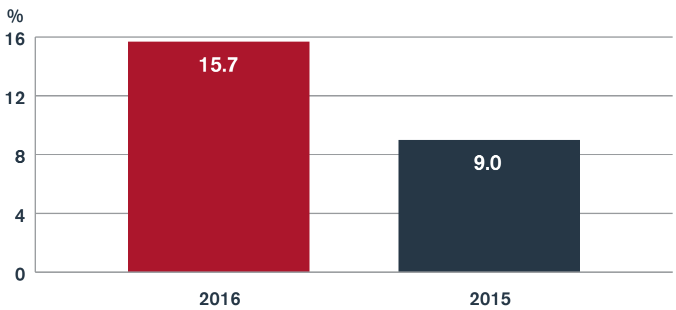
> **“This has been a difficult year for equity investment management and your Company has not been immune. The net assets of the Company declined by 1.1% in the reporting year.”**

Jamie Cayzer-Colvin, Chairman

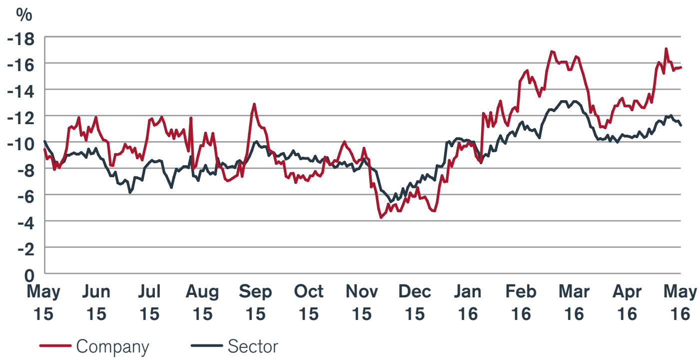
Strategic Report: Performance Highlights

Total Return Performance over the year to 31 May 2016

Discount at year end[4]



Discount[5]



Total Return Performance for the periods ended 31 May 2016

	1 year %	3 years %	5 years %	10 years %
NAV[1]	-1.1	42.9	98.8	195.4
Share Price[2]	-8.1	44.4	112.0	211.6
Benchmark[3]	-1.6	29.4	66.4	140.2
Average Sector NAV[6]	1.6	39.2	76.9	168.7
Average Sector Share Price[7]	5.0	51.3	92.8	182.0
FTSE All-Share Index	-6.3	9.6	31.2	67.5
FTSE SmallCap Index (excluding investment companies)	0.3	34.9	78.6	67.7

Strategic Report: Performance Highlights (continued)

NAV per share at year end

2016 **731.0p** 2015 754.1p

Share price at year end

2016 **616.5p** 2015 686.0p

Dividend for year

2016 **15.0p**[8] 2015 13.5p

Ongoing Charge[10]

2016 **0.44%** 2015 0.46%

Discount at year end

2016 **15.7%** 2015 9.0%

Gearing at year end

2016 **9.1%** 2015 7.5%

Dividend yield[9]

2016 **2.4%** 2015 2.0%

Total net assets

2016 **£546m** 2015 £563m

1 Net Asset Value per ordinary share total return with income reinvested for 1, 3 and 5 years and capital NAV plus income for 10 years
2 Share Price total return using mid-market closing price
3 Numis Smaller Companies Index (excluding investment companies)
4 Calculated using published daily NAVs with debt at par including current year revenue
5 Graph shows the Company's share price discount to NAV compared with the average discount of the AIC UK Smaller Companies sector over the year to 31 May 2016
6 Average NAV total return of the AIC UK Smaller Companies sector
7 Average share price total return of the AIC UK Smaller Companies sector
8 This represents an interim dividend of 4.0p and a proposed final dividend of 11.0p. See page 50 for more details
9 Based on the ordinary dividends paid for the year and the mid-market share price at the year end
10 Ongoing charge excluding performance fee. Ongoing charge including performance fee is 0.44% (2015: 0.88%)
Sources: Morningstar Funddata, Morningstar Direct, Henderson, Datastream
A glossary of terms is included on pages 21 and 22

Strategic Report: Business Model

Investment Objective

The Company's investment objective is to maximise shareholders' total returns by investing mainly in smaller companies that are quoted in the United Kingdom.

Strategy

The strategy of the Company is to pursue its investment objective. This is achieved through the appointment of external management which pursues the Company's investment policy. The investment trust company structure allows the shareholders, whether institutions or private investors, to access a diversified portfolio of investments that is professionally managed.

Investment Selection

We use rigorous research to identify high-quality smaller companies with strong growth potential. The benchmark is the Numis Smaller Companies Index (excluding investment companies). Generally, new investments are made in constituents of the benchmark index but they may continue to be held when the underlying companies grow out of the smaller companies sector. Once a portfolio company enters the FTSE 100 Index the Fund Manager has, in normal circumstances, six months to sell the position.

Investment Policy

The Company's portfolio is managed within a framework of investment limits and restrictions determined by the Board, the primary purpose of which is to spread and mitigate investment risk.

Diversification

The Company maintains a diversified portfolio, which is detailed on pages 8, 14 and 15. The portfolio is actively managed by Henderson, who provide regular reports on investment activity and portfolio construction to the Directors at and between Board meetings. The Company will not invest more than 5% of its total gross assets, calculated as at the time of investment (or additional investment), in any one holding. The Company will not make any investment that, calculated at the time of investment (or additional investment), would result in it holding more than 10% of an investee company's equity. The Board may give approval to Henderson to exceed these limits to as far as 10% and 20% respectively but only in exceptional circumstances.

Asset Allocation

Generally, the Company will invest in smaller companies that are quoted in the United Kingdom. Investments may include shares, securities and related financial instruments, including derivatives.

Gearing

The Company will borrow money for investment purposes if the Board considers it appropriate. Net borrowings are limited to a maximum of 30% of the value of shareholders' funds.

General

In accordance with the Listing Rules of the UK Listing Authority, the Company will not invest more than 15% of its gross assets in the shares of other listed closed-ended investment funds, including investment trusts, and will not invest more than 10% of its gross assets in companies that themselves may invest more than 15% of their gross assets in listed closed-ended investment funds.

Management

The Company has an independent Board of Directors which has appointed Henderson Investment Funds Limited ("HIFL") to act as its Alternative Investment Fund Manager. HIFL delegates investment management services to Henderson Global Investors Limited in accordance with an agreement which was effective from 22 July 2014 and can be terminated on six months' notice. Prior to July 2014 Henderson Global Investors Limited was appointed as Investment Manager. Both entities are authorised and regulated by the Financial Conduct Authority ("FCA"). References to Henderson within this report refer to the services provided by both entities.

The fund management team is led by Neil Hermon, who was appointed as the Company's Fund Manager with effect from November 2002. Neil Hermon has a shareholding in the ordinary shares of the Company. He receives a proportion of any performance fee paid by the Company to Henderson and a proportion of that is deferred into further shares in the Company. Indriatti van Hien was appointed Deputy Fund Manager with effect from 1 June 2016.

Henderson and its subsidiaries also provide accounting, company secretarial and general administrative services. Some of the administration and accounting services are carried out, on behalf of Henderson, by BNP Paribas Securities Services. Rachel Peat ACIS acts as Company Secretary on behalf of the Corporate Secretary, Henderson Secretarial Services Limited.

Since 1 June 2015, the management fee payable to Henderson is calculated quarterly as 0.35% (0.0875% per quarter) of the value of the net assets under management on the last day of the quarter preceding the quarter in respect of which the calculation is made. Assets under management for the purpose of calculating the management fee exclude any holdings in funds managed by Henderson. The management fee is payable quarterly in advance.

Strategic Report: Business Model (continued)

In addition, the management agreement provides for the payment of a performance fee, calculated as 15% of any outperformance of the benchmark index, on a total return basis, over the Company's accounting year. This is subject to a limit on the total management fees payable in any one year of 0.9% of the average value of the net assets of the Company during the year (calculated monthly). There is a further cap to the effect that any enhancement to net asset value resulting from share buy-backs in excess of 5% of the opening issued share capital is excluded from the calculation of the performance fee for the year. No performance fee is payable if on the last day of the Company's accounting year the Company's share price is lower than the share price as at the preceding year end. If on the last day of the Company's accounting year the net asset value per share, calculated, in accordance with the Company's accounting policies, net of costs (including any performance fee), is equal to or lower than the net asset value per share as at the preceding year end, the performance fee payable will be restricted to such amount, if any, as will result in the net asset value per share being higher than the net asset value per share at the preceding year end. There is no performance fee payable in respect of the year ended 31 May 2016 (2015: £2,000,000).

Any underperformance relative to the benchmark, or any unrewarded outperformance (for example as a result of a cap), will be carried forward and set against any outperformance or underperformance respectively in subsequent years. The net amount of outperformance or underperformance carried forward is termed the Historic Amount. At 31 May 2016 this was £62,653,767 (2015: £59,797,100).

Strategic Report: Chairman's Statement

The Chairman of the Company, Jamie Cayzer-Colvin, reports on the year to 31 May 2016

Performance

This has been a difficult year for equity investment management and your Company has not been immune. The net assets of the Company declined by 1.1% in the reporting year, outperforming our benchmark, the Numis Smaller Companies Index (excluding investment companies), by 0.5%. However the Company's discount widened, so the share price fell by 8.1%.

Our Fund Manager, Neil Hermon, and his team have outperformed our benchmark, whether measured over three, five, or ten years. Over the ten years to 31 May 2016, our net asset value total return is 195.4%, versus a total return from the benchmark of 140.2%. This is an impressive compound annual return to shareholders of 11.4% and is continuing testimony to the skills of Neil and his team.

I would, as always, like to thank all the Henderson staff and my Board for their efforts throughout the year on behalf of shareholders. I would also like to congratulate Indriatti van Hien, who was appointed Deputy Fund Manager in June this year, having worked alongside Neil since January 2013.

Board Composition

Keith Percy will be retiring from the Board at the AGM in September. I am very grateful to Keith for his invaluable service to the Company over the past ten years. I would also like to take this opportunity to welcome Victoria Sant to the Board, who will be appointed on 23 September 2016 and will stand for appointment by shareholders. Victoria was an investment manager at the Wellcome Trust for ten years, where she was responsible for the out-sourced long-only equity portion of the £18bn endowment portfolio, and a Trustee Director of the pension scheme. She is currently a senior adviser at the Investor Forum, with an active role engaging with UK-listed companies on strategic and governance issues. She is also a member of the investment committee of the National Trust.

Revenue and Dividend

The revenue return per share has increased to 15.9p, compared with 15.0p for the previous year. The Board is proposing a final dividend for the year of 11.0p per share, making a total dividend for the year of 15.0p (2015: 13.5p), as an interim dividend of 4.0p was paid in March. The final dividend is, of course, subject to shareholder approval at the Annual General Meeting to be held in September. This marks our 13th consecutive year of dividend growth.

Discount and Share Buy-backs

During the year, the AIC UK Smaller Companies sector as a whole traded at an average discount of 9.1% to NAV, with highs and lows of 13.1% and 5.5% respectively. At the year end, the Company's shares traded at a discount of 15.7%. The Company's discount ranged from 17.1% to 4.3%, with the average discount over the year being 10.3%.

The Board continues to monitor the discount and will consider the merits of buying back shares as markets evolve, though we do not currently believe that share buy-backs represent the most effective way of generating long term shareholder value. During the reporting year, no shares were bought back in the Company.

Continuation

Our shareholders are asked every three years to vote for the continuation of the Company, and a resolution to this effect will be put to the Annual General Meeting in September. The Henderson Smaller Companies Investment Trust plc has shown that active investment management, well-executed within the transparent and low-cost structure of an investment trust company, is a highly effective means of gaining exposure to this class of equity. We are therefore recommending shareholders to vote for the Company to continue.

Outlook

After the most dramatic couple of months in British politics, the implications of the Brexit vote are yet to play out fully in markets. Uncertainty is the only certainty and it is clear that volatility will continue until investors feel confident that the way forward for the UK is resolved. We may also find that interest rates remain at the current very low levels for longer and this, together with the weakness in the exchange rate, is likely to affect valuations and investor sentiment over the coming months. Any move back to more normal conditions may therefore be sometime away. However, as always in markets, there will be some companies that do better than others. Exporters can take advantage of the lower value of the pound and companies looking to invest can take advantage of lower rates.

Our view remains that this is the time to stick to what we do best, and we remain confident that skilled active investing founded on the basic fundamentals of investing in quality growth at the right price will win through in these uncertain times. This has always been Neil's style and one that he will continue to adopt.

Annual General Meeting

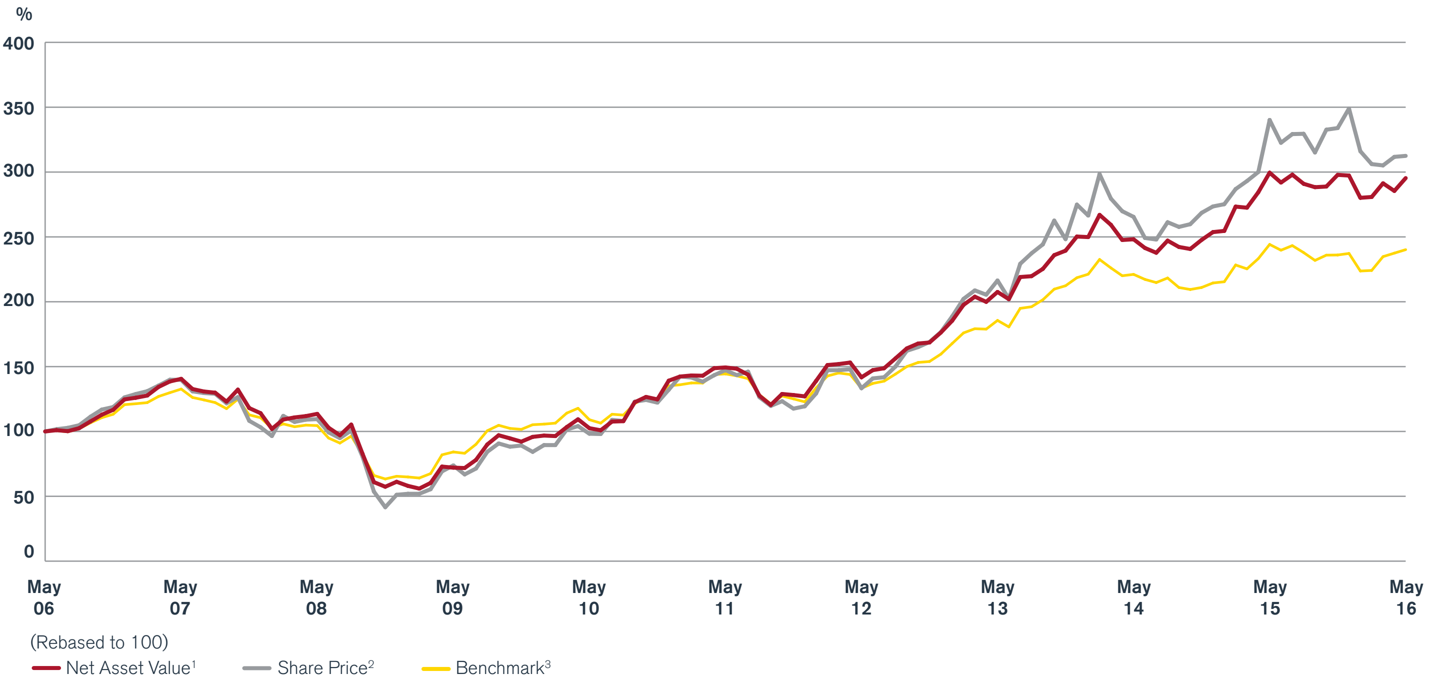
The Annual General Meeting of the Company will be held at 11.30am on Friday 23 September 2016 at the Registered Office, 201 Bishopsgate, London EC2M 3AE. The Notice of Meeting is set out in the accompanying circular to shareholders. We would encourage as many shareholders as possible to attend for the opportunity to meet the Board and to watch a presentation from Neil Hermon reviewing the year and looking forward to the year ahead.

The Company's AGM will be broadcast live on the internet. If you are unable to attend in person, you can watch the meeting as it happens by visiting **www.henderson.com/trustslive**.

Jamie Cayzer-Colvin
Chairman

Strategic Report: Historical Performance and Financial Information

Total Return Performance over the 10 years to 31 May 2016



Financial Information

		NAV per ordinary share			Discount							
At 31 May	Net assets £'000	With debt at par p	With debt at market value p	Mid-market price per ordinary share p	With debt at par %	With debt at market value %	Profit/ (loss) for year £'000	Revenue return p	Capital return p	Total return p	Dividend p	Expenses[4] %
2007	339,700	392.1	385.1	323.5	(17.50)	(16.00)	96,768	2.12	102.59	104.71	1.70	0.55 (1.31)
2008	255,471	317.6	310.9	252.0	(20.65)	(18.94)	(66,112)	4.64	(83.96)	(79.32)	3.80	0.51 (0.51)
2009	156,349	202.1	196.9	167.0	(17.37)	(15.19)	(90,365)	6.30	(121.71)	(115.41)	5.60	0.51 (0.51)
2010	207,533	277.1	269.7	216.0	(22.05)	(19.91)	59,540	4.59	74.70	79.29	3.60	0.58 (0.58)
2011	298,184	398.1	392.5	319.4	(19.77)	(18.62)	93,342	4.91	119.70	124.61	4.20	0.50 (1.16)
2012	279,926	374.5	367.9	284.3	(24.09)	(22.72)	(14,622)	6.07	(25.62)	(19.55)	5.50	0.50 (0.50)
2013	403,420	540.0	535.0	454.0	(15.93)	(15.14)	127,718	6.24	164.72	170.96	6.50	0.47 (1.07)
2014	476,281	637.6	634.3	547.0	(14.21)	(13.76)	79,958	12.67	94.37	107.04	11.00	0.44 (0.56)
2015	563,321	754.1	752.1	686.0	(9.03)	(8.79)	95,631	15.04	112.98	128.02	13.50	0.46 (0.88)
2016[5]	**546,080**	**731.0**	**731.0**	**616.5**	**(15.66)**	**(15.66)**	**(6,783)**	**15.92**	**(25.00)**	**(9.08)**	**15.00**	**0.44 (0.44)**

1 Net Asset Value per ordinary share total return with income reinvested
2 Share Price total return using mid-market closing price
3 Numis Smaller Companies Index (excluding investment companies)
4 Using Total Expense Ratio methodology for 2011 and previous years; Ongoing Charge methodology thereafter, figures excluding performance fee (figures in brackets include performance fee)
5 Since the redemption of the debenture stock, the Company's NAV and discount with debt at par or market value are identical because there is no difference in the values of the remaining debt liabilities

Sources: Morningstar Funddata, Henderson, Datastream

Strategic Report: Portfolio Information

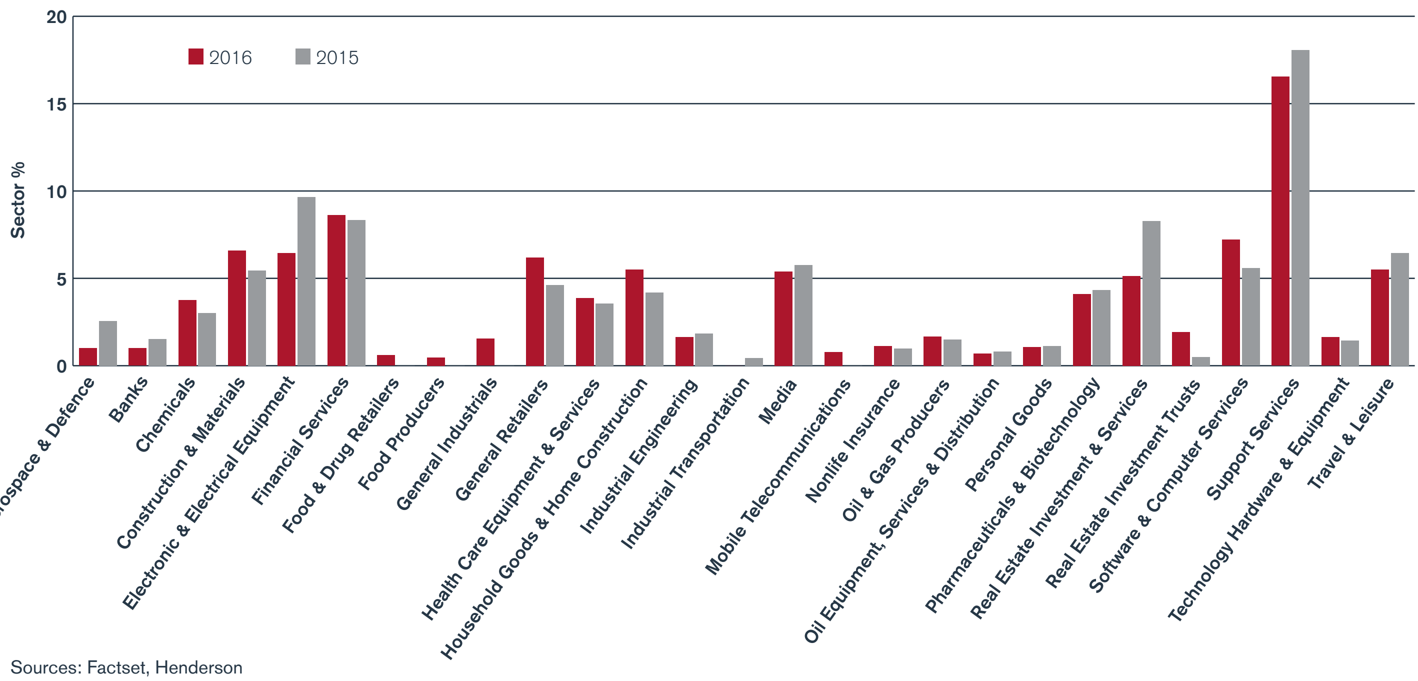
Performance Attribution

	Year ended 31 May	
	2016	2015
NAV total return	-1.1	20.4
Benchmark total return	-1.6	10.4
Relative performance	**0.5**	**10.0**
Made up:		
Stock selection	1.5	10.0
Gearing	-0.6	0.9
Expenses	-0.4	-0.9

Ten Largest Investments at 31 May 2016

Ranking 2016	Ranking 2015	Company	Principal activities	Valuation 2016 £'000	Portfolio %
1	1	Bellway	housebuilder	21,181	3.55
2	11	NMC Health	healthcare provider	16,963	2.85
3	2	e2v Technologies	electronic components	14,418	2.42
4	5	Intermediate Capital	mezzanine finance	12,849	2.16
5	3	Howden Joinery	kitchen manufacturer and retailer	11,915	2.00
6	13	Playtech	internet gaming software	10,557	1.77
7	4	Paragon	buy to let mortgage provider	10,281	1.73
8	6	Informa	business to business information	10,200	1.71
9	10	WS Atkins	engineering consultancy	10,144	1.70
10	9	Victrex	speciality chemicals	9,668	1.62
				128,176	**21.51**

Analysis of the Portfolio by Sector at 31 May



Sources: Factset, Henderson

Strategic Report: Fund Manager's Report

The Fund Manager of the portfolio, Neil Hermon, reports on the year to 31 May 2016

Market – year in review

The year under review was a poor one for equity markets. This was due to anaemic global economic growth despite supportive monetary policies from developed world central banks. Other problems included the slowing pace of Chinese economic growth, the collapse in oil and other commodity prices, the uncertainty provided by the EU referendum and the timing and pace of interest rate rises in the US. The fundamentals of the corporate sector remained robust. Companies continued to grow their dividends whilst balance sheets remained strong. Corporate earnings growth, though, was subdued as top line growth was hard to generate, profits in the commodity sector collapsed and the strength of sterling diluted the value of overseas earnings for UK companies.

Smaller companies outperformed larger companies over the year. The Numis Smaller Companies Index (excluding investment companies) has now outperformed the FTSE All-Share Index for the last eight years consecutively (and in 16 of the last 17 years).

Fund Performance

The Company had a reasonable year in performance terms – outperforming its benchmark but falling marginally in absolute terms. The net asset value fell 1.1%, on a total return basis. This compared to a decline of 1.6% (total return) from the Numis Smaller Companies Index (excluding investment companies). The outperformance came from a combination of underlying positive portfolio performance and a negative contribution from gearing in the Company, which can be seen in the attribution analysis on page 8. We have now outperformed the Numis Smaller Companies Index (excluding investment companies), in 12 of the past 13 years.

Gearing

Gearing started the year at 7.5% and ended it at 9.1%. In the year the company redeemed the £20 million 10.5% 2016 debenture and replaced it with a £30m 20-year unsecured loan notes at an interest rate of 3.33%. This facility was provided by MetLife, one of the largest life insurance companies in the world. The replacement of the debenture with the new loan notes will save the Company a significant amount annually in interest while providing committed long term debt at a low interest rate. The remainder of the Company's debt is provided by short term bank borrowings. Gearing was a negative contributor to performance in the year as markets fell but has been a significant positive over the 13 years I have managed the investment portfolio.

Attribution Analysis

The tables below and overleaf show the top five contributors to, and the bottom five detractors from, the Company's relative performance.

Principal contributors

	12 month return %	Relative contribution %
NMC Health	+52.1	+0.9
Bellway	+20.4	+0.8
Paysafe	+46.8	+0.6
Informa	+20.8	+0.5
Sanne	+60.7	+0.5

NMC is a Middle Eastern based healthcare operation. Its main facilities are in the United Arab Emirates, particularly Dubai and Abu Dhabi. NMC has grown strongly since its IPO in 2012 through the building of new facilities and acquisitions. This growth is set to continue, particularly given the positive structural opportunities in the UAE, driven by an under provision of state provided healthcare, the continued roll-out of mandatory health insurance and positive demographics. Even after a strong share price performance in the last year the shares still look good value compared to the international peer group, especially considering the strong earnings growth forecast.

Bellway is a national UK housebuilder. The UK housing market has seen an impressive recovery in the recent past aided by improving consumer confidence, low interest rates and Government initiatives, particularly Help to Buy. Margins, volumes and profits have been rising strongly. Bellway is looking to exploit these conditions by expanding its national footprint, whilst maintaining a strong land-bank and balance sheet. The outlook for the sector is aided by a benign land market as the number of competitors has reduced from the previous cycle, the structural under-supply of housing in the UK and the capital discipline Bellway and its peers are displaying.

Paysafe is a provider of online and mobile payment solutions. The company offers the full spectrum of online payment services including; payment processing, digital wallets, pre-paid card, white label technology and value added services such as risk management and consulting. An investment in Paysafe provides exposure to the positive trends in growth in e-commerce and online gaming. This year a transformational and highly synergistic acquisition of competitor Skrill added scale and product to Paysafe's existing business which was taken well by the market. Strong share price performance can also be credited to a further professionalisation of the business, with a new CFO spearheading the company's successful transition from the AIM market to a main listing. Looking ahead, buoyant end market exposures should provide for strong revenue growth and forecast momentum has been on their side. This in conjunction with further consolidation in the industry continues to make it an attractive investment.

Strategic Report: Fund Manager's Report (continued)

Informa is a leading business-to-business information group. Its activities include the provision of academic journals, books, data services, trade exhibitions and conferences. The company produced a very resilient profit performance during the downturn, helped by aggressive cost cutting. Also the balance sheet has been strengthened and cash generation has been strong. A new CEO has been appointed and he has significantly strengthened the management team. The aim is to re-invest in the areas that have struggled to deliver growth whilst expanding the fast growing exhibitions division by acquisition. The last year has seen positive momentum displayed in most parts of the business and over delivery against targets. This has led to a re-rating of the company which we feel has potential to continue.

Sanne is an independent and regulated provider of outsourced specialist corporate and fund administration and reporting services to alternative asset managers, financial institutions and other organisations. The specialism and complexity involved in the service it provides has historically allowed it to earn high margins which we view as sustainable in the medium run. Our investment in Sanne provides exposure to growing regulation in financial services, growth in alternative investments as an asset class, and continued trend of outsourcing back office functions. The company also benefits from a strong balance sheet, a sticky and diversified client base (90% of revenues are recurring) and plenty of M&A opportunities as larger administrators sell off non-core assets.

Principal detractors

	12 month return %	Relative contribution %
Interserve	-43.3	-0.7
Victrex	-28.8	-0.6
e2v Technologies	-19.1	-0.5
JD Sports[1]	+61.2	-0.5
Spectris	-26.1	-0.4

[1]Included in the benchmark index up to 31/12/15 but not owned by the Company (returns shown are those to 31/12/15)

Interserve is an international construction and support services group. Its major operations are focused in the UK and the Middle East. Interserve has been hit by a variety of problems in the last year. In support services the imposition of the minimum wage is hitting profits. The market has also become concerned by the exposure to the oil-revenue-dependent economies of the Middle East. In addition Interserve has announced substantial losses on three waste-to-energy construction contracts in the UK. These factors, combined with a leveraged balance sheet, have led to a severe fall in the share price. The shares now look very cheap and with the company exploring the potential sale of its equipment services division (which would remove concerns over the balance sheet and Middle East exposure) there is a strong potential for a sharp recovery in valuation.

Victrex is a manufacturer of a speciality thermoplastic PEEK. It is the world leader in its field with a dominant market share. Victrex has shown consistent long-term growth as demand for PEEK has grown as customers look to replace metals with lighter plastics with similar thermal properties. Although demand for PEEK is subject to the vagaries of the economic cycle, longer term its use will continue to increase. Additionally Victrex has developed a very successful medical business with PEEK used particularly in spinal and arthroscopy operations, which is growing independent of the economic cycle. The shares have performed poorly in the last year as its exposure to oil and gas and smartphone markets have proved to be a drag on volumes. An additional drag has been the strength of Sterling as Victrex is a major exporter. Victrex has recently expanded capacity as there are significant opportunities for growth in the medical, oil and gas, aerospace and smartphone markets and longer term we believe the company will return to its growth path.

e2v Technologies manufactures high technology electronic components. Although e2v is a company with significant technology and high margins, it has historically struggled to deliver consistent growth. This led to an undervaluation of the business. The appointment of a new chairman and CEO has led to a re-focusing of the business with cost taken out, a new customer-focused approach and de-cluttering of the organisation's processes. The initial results of this new approach were highly encouraging and the shares enjoyed a significant re-rating. In the past year the company has continued to deliver operationally but the shares have fallen back on profit-taking and a de-rating of the industrial sector.

JD Sports is a UK retailer of sports and leisure wear. The company has delivered very strong growth in profitability driven by like for like sales growth and a store opening programme. The company has also benefited from strong support from its brand suppliers, its product being considered fashionable and a weak competitive offering. The Company has no holding in JD Sports.

Spectris manufactures, designs and markets products for the electronic control and process instrumentation sectors. The company has a number of subsidiaries which tend to be market leaders in global market niches. Cash generation is sound, the management team is well respected and the balance sheet is strong. However recent growth in profits has been muted due to softness in end markets and sterling strength. The industrial sector has also de-rated as global growth in industrial production has disappointed. Longer term the company is well positioned for growth, especially if it deploys its balance sheet on acquisitions.

Portfolio Activity

Trading activity in the portfolio was consistent with an average holding period of four years. Turnover was slightly higher than our typical average due to the high level of M&A and IPO activity in the portfolio and does not represent a shift in our approach, which is to consider our investments as long-term in nature and to avoid unnecessary turnover. The focus has been on adding stocks to the portfolio that have good growth prospects, sound financial characteristics and strong management, at a valuation level that does not reflect these strengths. Likewise we have been employing strong sell disciplines to cut out stocks that fail to meet these criteria.

Strategic Report: Fund Manager's Report (continued)

In the year we have added a number of new positions to our portfolio. These included:-

Accesso provides leading edge queue management, point of sale and guest management and ticketing technology to over 1,000 attractions and venues across 25 countries. These include; theme parks, water parks, cultural attractions, live performance venues, sporting events and ski and snow parks. Customers include leading names in the leisure industry such as Merlin Entertainment, Universal Parks, Six Flags and Cedar Fair. The company's strategy is to become the premier technology partner within the leisure and entertainment market by providing innovative and secure e-commerce solutions that help deliver great guest experiences. Accesso is a platform business with the ability to show high operating leverage. The revenue model is designed to be disruptive (undercutting traditional ticket distributors) and the company's IP is patent protected. We believe this strong combination makes for an attractive investment case.

Charles Taylor is a specialist provider of services to the insurance industry. This includes the management of mutual insurance associations, loss adjusting and specialist support services. A new management team have substantially improved the business, rationalising operations and improving profitability. The company has also raised fresh capital giving it flexibility to make acquisitions. The valuation of the company appears low especially considering the cyclically depressed profitability of its loss adjusting business and Charles Taylor offers dependable growth with low sensitivity to global economic growth.

Gamma Communications supplies voice, data and mobile telephony products and services in the UK. The company has grown impressively, driven by a lack of legacy and declining services but also by providing excellent customer service to its core SME customer base. This is a competitive advantage against slow-moving incumbent providers. The company has had a history of exceeding expectations due to strong growth in cloud PBX and SIP trunk volumes. Future opportunities look bright, especially as Gamma is expanding its product range by launching a new mobile service.

Melrose is a diversified engineering group whose raison d'etre is to buy underperforming businesses, improve them and then sell the assets on. Essentially it is deploying a private equity model in the public markets. The company has had significant success in the past with its acquisitions of McKechnie, FKI and most recently Elster. We have owned Melrose in the past but sold it due to size considerations. However post a capital return to shareholders after the sale of Elster to Honeywell the market capitalisation has returned into our range and has given us the opportunity to re-invest in a management team who have a demonstrable track record of making money for shareholders.

RPC is a manufacturer of products principally for the plastic packaging industry. It is a broad based group operating principally in mainland Europe and the UK. Through scale efficiencies and natural consolidation in customer's supply chains RPC is growing turnover organically by low single digits. However this is being supplemented by acquisition activity as RPC looks to consolidate what is a fragmented industry. This is driving significant synergy benefits in raw material purchasing and site consolidation. The highly ambitious management team have established a strong track record in value creation and we expect them to grow RPC significantly in future years.

Scapa is a manufacturer of technical tapes, adhesive films and compounds. The company has achieved a remarkable resurgence since a new management team was appointed in 2009. Margins have improved dramatically, the balance sheet has been transformed and inherited asbestos liabilities have been dealt with. The company has bright prospects driven by further margin improvements, through factory rationalisation, in its industrial division but more importantly strong organic growth in its healthcare division, where it is becoming a trusted preferred supplier to the major medical device companies. The company also has the ability to supplement this organic growth through selected acquisitions, focused on the healthcare market.

In addition to the companies mentioned above, we invested in a number of IPOs (initial public offerings) in the year. These included **Countryside Properties**, a UK housebuilder; **Gym Group**, the low cost gym chain; **Ibstock**, the leading UK brick manufacturer; **Joules**, a fashion retailer; **Midwich**, a leading European distributor of AV equipment; **Motorpoint**, a second hand automotive retailer; and **Softcat**, an IT re-seller for the small and medium sized business community.

To balance the additions to our portfolio, we have disposed of positions in companies which we felt were set for poor price performance. We disposed of our holding in **Restaurant Group**, the restaurant and pub operator, where the company has suffered from increased competition, a weakening brand profile and poor operational delivery. We also disposed of our holding in **Elementis**, the speciality chemicals company, where growth has been disappointing due to weak oil and gas markets, slow Asian markets and increased competition in its chromium business. Other companies we sold due to a belief that they were structurally challenged or suffering from poor operational performance included **Fenner**, the conveyor belt and seals business; **Countrywide**, the UK estate agent; **Speedy Hire**, the plant hire company; **Thomas Cook**, the travel agency; and **Ultra Electronics**, the defence electronics business.

We benefited from a level of takeover activity in the year. Five portfolio companies received agreed bids. The clear similarity in these bids was the nature of the buyers, with the bidders being either foreign corporates or private equity groups. This reflects the open nature of the UK market, the strength of global corporate balance sheets and the low cost of debt. Within our portfolio, takeover bids were received for **Anite**, a telecoms testing business, from Keysight Technologies; **Chime Communications**, a marketing services group, from private equity; **Hellermann Tyton**, a cable management solutions provider, from Delphi Automotive; **ISG**, a fit-out and construction group, from Cathexis Capital; and **Quintain Estates**, a property developer, from Lone Star.

Strategic Report: Fund Manager's Report (continued)

Portfolio Outlook

The following table shows the Company's key stock positions versus the Numis Smaller Companies Index (excluding investment companies) at the end of May 2016.

Top ten active positions at 31 May 2016	Holding %	Index Weight %	Active Weight %
Bellway	3.6	–	3.6
NMC Health	2.8	–	2.8
Intermediate Capital	2.2	–	2.2
e2v Technologies	2.4	0.3	2.1
Howden Joinery	2.0	–	2.0
Playtech	1.8	–	1.8
Informa	1.7	–	1.7
WS Atkins	1.7	–	1.7
Victrex	1.6	–	1.6
Clinigen	1.6	–	1.6

A brief description of the largest active positions (excluding Bellway, e2v Technologies, Informa, NMC Health and Victrex which are covered earlier) follows:

Intermediate Capital is an alternative finance provider and asset manager. It is a leading provider of mezzanine finance to LBO markets. It also owns a highly successful mezzanine, property lending and credit fund management operation. Its portfolio of investments are performing well but the primary growth engine of the business is the fund management operation where it is having real success in growing assets due to the strength of its performance, the quality of the team and underlying demand for its product in an income-hungry world. The management are also targeting an increase in the company's return on equity by returning substantial surplus capital.

Howden Joinery is a manufacturer and retailer of kitchens in the UK. From launch in 1990 it has grown organically to over 600 branches and taken a significant market share by providing a first-class service to its client, the jobbing builder, with keen prices and excellent stock availability. The company is also very cash generative but in the past this cash has been consumed by pension and property liabilities inherited from its former parent, MFI. However these problems have now been effectively worked through and Howden is starting to raise the dividend aggressively. With branch roll-out continuing and the kitchen market beginning to recover, Howden is well placed to grow profitability.

Playtech is one of the world's largest gaming and sports betting software suppliers. The company provides white-label software for online and mobile; casino, poker, bingo, sports betting and live dealer games; and has most recently made acquisitions in the spread-betting market. Playtech benefits from operating in an industry with high barriers to entry and strong supplier power (platform migrations are very risky for online B2C businesses). This together with long-term contracts (five to seven years and increasing) and relatively low levels of competition makes the company well placed to benefit from global growth in online gaming. We expect returns from Playtech to be driven by continued strong earnings momentum and a growing dividend. However, we believe the greatest returns should be made from a market re-rating; driven primarily by an increase in the proportion of regulated earnings and more credit given for its high, sustainable and cash-backed margins.

WS Atkins is an international engineering consultant, with operations principally in the UK, USA, Middle East and Asia. A new management team has been re-structuring the company with low-margin activities sold and operations rationalised. With this restructuring mostly completed, the company is starting to see growth in profitability and future prospects look strong. The company also enjoys a cash-rich balance sheet and is looking to deploy this on acquisitions that will augment organic growth. The company announced the acquisition of a large nuclear engineering consultancy firm, PP&T, in 2015.

Clinigen is a global speciality pharmaceutical services business. Its core competencies are providing comparator drugs and other services for clinical trials and providing market access for drugs that are difficult to obtain or yet to be licensed. It also has a speciality pharmaceutical division which looks to acquire niche drugs from major pharmaceutical companies, which it thinks can perform better with additional regulatory approval or increased targeted marketing. The company has seen strong growth since its IPO in 2012 and this is likely to continue given the strength of the management team and the positive structural growth of its end markets.

Market Outlook

The surprise EU referendum result precipitated a sharp negative shock to markets around the globe. We have witnessed a seismic moment in UK political, social and economic history. The repercussions of the referendum will, however, only become clear over the coming years. For the moment, it is impossible to estimate the long-term political impacts for the UK and it is also very difficult to predict the future economic impact.

On the political front, the Prime Minister has been replaced, the Leader of the Opposition is facing a leadership challenge, and the SNP is already talking about a second Scottish independence referendum. More broadly in Europe, the very future of the EU may be at stake. Meanwhile, we have no idea yet what shape Brexit will take and what will be the outcome of trade negotiations with the EU and the rest of the world.

In the weeks since the referendum, we have seen a sharp decline in the value of the pound. The FTSE 100 has been resilient, but that reflects the international nature of large UK corporates and the extent of their international earnings. The more domestically focused small and mid-cap indices have been harder hit. The general consensus is that the UK economy is set for a period of slowdown, if not recession.

In the corporate sector, conditions are intrinsically stronger than they were during the financial crisis of 2008-9. Balance sheets are robust and dividends are well supported. Although corporate profitability may come under pressure, companies are better placed to deal with the fall-out from an economic slowdown. In addition a large proportion of UK corporate earnings comes from overseas, even among smaller companies, and will be boosted by the de-valuation of sterling.

Strategic Report: Fund Manager's Report (continued)

In conclusion, the year under review has been a reasonable one for the Company. Relative performance was satisfactory and our portfolio companies have, overall, performed robustly. Our investments are generally trading well, soundly financed and attractively valued. Additionally, the smaller company market continues to throw up exciting growth opportunities in which the Company can invest. The short term is set to be very uncertain but we are confident that over the medium to longer term we can generate significant value from a consistent and disciplined investment approach.

Neil Hermon
Fund Manager

Investment Portfolio at 31 May 2016

Company	Principal activities	Valuation £'000	Portfolio %
Bellway	*housebuilder*	**21,181**	**3.55**
NMC Health	*healthcare provider*	**16,963**	**2.85**
e2v Technologies	*electronic components*	**14,418**	**2.42**
Intermediate Capital	*mezzanine finance*	**12,849**	**2.16**
Howden Joinery	*kitchen manufacturer and retailer*	**11,915**	**2.00**
Playtech	*internet gaming software*	**10,557**	**1.77**
Paragon	*buy to let mortgage provider*	**10,281**	**1.73**
Informa	*business to business information*	**10,200**	**1.71**
WS Atkins	*engineering consultancy*	**10,144**	**1.70**
Victrex	*speciality chemicals*	**9,668**	**1.62**
10 largest		**128,176**	**21.51**
Clinigen[1]	*pharmaceuticals*	9,435	1.58
RPC	*plastic packaging manufacturer*	9,183	1.54
Paysafe	*online payment processor*	9,064	1.52
NCC	*IT security*	8,950	1.50
Balfour Beatty	*international contractor*	8,673	1.46
Renishaw	*precision measuring and calibration equipment*	8,380	1.41
Sanne	*investment management services*	8,081	1.36
John Laing	*infrastructure investment*	8,069	1.35
Grainger	*residential property investor*	7,988	1.34
Interserve	*international contractor*	7,937	1.33
20 largest		**213,936**	**35.90**
Capital & Regional	*retail property investor*	7,705	1.29
Laird	*electronic products*	7,695	1.29
Essentra	*speciality plastic producer and distribution*	7,636	1.28
Northgate	*commercial vehicle hire*	7,592	1.28
AA	*roadside assistance*	7,488	1.26
Esure	*motor and property insurer*	6,696	1.12
Ibstock	*bricks manufacturer*	6,634	1.11
OneSavings Bank	*banks*	6,632	1.11
Spectris	*electronic control and process instrumentation*	6,544	1.10
Synthomer	*speciality chemicals*	6,532	1.10
30 largest		**285,090**	**47.84**
Aveva Group	*design software*	6,456	1.08
Dechra Pharmaceuticals	*veterinary pharmaceuticals*	6,382	1.07
Ted Baker	*clothing retailer*	6,334	1.06
St Modwen Properties	*real estate investment and services*	6,204	1.04
Scapa[1]	*technical tapes*	6,172	1.04
Consort Medical	*healthcare products*	6,102	1.03
Senior	*aerospace and automotive products*	5,981	1.00
Aldermore	*banks*	5,940	1.00
Cineworld	*cinema operator*	5,917	0.99
Crest Nicholson	*housebuilder*	5,882	0.99
40 largest		**346,460**	**58.14**
Jupiter Fund Management	*investment management company*	5,749	0.97
Countryside	*housebuilder*	5,683	0.95
Oxford Instruments	*advanced instrumentation equipment*	5,470	0.92
DFS	*furniture retailer*	5,430	0.91
LSL Property Services	*real estate services*	5,325	0.89
Euromoney Institutional Investor	*business to business information*	5,319	0.89
Eurocell	*building products*	5,280	0.89
RWS[1]	*patent translation services*	5,060	0.85
Tarsus Group	*exhibition organiser*	5,012	0.84
Cairn Energy	*oil & gas exploration and production*	4,824	0.81
50 largest		**399,612**	**67.06**
Servelec	*healthcare software provider*	4,813	0.81
Gamma Communications[1]	*telecommunication services*	4,647	0.78
SSP	*contract catering*	4,548	0.76
GVC	*online gaming operator*	4,515	0.76
Dunelm	*homewares retailer*	4,486	0.75
Brown (N) Group	*clothing retailer*	4,482	0.75
WYG[1]	*engineering consultancy*	4,389	0.74

Investment Portfolio at 31 May 2016 (continued)

Company	Principal activities	Valuation £'000	Portfolio %
Tyman	*building products*	4,372	0.73
Firstgroup	*bus and rail operator*	4,324	0.73
EMIS[1]	*healthcare IT services*	4,301	0.72
60 largest		**444,489**	**74.59**
Hunting	*oil equipment and services*	4,182	0.70
Rotork	*process control solutions*	4,180	0.70
Vectura	*respiratory pharmaceuticals*	4,110	0.69
Exova	*material testing*	4,061	0.68
Keller	*ground engineering services*	3,959	0.67
Safestyle[1]	*window replacement retailer*	3,957	0.66
CLS	*real estate investment and services*	3,947	0.66
Lookers	*automotive retailer*	3,929	0.66
ITE Group	*exhibition organiser*	3,871	0.65
Brewin Dolphin	*wealth manager*	3,870	0.65
70 largest		**484,555**	**81.31**
Sherborne Investors	*speciality finance*	3,859	0.65
Safestore Holdings	*self storage operator*	3,843	0.65
Melrose Industries	*engineering group*	3,843	0.64
Unite Group	*student accommodation investor*	3,775	0.64
Polypipe	*building products*	3,660	0.61
Volution	*building products*	3,645	0.61
Xaar	*electronic equipment*	3,638	0.61
Conviviality[1]	*beverage wholesaler*	3,585	0.60
GB Group[1]	*data intelligence services*	3,450	0.58
Urban & Civic	*real estate investment and services*	3,401	0.57
80 largest		**521,254**	**87.47**
Ascential	*exhibition organiser and data services*	3,322	0.56
Softcat	*software reseller*	3,185	0.53
Premier Oil	*oil & gas exploration and production*	3,179	0.53
Midwich[1]	*AV equipment distributor*	3,084	0.52
Costain	*contractor*	3,083	0.52
Gym Group	*gym operator*	2,899	0.49
Dairy Crest	*food manufacturer and distributor*	2,890	0.48
Marshall Motor[1]	*automotive retailer*	2,872	0.48
Charles Taylor	*insurance management services*	2,787	0.47
Tribal Group[1]	*education support services & software*	2,728	0.46
90 largest		**551,283**	**92.51**
Restore[1]	*office service provider*	2,691	0.45
SQS Software[1]	*software testing*	2,679	0.45
Joules[1]	*clothing retailer*	2,678	0.45
Digital Barriers[1]	*digital security*	2,668	0.44
SDL	*language software service provider*	2,548	0.43
Next Fifteen Communications[1]	*PR and media services*	2,546	0.43
Motorpoint	*motor retailer*	2,379	0.40
Carpetright	*carpet retailer*	2,317	0.39
Quantum Pharma[1]	*speciality pharmaceuticals*	2,312	0.39
Koovs[1]	*online fashion retailer*	2,299	0.38
100 largest		**576,400**	**96.72**
Abcam[1]	*internet retailer of antibodies*	2,242	0.38
Accesso[1]	*leisure software provider*	2,161	0.36
SCS	*furniture retailer*	2,057	0.35
Imagination Technologies	*semi conductor intellectual property licensing*	2,011	0.34
Blancco Technology[1]	*data erasure software*	1,980	0.33
Faroe Petroleum[1]	*oil & gas exploration and production*	1,944	0.33
Ebiquity[1]	*media agency*	1,860	0.31
Equiniti	*financial services outsourcer*	1,815	0.30
Severfield	*industrial engineering*	1,741	0.29
RM	*education software and services*	1,716	0.29
Total equity investments		**595,927**	**100.00**

There were no convertible or fixed interest securities at 31 May 2016 (2015: None)

1 quoted on the Alternative Investment Market

Strategic Report: Corporate Information

Directors

The Directors appointed to the Board at the date of this report are:

Jamie Cayzer-Colvin

Position: Chairman of the Board
Date of appointment: 13 May 2011 (Chairman in September 2011)
Jamie is an executive Director of Caledonia Investments plc and among other appointments, he is a Director of Polar Capital Holdings plc, Chairs the Royal Horticultural Society pension scheme, and is a trustee of the Heritage of London Trust, plus a number of unquoted companies and charities. Previously, Jamie served as a non executive director on the boards of Close Brothers plc and Rathbone Brothers plc.

Keith Percy

Position: Director (Senior Independent Director)
Date of appointment: 21 July 2006
Keith is a Director of JPMorgan Japanese Investment Trust plc and Standard Life Equity Income Trust plc. He was previously Chairman of Brunner Investment Trust plc.

David Lamb

Position: Director
Date of appointment: 1 August 2013
David is Managing Director of St James's Place plc. He is a Chairman of the Investment Committee and a Trustee of the St. James's Place Foundation. David is also a Governor of the University of the West of England.

Mary Ann Sieghart

Position: Director
Date of appointment: 18 July 2008
Mary Ann is a non-executive Director of The Merchants Trust plc, DLN Digital Limited and the Content Board of Ofcom. She chairs the Social Market Foundation, sits on the council of Tate Modern and the advisory council of Into University, and is a trustee of the Kennedy Memorial Trust. She presents occasional programmes on Radio 4. She was Assistant Editor of The Times from 1998 to 2007 and is also a former City Editor and Lex Columnist.

Beatrice Hollond

Position: Director and Chairman of the Audit Committee
Date of appointment: 23 July 2010 (Audit Committee Chairman in September 2010)
Beatrice is Deputy Chairman of Millbank Financial Services Limited, an independent family office, and Chairman of Millbank Investment Managers Limited, its investment management subsidiary. She is Chairman of Keystone Investment Trust plc and a Director of Templeton Emerging Markets Investment Trust PLC, M&G Group Limited and on the Board of Brown Advisory. Among other appointments she is a Trustee of the Esmée Fairbairn Foundation and an Advisory Fellow of Pembroke College, Oxford and chairs the Investment Committee of its Endowment Fund.

All the Directors are independent and all are members of the Management Engagement Committee and the Nomination Committee, both are chaired by Jamie Cayzer-Colvin.

Beatrice Hollond chairs the Audit Committee, the other members of which are Keith Percy, Mary Ann Sieghart and David Lamb.

Strategic Report: Corporate Information (continued)

Registered Office

201 Bishopsgate
London EC2M 3AE

Service Providers

Alternative Investment Fund Manager

Henderson Investment Funds Limited
201 Bishopsgate
London EC2M 3AE

Corporate Secretary

Henderson Secretarial Services Limited
201 Bishopsgate
London EC2M 3AE
Telephone: 020 7818 1818
Email: trusts@henderson.com

Registrar

Computershare Investor Services PLC
The Pavilions
Bridgwater Road
Bristol BS99 6ZZ
Telephone: 0370 707 1057

Depositary and Custodian

HSBC Bank plc
8 Canada Square
London E14 5HQ

Broker

Numis Securities
The London Stock Exchange Building
10 Paternoster Square
London EC4M 7LT

Independent Auditors

Chartered Accountants and Statutory Auditors

PricewaterhouseCoopers LLP
7 More London Riverside
London SE1 2RT

Financial Calendar

Annual results	August 2016
Ex-dividend date	1 September 2016
Dividend record date	2 September 2016
Annual General Meeting[1]	23 September 2016
Final dividend payable	30 September 2016
Half year results	January 2017
Interim dividend payable	March 2017

Information Sources

For more information about the Company, visit the website at
www.hendersonsmallercompanies.com

HGi

HGi is a content platform provided by Henderson that offers online personalisation where you can "follow" investment experts, topics and the trusts that are of interest to you. By creating your HGi profile you will be updated regularly on the topics that interest you most, bringing you closer to Henderson's investment expertise.

Scan the QR code or use this short URL to register for HGi: http://HGi.co/rb

Follow Henderson Investment Trusts on Twitter, YouTube and Facebook

Investing

Shares can be purchased in the market via a stockbroker or through share dealing platforms. They can also be held through share plans, ISAs or pensions and links to various providers are included on the website. Individuals holding shares through Halifax Share Dealing Limited can write to them at Lovell Park Road, Leeds LS1 1NS or contact them via telephone 03457 22 55 25, email **Henderson@halifax.co.uk** or visit their website **www.halifax.co.uk/sharedealing**.

Potential investors are reminded that the value of investments and the income from them may go down as well as up and investors may not receive back the full amount invested. Tax benefits may vary as a result of statutory changes and their value will depend on individual circumstances.

Nominee Share Code

Where notification has been provided in advance, the Company will arrange for copies of shareholder communications to be provided to the operators of nominee accounts. Nominee investors may attend General Meetings and speak at them when invited to do so by the Chairman. Investors via Halifax Share Dealing receive all shareholder communications and a voting instruction form is provided to facilitate voting at General Meetings of the Company.

1 At the Company's Registered Office at 11.30am

Strategic Report: Corporate Information (continued)

Status

The Company is an investment company as defined in Section 833 of the Companies Act 2006 (the "Companies Act") and operates as an investment trust in accordance with Section 1158 of the Corporation Tax Act 2010 ("Section 1158"), is subject to the Listing Rules of the Financial Conduct Authority and is governed by its Articles of Association, amendments to which must be approved by shareholders by way of a special resolution. The Company is not a close company.

The Company has obtained approval from HMRC of its status as an investment trust under Section 1158; the Directors are of the opinion that the Company has conducted its affairs in compliance with Section 1158 since approval was granted and intends to continue to do so. The Company is liable to corporation tax on its net revenue profits but is exempt from corporation tax on capital gains if it has complied at all times with Section 1158.

Principal Risks and Uncertainties

The Board, with the assistance of Henderson, has carried out a robust assessment of the principal risks facing the Company which relate to the activity of investing in the shares of smaller companies that are listed (or quoted) in the United Kingdom. In carrying out this assessment, the Board has considered the market uncertainty arising from the result of the UK referendum to leave the European Union. Although the Company invests almost entirely in securities that are quoted on recognised markets, share prices may move rapidly and it may not be possible to realise an investment at Henderson's assessment of its value. The companies in which investments are made may operate unsuccessfully, or fail entirely, such that shareholder value is lost. The Company is also exposed to the operational risk that one or more of its suppliers may not provide the required level of service. The Board considers regularly the principal risks facing the Company in order to mitigate them as far as practicable. A fuller description of the principal risks and uncertainties follows. With the assistance of Henderson, the Board has drawn up a risk matrix which identifies the key risks to the Company. The Board policy on risk management has not materially changed from last year. The principal risks fall broadly under the following categories:

Investment activity and strategy

An inappropriate investment strategy (for example, in terms of asset allocation or the level of gearing) may lead to underperformance against the Company's benchmark and the companies in its peer group; it may also result in the Company's shares trading at a wider discount to the net asset value per share. The Board manages these risks by ensuring a diversification of investments and a regular review of the extent of borrowings. Henderson operates in accordance with investment limits and restrictions determined by the Board; these include limits on the extent to which borrowings may be used. The Board reviews its investment limits and restrictions regularly and Henderson confirms its compliance with them each month. Henderson provides the Directors with management information, including performance data and reports and shareholder analysis. The Board monitors the implementation and results of the investment process with the Fund Manager, who attends all Board meetings, and reviews regularly data that monitors risk factors in respect of the portfolio. The Board reviews investment strategy at each Board meeting.

Accounting, legal and regulatory

In order to qualify as an investment trust the Company must comply with Section 1158 of the Corporation Tax Act 2010. A breach of Section 1158 could result in the Company losing investment trust status and, as a consequence, capital gains realised within the Company's portfolio would be subject to corporation tax. The Section 1158 criteria are monitored by Henderson and the results are reported to the Directors at each Board meeting. The Company must comply with the provisions of the Companies Act 2006 and, as the Company's shares are listed for trading on the London Stock Exchange, the Company must comply with the UK Listing Authority's Listing Rules and Disclosure Guidance and Transparency Rules and the Prospectus Rules ("UKLA Rules").

A breach of the Companies Act could result in the Company and/or the Directors being fined or becoming the subject of criminal proceedings. Breach of the UKLA Rules could result in the suspension of the Company's shares which would in turn lead to a breach of Section 1158. The Board relies on its Company Secretary and its professional advisers to ensure compliance with the Companies Act and UKLA Rules.

Operational

Disruption to, or failure of, Henderson's accounting, dealing or payment systems or the Custodian's records could prevent the accurate reporting and monitoring of the Company's financial position. Henderson has contracted some of its operational functions, principally those relating to trade processing, investment administration and accounting, to BNP Paribas Securities Services. Details of how the Board monitors the services provided by Henderson and its other suppliers, and the key elements designed to provide effective internal control, are explained further in the internal control section of the Corporate Governance Statement on page 31.

Financial instruments and the management of risk

By its nature as an investment trust, the Company is exposed in varying degrees to market risk (comprising market price risk, currency risk and interest rate risk), liquidity risk and credit and counterparty risk. An analysis of these financial risks and the Company's policies for managing them are set out in note 15 on pages 53 to 56.

Borrowing

The Company has access to borrowings of up to £70 million (2015: £60 million), £30 million of unsecured loan notes, which funded on 23 May 2016, and a committed bank facility with National Australia Bank for £40 million. In addition the Company has a small amount of Preference Stock in issue (see page 52 for more details). The Company's £20 million debenture stock was redeemed on 31 May 2016.

Viability Statement

The Company is a long term investor; the Board believe it is appropriate to assess the Company's viability over a three year period in recognition of our long term horizon and what we believe to be

Strategic Report: Corporate Information (continued)

investors' horizons, taking account of the Company's current position and the potential impact of the principal risks and uncertainties as documented above in this Strategic Report.

The assessment has considered the impact of the likelihood of the principal risks and uncertainties facing the Company, in particular investment strategy and performance against benchmark, whether from asset allocation or the level of gearing, and market risk, in severe but plausible scenarios, and the effectiveness of any mitigating controls in place.

The Board took into account the liquidity of the portfolio and the borrowings in place when considering the viability of the Company over the next three years and its ability to meet liabilities as they fall due. This included consideration of the duration of the Company's loan and borrowing facilities and how a breach of any covenants could impact on the Company's net asset value and share price.

The Board do not expect there to be any significant change in the current principal risks and adequacy of the mitigating controls in place. Also the Directors do not envisage any change in strategy or objectives or any events that would prevent the Company from continuing to operate over that period as the Company's assets are liquid, its commitments are limited and the Company intends to continue to operate as an investment trust. Only a substantial financial crisis affecting the global economy could have an impact on this assessment. Whilst there is currently uncertainty in the markets following the UK referendum result to leave the European Union, the Board does not believe that this will have a long term impact on the viability of the Company and its ability to continue in operation.

The Board recognise that there is a continuation vote that is due to take place at the 2016 Annual General Meeting. The Directors support the continuation of the Company and expect that the Company will continue to exist for the foreseeable future, at least for the period of assessment. However, if such a vote were not passed, the Directors would follow the necessary provisions relating to the winding up of the Company and the realisation of its assets.

Based on this assessment, the Board have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the next three year period.

Future Developments

The future success of the Company is dependent primarily on the performance of its investments, which will to a significant degree reflect the performance of the stock market and Henderson. Although the Company invests in companies that are listed or quoted in the United Kingdom, the underlying businesses of those companies are affected by various economic factors, many of an international nature. The Board's intention is that the Company will continue to pursue its investment objective in accordance with its investment policy. Further comment on the outlook for the Company is given in the Chairman's Statement and in the Fund Manager's Review.

Key Performance Indicators ("KPIs")

In order to measure the success of the Company in meeting its objective and to evaluate the performance of Henderson, the Directors take into account the following KPIs. The charts and tables on pages 2, 3 and 7 show how the Company has performed against these KPIs:

Performance measured against the benchmark

The Board reviews, at each of its meetings, the performance of the portfolio, the net asset value per share ("NAV") and the share price and compares them with the performance of the Company's benchmark.

Performance measured against the peer group

The Company is included in the AIC's UK Smaller Companies sector, which represents the Company's peer group. In addition to comparison against the benchmark, the Board also considers the performance against the peer group.

Discount to the net asset value per share

The Board monitors the level of the discount to the NAV at which the Company's shares trade and reviews the average discount for the Company's relevant AIC sector (the UK Smaller Companies sector).

The Board considers whether to use share buy-backs to enhance shareholder value. Shares are only bought back at a price below the prevailing NAV, thereby increasing the NAV for the remaining shareholders.

The Company publishes a NAV figure on a daily basis, through the official newswire of the London Stock Exchange. This figure is calculated in accordance with the AIC formula (and since 1 June 2008 includes current financial year revenue items).

Ongoing Charge

The Board regularly reviews the ongoing charge and monitors the expenses incurred by the Company. For the year ended 31 May 2016 the Ongoing Charge was 0.44% both including and excluding performance fee because there was no performance fee payable (2015: 0.46% excluding performance fee and 0.88% including performance fee).

Corporate Responsibility

Responsible Investment

Henderson is responsible for reporting on its work on corporate governance and corporate responsibility (or social, environmental and ethical ("SEE") issues) in the companies in which it invests on its clients' behalf, across all funds as part of its management duties. In May 2005 Henderson became a founding signatory to the United Nations Principles for Responsible Investment. The Principles, developed under the auspices of the UN Secretary-General, are a voluntary and aspirational framework for incorporating environmental, social and corporate governance ("ESG") issues into mainstream investment decision-making and ownership practices. The way companies respond to sustainability and corporate responsibility can

Strategic Report: Corporate Information (continued)

affect their business performance, both directly and indirectly. An investee company's policy on social responsibility and the environment is considered by Henderson's risk team but investments are not ruled out on social and environmental grounds only.

Voting Policy and the UK Stewardship Code

Henderson's responsible investment policy sets out its approach to corporate governance and corporate responsibility for all the companies in which it invests on behalf of its clients and its policy on proxy voting. The policy also sets out how Henderson implements the Stewardship Code. The Company has reviewed the policy and has delegated responsibility for voting to Henderson. The Board receives regular reports on the voting undertaken by Henderson on behalf of the Company. The Board and Henderson believe that voting at General Meetings is an important aspect of corporate stewardship and a means of signalling shareholder views on board policy, practices and performance. Voting recommendations are guided by the best interests of the investee companies' shareholders. Depending on the nature of the resolution the Fund Manager will give specific instructions on voting non-routine and unusual or controversial resolutions. Decisions not to support resolutions and the rationale for doing so are fed back to the investee company prior to voting.

Practical difficulties may prevent Henderson voting in some markets. In particular, various factors, including restrictions on dealing and costs, may inhibit voting in some international markets and must be taken into account.

The Henderson responsible investment policy and further details of Henderson's responsible investment activities can be found on the Henderson website, **www.henderson.com**.

Employees, Social, Community, Human Rights and Environmental Matters

The Company's core activities are undertaken by Henderson, which has implemented environmental management practices, including systems to limit the use of non-renewable resources and to minimise the impact of operations on the environment, and is focused on reducing greenhouse gas emissions and minimising waste, where possible. The Company has therefore not reported on these, or social, community or human rights issues here; Henderson's policies are included in its annual report which can be found on its website.

Henderson's corporate responsibility statement is included on the website detailed above. In 2012 it was granted CarbonNeutral Company status which it has committed to maintain at least until the end of 2018.

The Company's Annual Report is printed on paper produced using 50% recycled post-consumer waste and 50% wood fibre from fully sustainable forests with certification by the Forest Stewardship Council; the printing company used is certified as CarbonNeutral®.

Modern Slavery Act 2015

As an investment vehicle the Company does not provide goods or services in the normal course of business, and does not have customers. Accordingly, the Directors consider that the Company is not required to make any slavery or human trafficking statement under the Modern Slavery Act 2015.

Board Diversity

At the year end, the Board comprised of five Directors, two of whom are female. When Mr Percy steps down at the Annual General Meeting and the election of Victoria Sant to the Board this will increase to 60%. The Directors' appointment to the Board was based on skills and experience. More information on the Board's consideration of diversity is given in the Corporate Governance Statement. The Company has no employees and therefore, there is nothing further to report in respect of gender representation within the Company.

For and on behalf of the Board

Jamie Cayzer-Colvin
Chairman
10 August 2016

Strategic Report: Glossary

Alternative Investment Fund Managers Directive ("AIFMD")

Agreed by the European Parliament and the Council of the European Union and transposed into UK legislation, the AIFMD classifies certain investment vehicles, including investment companies, as Alternative Investment Funds ("AIFs") and requires them to appoint an Alternative Investment Fund Manager ("AIFM") and depositary to manage and oversee the operations of the investment vehicle. The Board of the Company retains responsibility for strategy, operations and compliance and the Directors retain a fiduciary duty to shareholders.

Association of Investment Companies ("AIC")

The Company is a member of the AIC which is the trade body for investment companies and represents the industry in relation to various matters which impact the regulation of such entities.

Benchmark

An index against which performance is compared. For the Company this is the Numis Smaller Companies Index (excluding investment companies).

Custodian

The Custodian is responsible for ensuring the safe custody of the Company's assets and that all transactions in the underlying holdings are transacted in an accurate and timely manner.

Depositary

From 22 July 2014 all AIFs were required to appoint a Depositary which has responsibility for overseeing the operations of the Company including safekeeping, cash monitoring and verification of ownership and valuation of the underlying holdings and is responsible for the appointment of a Custodian. The Depositary is strictly liable for the loss of any investments or other assets in its custody unless it has notified that it is has discharged its liability in certain markets. The Depositary has confirmed that it has not discharged liability in relation to any of the Company's assets.

Derivative

A contract between two or more parties in relation to an underlying security. The value of a derivative will fluctuate in accordance with the value of the security and is a form of gearing as the fluctuations in value are usually greater than the fluctuations in the underlying security's value. Examples of derivatives are put and call options, swap contracts, futures and contracts for difference. Foreign exchange, interest rates and commodities may also be traded using derivative contracts.

Dividend Dates

When declared or recommended, each dividend will have three key dates applied to it. The payment date is the date on which shareholders will receive their dividend, either by BACS transfer or by receipt of a dividend cheque. The record date applied to the dividend is used as a cut-off for the Company's Registrars to know which shareholders should be paid a dividend. Only shareholders on the register of members at the close of business on the record date will receive the dividend. The ex-dividend date is the business day before the record date and is the date upon which the Company's net asset value will be disclosed ex-dividend.

Gearing

Gearing means borrowing money to buy assets with the expectation that the return on investments bought will exceed the interest cost of the borrowings. The gearing percentage reflects the amount of borrowings (e.g. bank loans or overdrafts) the Company has used to invest in the market, and is calculated by taking the difference between total investments and equity shareholders' funds, dividing this by equity shareholders' funds and multiplying by 100. The Company can also use synthetic gearing through derivatives and foreign exchange hedging.

Investment Trusts

Investment trusts are public limited companies, listed on the London Stock Exchange, which provide shareholders with a professionally managed portfolio of investments. Investment trusts are exempt from tax on the capital gains arising on their investments subject to meeting certain criteria. Income, net of expenses and tax, is substantially distributed to shareholders. Investment trusts are also known as investment companies, although the tax legislation retains the reference to investment trusts.

Liquidity

In the context of the liquidity of shares in the stock market, this refers to the availability of buyers in the market for the share in question. Where the market in a particular share is described as liquid, that share will be in demand and holders wishing to sell their shares should find ready buyers. Conversely, where the market in a share is illiquid the difficulty of finding a buyer will tend to depress the price that might be negotiated for a sale.

Market Capitalisation ("Market Cap")

The market value of a company, calculated by multiplying the mid-market price per share by the number of shares in issue.

Strategic Report: Glossary (continued)

Net Asset Value ("NAV") per Ordinary Share

The value of the Company's assets (i.e. investments and cash held) less any liabilities (i.e. bank borrowings and debt securities) for which the Company is responsible, divided by the number of shares in issue. The aggregate NAV is also referred to as shareholders' funds on the balance sheet. The NAV is published daily.

Ongoing Charge

The ongoing charge reflects those expenses of a type which are likely to recur in the foreseeable future, whether charged to capital or revenue, and which relate to the operation of the Company as a collective fund, excluding the costs of acquisition or disposal of investments, financing charges and gains or losses arising on investments. The ongoing charge is based on actual costs incurred in the year as being the best estimate of future costs, excluding any performance fees in accordance with the AIC methodology and is the annualised ongoing charge expressed as a percentage of the average aggregate NAV in the period.

Premium/Discount

The amount by which the market price per share of an investment trust is either higher (premium) or lower (discount) than the NAV per share, expressed as a percentage of the NAV per share.

Revenue Return Per Share

The revenue return per share is the revenue return profit for the year divided by the weighted average number of ordinary shares in issue during the year.

Total Return Performance

This is the return on the share price or NAV taking into account both the rise and fall of share prices and the dividends and interest paid to shareholders. Any dividends received by a shareholder are assumed to have been reinvested in either additional shares (for share price total return) or the Company's assets (for NAV total return).

Yield

The annual dividend expressed as a percentage of the share price.

Corporate Report

Report of the Directors

The Directors present the audited financial statements of the Company and their report for the year from 1 June 2015 to 31 May 2016. The Henderson Smaller Companies Investment Trust plc (the "Company") (registered in England & Wales on 16 December 1887 with company registration number 25526) was active throughout the year under review and was not dormant.

Directors' Remuneration and Shareholdings

The Directors' Remuneration Report on pages 27 and 28 provides information on the remuneration and share interests of the Directors.

Directors' Conflicts of Interest

The Company's Articles of Association permit the Board to consider and, if it sees fit, to authorise situations where a Director has an interest that conflicts, or may possibly conflict, with the interests of the Company ("situational conflicts"). The Board has a formal system in place for Directors to declare situational conflicts to be considered for authorisation by those Directors who have no interest in the matter being considered. In deciding whether to authorise a situational conflict, the non-conflicted Directors must act honestly and in good faith with a view to the best interests of the Company and they may impose limits or conditions when giving the authorisation, or subsequently, if they think this is appropriate. Any situational conflicts considered, and any authorisations given, are recorded in the relevant meetings' minutes and the register of interests. The prescribed procedures have been followed in deciding whether, and on what terms, to authorise situational conflicts and the Board believes that the systems it has in place for reporting and considering situational conflicts continues to operate effectively.

Directors' Insurance and Indemnity

Directors' and officers' liability insurance cover is in place in respect of the Directors. The Company's Articles of Association provide, subject to the provisions of UK legislation, an indemnity out of the assets of the Company for every Director or other officer of the Company against any liability which he or she may incur as a Director or other officer of the Company in defending any proceedings (whether civil or criminal) in which judgement is given in his or her favour, or he or she is acquitted, or in connection with any application under the Companies Act 2006 in which he or she is granted relief by the court.

Donations

During the year the Company made charitable donations totalling £5,000 (2015: £5,000). No political donations were made (2015: £nil).

The Board supports a number of charities, all of which are personally selected on an annual basis by the Directors. These charities span a variety of different causes including further education, working with underprivileged and deprived children and young people, motor neurone disease and the rehabilitation of prisoners.

Related Party Transactions

The Company's transactions with related parties in the year were with the Directors and Henderson. There have been no material transactions between the Company and its Directors during the year and the only amounts paid to them were in respect of expenses and remuneration for which there were no outstanding amounts payable at the year end. Directors' shareholdings are disclosed on page 27.

In relation to the provision of services by Henderson, other than fees payable by the Company in the ordinary course of business and the provision of sales and marketing services there have been no material transactions with Henderson affecting the financial position of the Company during the year under review. More details on transactions with Henderson, including amounts outstanding at the year end, are given in note 21 on page 58.

Share Capital

The Company's share capital comprises:

Ordinary shares of 25p nominal value each ("shares")
The voting rights of the shares on a poll are one vote for each share held. At 31 May 2016 and 31 May 2015 the number of shares in issue, and thus the number of voting rights, was 74,701,796. This represents 99.98% of the Company's share capital.

Preference Stock units of £1 each ("preference stock units")
Preference stockholders have no rights to attend and vote at General Meetings (except where the dividend is six months in arrears or on a resolution to wind up the Company). At 31 May 2016 and 31 May 2015 there were 4,257 preference stock units in issue. This represents 0.02% of the Company's share capital.

There are no restrictions on the transfer of the Company's share capital and there are no shares or stock which carry specific rights with regards to control of the Company.

The Directors seek annual authority from shareholders to allot new ordinary shares, to dis-apply the pre-emption rights of existing shareholders and to buy back for cancellation or to be held in treasury the Company's ordinary shares. The Company's Articles of Association permit the Company to purchase its own shares and to fund such purchases from its accumulated realised capital reserves.

At the Annual General Meeting in October 2015 a special resolution was passed giving the Company authority, until the conclusion of the Annual General Meeting in 2016, to make market purchases for cancellation of the Company's own ordinary shares up to a maximum of 11,197,799 shares (being 14.99% of the issued ordinary share capital as at 2 October 2015). In the period from 31 May 2016 to 9 August 2016 the Company did not buy back any ordinary shares. There remained 11,197,799 ordinary shares available within the buy-back authority granted in 2015. A fresh buy-back authority will be sought at the Annual General Meeting in September. Shares are not bought back unless the result is an increase in the NAV per ordinary share.

The Company also seeks annual authority to buy back preference stock units. No preference stock units were bought back during the year. A fresh buy-back authority will be sought at the Annual General Meeting in September. Further details of the preference stock units are given in note 14 on page 52.

Report of the Directors (continued)

Holdings in the Company's Shares

Declarations of interests in the voting rights of the Company as at 31 May 2016 in accordance with the UK Listing Authority's Disclosure Guidance and Transparency Rules were as follows:

	Number of ordinary shares held	% of voting rights
Lazard Asset Management LLC	6,093,799	8.16
East Riding of Yorkshire Council	4,454,111	5.96
1607 Capital Partners LLC	3,710,573	4.97
Newton Asset Management Ltd	3,697,223	4.94
Standard Life Investments	3,674,513	4.92
Prudential plc Group of Companies	2,897,854	3.87
Royal London Asset Management Ltd	2,893,256	3.87

There have been no further changes notified in the period to 9 August 2016.

The Board is aware that, as at 31 May 2016, 3.78% of the issued ordinary shares are held on behalf of participants in Halifax Share Dealing products run by Halifax Share Dealing Limited ("HSDL"). In accordance with the arrangements made between HSDL and Henderson, the participants in this scheme are given the opportunity to instruct HSDL's nominee company to exercise the voting rights appertaining to their shares in respect of all General Meetings of the Company.

Life of the Company

The Board announced on 27 September 2002 that it proposed to introduce regular continuation votes for the Company. A continuation vote was put to the Annual General Meetings of the Company held in 2004, 2007, 2010 and 2013 and will accordingly be put to shareholders again this year. In the event of the shareholders in General Meeting voting against the continuation of the Company, the Directors would expect to convene a further General Meeting, as soon as practicable, at which proposals to liquidate, reorganise or reconstruct the Company would be put forward.

Annual General Meeting ("AGM")

The AGM will be held on 23 September 2016 at 11.30 am at the Company's Registered Office. The Notice and details of the resolutions to be put at the AGM are contained in the document being sent to shareholders with this report.

Corporate Governance

The Corporate Governance Statement set out on pages 29 to 32 forms part of the Report of the Directors.

Other Information

Information on recommended dividends, future developments and financial risks are detailed in the Strategic Report.

Directors' Statement as to Disclosure of Information to the Auditors

Each of the Directors who were members of the Board at the date of approval of this report confirms that to the best of his or her knowledge and belief, there is no information relevant to the preparation of the Annual Report which the Company's Auditors is unaware and he or she has taken all the steps a Director might reasonably be expected to have taken to be aware of relevant audit information and to establish that the Company's Auditors is aware of that information.

Global Greenhouse Gas Emissions

As an externally managed investment trust company, the Company has no greenhouse gas emissions to report from its operations for the year to 31 May 2016 (2015: same), nor does it have responsibility for any other emissions producing sources under the Companies Act 2006 (Strategic Report and Directors' Reports) Regulations 2013.

Listing Rule 9.8.4

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

By order of the Board

Henderson Secretarial Services Limited
Corporate Secretary
10 August 2016

Statement of Directors' Responsibilities

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the Company's financial statements in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union. Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that year. In preparing these financial statements, the Directors are required to:

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

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

The Directors consider that the Annual Report, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

Statement under DTR 4.1.12

Each of the Directors, who are listed on page 16, confirms that, to the best of his or her knowledge:

- the financial statements, which have been prepared in accordance with IFRS as adopted by the European Union on a going concern basis, give a true and fair view of the assets, liabilities, financial position and profit of the Company; and
- the Strategic Report includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that it faces.

For and on behalf of the Board

Jamie Cayzer-Colvin
Chairman
10 August 2016

The financial statements are published on **www.hendersonsmallercompanies.com** which is a website maintained by Henderson.

Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The maintenance and integrity of the website is the responsibility of Henderson; the work carried out by the Auditors does not involve consideration of these matters and, accordingly, the Auditors accept no responsibility for any changes that may have occurred to the Annual Report since it was initially presented on the website.

Directors' Remuneration Report

Introduction

This report is submitted in accordance with Schedule 8 of The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 as amended in August 2013 (the "Regulations"). The report also meets the relevant requirements of the Companies Act 2006 (the "Act") and the Listing Rules of the Financial Conduct Authority and describes how the Board has applied the principles relating to Directors' remuneration. As required by section 439 of the Act, an ordinary resolution to approve the report will be proposed at the Annual General Meeting ("AGM") on 23 September 2016. The Company's remuneration policy was approved by shareholders at the AGM in 2014 in accordance with section 439A of the Act. No changes to the policy are currently proposed.

The Company's Auditors are required to report on certain information contained within this report; where information set out below has been audited it is indicated as such.

All Directors are non-executive and the Company has no chief executive officer or employees; as such some of the reporting requirements contained in the Regulations are not applicable and have not been reported on, including the requirement for a future policy table and an illustrative representation of the level of remuneration that could be received by each individual Director. It is believed that all relevant information is disclosed within this report in an appropriate format.

The Board as a whole considers Directors' remuneration. Therefore, the Board has not appointed a Remuneration Committee to consider such matters. The Board has not been provided with advice or services by any person in respect of its consideration of the Directors' remuneration (although the Directors review annually the fees paid to the boards of directors of other comparable investment trust companies).

Remuneration Policy

The Board consists entirely of non-executive Directors who meet six times a year to deal with the important aspects of the Company's affairs. New Directors are appointed with the expectation that they will serve for a minimum period of three years. Directors' appointments are reviewed formally every three years thereafter by the Board as a whole. None of the Directors has a contract of service or a contract for services and a Director may resign by notice in writing to the Board at any time; there are no set notice periods.

The Company's policy is for the Directors to be remunerated in the form of fees, payable quarterly in arrears, to the Director personally or to a third party specified by him or her. There are no long-term incentive schemes and the fees are not specifically related to the Directors' performance, either individually or collectively.

The Company's policy is that the fees payable to the Directors should reflect the time spent by the Board on the Company's affairs and the responsibilities borne by the Directors and should be sufficient to promote the long-term success of the Company. The policy is for the Chairman of the Board and the Chairman of the Audit Committee to be paid higher fees than the other Directors in recognition of their more onerous roles. The policy is to review the fee rates annually, although such review will not necessarily result in any change to them. The Company's Articles of Association limit the fees payable to the Directors to £200,000 per annum.

Annual Statement

As Chairman, Jamie Cayzer-Colvin reports that there have been no changes to Directors' remuneration for the year ended 31 May 2016. As reported in last year's Annual Report, fees were increased with effect from 1 June 2015. These increases were made after consideration of the fees paid to other investment trusts in the sector of an equivalent size and also in relation to the fees paid to directors of other Henderson managed trusts. These increases ensure the Directors are properly remunerated for their services to the Company and that the Company can remain competitive when seeking new Directors.

Annual Report on Remuneration

Directors' interests in shares (audited)

	Ordinary shares of 25p	
	31 May 2016	1 June 2015
Jamie Cayzer-Colvin	12,000	12,000
Beatrice Hollond	5,700	5,700
David Lamb	5,802	4,143
Keith Percy	5,980	5,980
Mary Ann Sieghart	5,918	4,448

No Director had an interest in the Debenture Stock or Preference Stock of the Company.

The interests of the Directors in the ordinary shares of the Company at the beginning and end of the financial year are shown in the above table. Since the year end, Mary Ann Sieghart has purchased a further 1,620 shares on 6 June 2016. There have been no other changes to any of the Directors' holdings in the period to 9 August 2016.

Relative Importance of Spend on Pay

In order to show the relative importance of spend on pay, the table below sets out the total level of remuneration compared to the distributions paid to shareholders by way of dividends. There were no share buy-backs during the year. There were no other significant distributions, payments or other uses of the Company's profit or cash flow deemed to assist in the understanding of the relative importance of spend on pay.

	2016 £	2015 £	Change £
Total remuneration	130,448	114,094	16,354
Ordinary dividends paid during the year	11,205,269	10,084,742	1,120,527

Statement of Voting at AGM

At the 2015 AGM 39,462,230 votes (99.68%) were received voting for the resolution seeking approval of the Directors' Remuneration Report, 56,494 (0.14%) were against, 69,529 (0.18%) were discretionary and 35,241 were withheld; the percentage of votes excludes votes withheld. In relation to the approval of the remuneration policy, 42,781,085 votes (99.50%) were received voting for the resolution, 163,259 (0.38%) were against, 53,268 (0.12%) were discretionary and 223,745 were withheld.

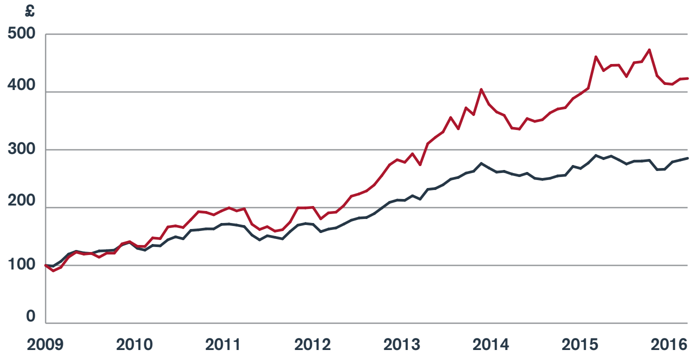
Directors' Remuneration Report (continued)

Performance

The graph compares the mid-market price of the Company's ordinary shares over the seven year period ended 31 May 2016 with the return from the Numis Smaller Companies Index (excluding investment companies) on a total return basis in sterling terms ("Benchmark") over the same period.

Company's share price total return, assuming the investment of £100 on 31 May 2009 and the reinvestment of all dividends (excluding dealing expenses) (Source: Morningstar Funddata)

Benchmark total return, assuming the notional investment of £100 on 31 May 2009 and the reinvestment of all income (excluding dealing expenses) (Source: Datastream)



Directors' Remuneration (audited)

The remuneration paid to the Directors who served during the years ended 31 May 2016 and 31 May 2015 was as follows:

	2016 Total salary and fees £	2015 Total salary and fees £	2016 Expenses and taxable benefits £	2015 Expenses and taxable benefits £	2016 Total £	2015 Total £
Jamie Cayzer-Colvin[1]	34,000	30,000	360	–	34,360	30,000
Beatrice Hollond[2]	27,000	24,000	–	–	27,000	24,000
David Lamb	23,000	20,000	–	–	23,000	20,000
Keith Percy	23,000	20,000	88	94	23,088	20,094
Mary Ann Sieghart	23,000	20,000	–	–	23,000	20,000
Total	**130,000**	**114,000**	**448**	**94**	**130,448**	**114,094**

Notes:
The table above omits other columns set out in the relevant regulations because no payments of other types such as performance related pay, vesting performance related pay and pension related benefits were made
1 Chairman and highest paid Director
2 Chairman of the Audit Committee

No other remuneration or compensation was paid or payable by the Company during the year to any of the current or former Directors or third parties specified by any of them.

For and on behalf of the Board

Jamie Cayzer-Colvin
Chairman
10 August 2016

Corporate Governance Statement

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

Applicable Corporate Governance Codes

The Board is accountable to shareholders for the governance of the Company's affairs. As an investment company, the Company's day-to-day responsibilities are delegated to third parties; the Company has no employees and the Directors are all non-executive. Therefore not all the provisions of the UK Corporate Governance Code (the "UK Code") issued by the Financial Reporting Council ("FRC") in September 2014 are directly applicable to the Company. The Board has therefore considered the principles and recommendations of the Code of Corporate Governance published by the Association of Investment Companies in February 2015 (the "AIC Code") by reference to the AIC Corporate Governance Guide for Investment Companies (the "AIC Guide"). The AIC Code, as explained by the AIC Guide, addresses all the applicable principles set out in the UK Code as well as setting out additional principles and recommendations on issues that are of specific relevance to the Company. The FRC has confirmed that by following the AIC Guide, boards of investment companies should fully meet their obligations in relation to the UK Code and paragraph 9.8.6 of the Listing Rules.

The Board has noted that the FRC and the AIC have issued revised Codes which the Company will be required to report against next year.

Copies of the AIC Code, the AIC Guide and the UK Code can be found on the respective organisations' websites: **www.theaic.co.uk** and **www.frc.org.uk**.

Statement of Compliance

The Directors believe that the Company has complied with the recommendations of the AIC Code that are applicable to smaller companies (those below the FTSE 350) during the year under review and up to the date of this report and thereby the provisions of the UK Code except as set out below.

The UK Code includes provisions relating to:

- the role of the chief executive;
- executive directors' remuneration; and
- the need for an internal audit function.

For the reasons set out in the AIC Guide, and as explained in the UK Code, the Board considers these provisions are not relevant to the position of the Company as it is an externally managed investment company. In particular, all of the Company's day to day management and administrative functions are outsourced to third parties. As a result, the Company has no executive directors, employees or internal operations.

The Board

The Board is collectively responsible for the success of the Company. Its role is to provide entrepreneurial leadership within a framework of prudent and effective controls that enable risk to be assessed and managed. The Board is responsible for setting the Company's standards and values and for ensuring that its obligations to its shareholders and others are understood and met. The Board sets the Company's strategic aims (subject to the Company's Articles of Association, and to such approval of the shareholders in General Meeting as may be required from time to time) and ensures that the necessary resources are in place to enable the Company's objectives to be met.

The Board currently consists of five non-executive Directors. All Directors have a wide range of other interests and are not dependent on the Company itself. At a Board meeting in May the Directors reviewed their independence and confirmed that all Directors remain wholly independent of Henderson. Their biographical details, set out on page 16, demonstrate a breadth of investment, commercial and professional experience with an international perspective.

The Board meets six times a year and deals with the important aspects of the Company's affairs, including the setting of parameters for and the monitoring of investment strategy and the review of investment performance. The Board sets limits on the size and concentration of new investments, on any use of derivatives and on the extent to which borrowings may be used. The application of these and other restrictions, including those which govern the Company's tax status as an investment trust, are reviewed regularly at meetings of the Board. Henderson takes decisions as to the purchase and sale of individual investments and is responsible for effecting those decisions on the best available terms.

The Chairman is responsible for leading the Board and for ensuring that it continues to deal effectively with all the aspects of its role. In particular, he ensures that Henderson provides the Directors, in a timely manner, with management, regulatory and financial information that is clear, accurate and relevant. Representatives of Henderson attend each Board meeting, enabling the Directors to seek clarification on specific issues or to probe further on matters of concern. The Board has a formal schedule of matters specifically reserved for its decision, which include strategy, management and structure, financial reporting and other communications, Board membership and other appointments, contracts, internal controls and corporate governance. There is an agreed procedure for Directors, in the furtherance of their duties, to take independent professional advice, if necessary, at the Company's expense. The Directors have access to the advice and services of the Corporate Secretary, through its appointed representative, who is responsible to the Board for ensuring that Board procedures are followed.

The Board may appoint Directors to the Board without shareholder approval. Any Director so appointed must stand for election by the shareholders at the next Annual General Meeting in accordance with the Articles of Association. Victoria Sant will stand for election at this year's AGM following her appointment to the Board on 23 September 2016. The total number of Directors shall not be less than two nor more than fifteen.

In addition, under the Articles of Association, shareholders may remove a Director before the end of his or her term by passing a special resolution at a General Meeting of the Company. A special resolution is passed if more than 75% of the votes cast, in person or by proxy, are in favour of the resolution.

Corporate Governance Statement (continued)

When a Director is appointed he or she is offered an induction programme organised by Henderson at the request of the Chairman. Directors are also provided, on a regular basis, with key information on the Company's policies, regulatory and statutory requirements and internal controls. Changes affecting Directors' responsibilities are advised to the Board as they arise. Directors are encouraged to attend suitable training courses on an ongoing basis at the Company's expense.

The Board have agreed that all Directors will stand for re-election on an annual basis. This year Keith Percy will not be seeking re-election as he is standing down at the AGM, having served on the Board since July 2006.

The Board's tenure and succession policy seeks to ensure that the Board is well balanced and refreshed regularly by the appointment of new Directors with the skills and experience necessary, in particular, to replace those lost by Directors' retirements. Directors must be able to demonstrate their commitment, including in terms of time, to the Company. The Board is of the view that length of service does not of itself impair a Director's ability to act independently. Rather, a long serving Director can offer a perspective that adds value to the deliberations of a well-balanced investment trust company board. Accordingly, the Board does not consider that Directors lose their independence solely by virtue of length of service but the roles and contributions of long-serving Directors will be subject to particularly rigorous review every year.

Board Evaluation

The Board's procedure in the current year for evaluating the performance of the Board, its Committees and the individual Directors has been by means of questionnaire. The evaluation process is designed to show whether individual Directors continue to contribute effectively to the Board and to clarify the strengths and weaknesses of the Board's composition and processes. The Chairman takes the lead in acting on the results of the evaluation process. In respect of the Chairman, a meeting of the Directors was held under the chairmanship of the Senior Independent Director, without the Chairman present, to evaluate his performance.

The Chairman of the Company is an independent non executive Director. Keith Percy is the Company's Senior Independent Director. Following his retirement from the Board, Mary Ann Sieghart will be the Company's Senior Independent Director. The Board considers that all the Directors have different qualities and areas of expertise on which they may lead when issues arise.

Board Committees

The Board has established Audit, Management Engagement and Nomination Committees with defined terms of reference and duties. All three Committees comprise non-executive Directors appointed by the Board; the Board also appoints the Chairman of each of the Committees. The membership of these Committees is set out on page 16. A record of the meetings held during the year is set out on page 31.

The terms of reference of the three Committees are available for inspection on the Company's website **www.hendersonsmallercompanies.com** or on application to the Corporate Secretary.

Audit Committee

The Audit Committee is chaired by Beatrice Hollond, the other members of which are Keith Percy, Mary Ann Sieghart and David Lamb. None of the members of the Audit Committee are accountants by profession but the Board consider some of the Directors, including the Audit Committee Chairman, to have recent and relevant financial experience. David Lamb is a qualified actuary. The Report of the Audit Committee can be found on pages 33 and 34.

Management Engagement Committee

All Directors are members of the Management Engagement Committee, which is chaired by the Chairman of the Board. The Management Engagement Committee is responsible for the regular review of the terms of the management contract with Henderson. The Management Engagement Committee met once formally during the year. The details of the management arrangements are set out on pages 4 and 5.

Nomination Committee

All Directors are members of the Nomination Committee, which is chaired by the Chairman of the Board (who would not chair the Committee when the Chairman's successor was being considered). The Committee is responsible for reviewing Board succession planning and tenure policy, the performance of the Board as a whole and the Board Committees and the appointment of new Directors through an established formal procedure.

When considering succession planning, the Committee bears in mind the balance of skills, knowledge, experience and diversity existing on the Board although does not consider it appropriate to have set targets in relation to diversity. The Nomination Committee considers diversity as part of the annual performance evaluation and it is felt that there is a broad range of backgrounds, experience and gender and each Director brings different qualities to the Board and its discussions. The Nomination Committee will recommend when the recruitment of additional non-executive Directors is required to enhance the diversity on the Board. Once a decision is made to recruit additional Directors to the Board, a formal job description is drawn up. The Committee will use external agencies as and when the requirement to recruit an additional Board member becomes necessary and did so with the recruitment of Victoria Sant, when Nurole Ltd, who have not provided any other services to the Company were engaged. The Committee also reviews and recommends to the Board the Directors seeking re-election on an annual basis. Recommendation is not automatic and will follow a process of evaluation of each Director's performance and consideration of the Director's independence. The Committee also takes into account the mix of skills and experience of the current Board members. In accordance with the UK Code any Director serving for longer than six years would be subject to particularly rigorous assessment of his or her contribution.

The Committee meets annually to carry out its review of the Board, its composition and size and its Committees.

Corporate Governance Statement (continued)

Board attendance

The table below sets out the number of Board and Committee meetings held during the year under review and the number of meetings attended by each Director. All Directors attended the AGM in October 2015.

	Board	AC	MEC	NC
Number of meetings	**6**	**3**	**1**	**2**
Jamie Cayzer-Colvin[1]	6	3	1	2
Keith Percy	6	3	1	2
David Lamb	6	3	1	2
Mary Ann Sieghart	6	3	–	1
Beatrice Hollond	6	3	1	2

AC: Audit Committee
MEC: Management Engagement Committee
NC: Nomination Committee
1 Jamie Cayzer-Colvin is not a member of the Audit Committee but attends meetings by invitation

The Directors and committees of the Board also met during the year to undertake business such as approval of the Company's results.

Internal Controls

The Board has established an ongoing process for identifying, evaluating and managing any major risks faced by the Company. The process accords with Guidance on Risk Management, Internal Controls and Related Financial and Business Reporting issued by the FRC in September 2014 and is subject to regular review by the Board. The Board has overall responsibility for the Company's system of internal controls and for reviewing its effectiveness. However, such a system is designed to manage rather than eliminate risks of failure to achieve the Company's business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss. The Board has reviewed the effectiveness of the Company's system of internal controls for the year ended 31 May 2016. During the course of its review the Board has not identified or been advised of any failings or weaknesses that have been determined as significant. All business risks faced by the Company are recorded in a detailed risk map which is reviewed regularly.

Henderson has established an internal control framework to provide reasonable, but not absolute, assurance on the effectiveness of the internal controls operated on behalf of its clients. The effectiveness of the internal controls is assessed by Henderson's compliance, internal audit and risk departments on a continuing basis. The Board receives a formal report on a quarterly basis which details the steps taken to monitor the areas of risk, including those that are not directly the responsibility of Henderson, and which reports the details of any known internal control failures. The Board receives a report on Henderson's internal controls each year which includes a report from Henderson's Auditors on the control policies and procedures in operation.

The Company does not have an internal audit function; it delegates to third parties most of its operations and does not employ any staff. Accordingly, in practice the Board must place reliance on Henderson and its other contractors to ensure that they operate effective internal audit functions. The Board will continue to monitor its system of internal control in order to provide assurance that it operates as intended and the Directors will review at least annually whether a function equivalent to an internal audit is needed.

Accountability and Relationship with Henderson

The Statement of Directors' Responsibilities in respect of the financial statements is set out on page 26, the Independent Auditors' Report on pages 35 to 39 and the Viability Statement on pages 18 and 19.

The Board has delegated contractually to external third parties, including Henderson, the management of the investment portfolio, the custodial services (which include the safeguarding of the assets which is delegated through the appointment of the Depositary as explained on page 21), the day-to-day accounting, company secretarial and administration requirements and registration services. Each of these contracts was entered into after full and proper consideration by the Board of the quality and cost of the services offered, including the control systems in operation in so far as they relate to the affairs of the Company.

The Board receives and considers regular reports from Henderson and ad hoc reports and information are supplied to the Board as required. In addition, the Chairman is able to attend meetings of all the chairmen of the investment trust companies managed by Henderson which provides a forum to discuss industry matters which would then be reported to the Board.

Henderson takes decisions as to the purchase and sale of individual investments. Henderson also ensures that all Directors receive, in a timely manner, all relevant management, regulatory and financial information. Representatives of Henderson attend each Board meeting enabling the Directors to probe further on matters of concern. The Directors have access to the advice and services of the Corporate Secretary through its appointed representative who is responsible to the Board for ensuring that Board and Committee procedures are followed and that applicable rules and regulations are complied with. The proceedings at all Board and Committee meetings are fully recorded through a process that allows any Director's concerns to be recorded in the minutes. The Board and Henderson operate in a supportive, co-operative and open environment.

The Corporate Secretary, Henderson Secretarial Services Limited, is a subsidiary of Henderson with its own reporting lines and audited internal controls. There are processes and controls in place to ensure that there is a clear distinction between the two entities, particularly when dealing with any conflicts or issues between the Company and Henderson. Any correspondence from shareholders addressed to the Chairman or the Company received at Henderson's offices is forwarded to the Chairman of the Company in line with the audited procedures in place. Any correspondence is submitted to the next Board meeting.

Corporate Governance Statement (continued)

Henderson and BNP Paribas Securities Services, which acts for Henderson, have arrangements in place by which their staff may, in confidence, raise concerns about possible improprieties in relation to financial reporting or other matters.

The Board has reviewed the implications of the Bribery Act 2010, which came into force on 1 July 2011, and confirmed its zero tolerance to bribery and corruption in its business activities. It has received assurances from the Company's main contractors and suppliers that they will maintain adequate safeguards to protect against any potentially illegal behaviour by their employees and agents.

Continued Appointment of Henderson

The Board considers the arrangements for the provision of investment management and other services to the Company on an ongoing basis. The principal contents of the management agreement with Henderson are contained on pages 4 and 5.

In addition to the monitoring of investment performance at each meeting, through the Management Engagement Committee an annual review of the Company's investment performance over both the short and longer terms, together with the quality of other services provided by Henderson, including company secretarial and accounting, is undertaken.

Following an annual review, it is the Directors' opinion that the continuing appointment of Henderson on the existing terms is in the interest of the Company and its Shareholders as a whole.

Share Capital

Please see the Report of the Directors on page 24.

Relations with Shareholders

Shareholder relations are given high priority by the Board. The prime medium by which the Company communicates with its shareholders is through the half year results and Annual Report which aim to provide shareholders with a clear understanding of the Company's activities and their results. This information is supplemented by the daily calculation and publication of the NAV per share to a regulatory information service and a monthly fact sheet which is available on the website. Henderson also provides information on the Company and Fund Manager videos on the website, via various social media channels and through its HGi content platform, more details of which are included on page 17.

The Board considers that shareholders should be encouraged to attend and participate in the AGM, which will also be available to watch as it happens by visiting **www.henderson.com/trustslive**. Shareholders have the opportunity to address questions to the Chairman of the Board, the Chairman of the Audit Committee and all other Directors at the meeting and the Fund Manager will make a presentation to shareholders. A summary of the proxy votes received on the resolutions proposed is displayed at the meeting and each substantial issue is dealt with in a separate resolution. It is the intention of the Board that the Annual Report and notice of AGM be issued to shareholders so as to provide at least 20 working days' notice of the meeting. These documents are also included on the website. Shareholders wishing to lodge questions in advance of the meeting, or raise issues or concerns at any time, are invited to do so by writing to the Chairman via the Corporate Secretary at the address given on page 17.

General presentations to both shareholders and analysts follow the publication of the annual results. All meetings between Henderson and shareholders are reported to the Board.

By order of the Board

Henderson Secretarial Services Limited
Corporate Secretary
10 August 2016

Report of the Audit Committee

The Audit Committee is chaired by Beatrice Hollond, the other members are Keith Percy, Mary Ann Sieghart and David Lamb. Jamie Cayzer-Colvin attends the Audit Committee meetings by invitation. Although none of the members of the Audit Committee are by profession an accountant, the Board considers that several of the Directors, including the Chairman of the Audit Committee, have recent and relevant financial experience from their senior management roles elsewhere.

Meetings

The Audit Committee's usual programme is to meet at least three times a year: in advance of the publication of both the annual and the half year results and on at least one other occasion with an agenda that is focused on its broader responsibilities. The Company's Auditors are invited to attend meetings of the Committee on a regular basis. Representatives of Henderson and BNP Paribas Securities Services may also be invited to attend if deemed necessary by the Committee.

Role and Responsibilities

The role of the Committee is to assist the Board in applying financial reporting and internal control principles and to maintain an appropriate relationship with the Auditors. The Audit Committee formally reports to the Board, the Committee's responsibilities are set out in formal terms of reference which are reviewed at least annually.

In the year under review the main duties undertaken were:

- a review of the half year results and the Annual Report, including the disclosures made therein in relation to internal controls and risk management, viability, going concern and related parties and consideration of whether the report is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy in order to make recommendations to the Board. In assessing whether the report is fair, balanced and understandable, each Director reviewed the disclosures made, applying their respective knowledge and expertise;

- consideration of the quality and effectiveness of the accounting records and management information maintained on behalf of the Company, relying on meetings with and reports from Henderson;

- consideration of the internal controls in place at Henderson and BNP Paribas Securities Services as administrator, and Henderson's policies in relation to cyber risk and business continuity, meeting with representatives of Henderson's internal audit and risk departments periodically;

- consideration of the whistle blowing policy that Henderson has put in place for its staff to raise concerns about possible improprieties, including in relation to the Company, in confidence. The policy includes the necessary arrangements for independent investigation and follow up action;

- consideration of the key risks, risk management systems in place and the Company's risk map;

- consideration of the Company's Anti-Bribery Policy;

- consideration of whether there is a need for an internal audit function in order to make a recommendation to the Board;

- consideration of the nature and scope of the external audit and the findings therefrom;

- consideration of the appointment of the Auditors, the Auditors' effectiveness, performance and remuneration;

- consideration of the Auditors' independence and objectivity and the provision of any non-audit services;

- consideration of the annual confirmation from the Company's Depositary; and

- consideration of the appropriate level of dividend to be paid by the Company.

Policy on Non-Audit Services

In July 2011 the Audit Committee adopted a new policy on the provision of non-audit services, in accordance with the Financial Reporting Council's Guidance on Audit Committees. The Committee has determined that the Auditors will not be engaged to provide any non-audit services where the Committee considers there to be any significant risk of their independence, objectivity and effectiveness being compromised by the provision of such services. The Committee may approve the provision of non-audit services if it considers such services to be (a) relevant to the statutory audit work; (b) more efficiently provided by the external audit firm than by a third party; and (c) at low risk of impairing the independence, objectivity and effectiveness of the audit. The Audit Committee will refer to the Board any engagement with a cost or potential cost greater than £20,000 (or the cost, excluding VAT, of the most recent annual audit if higher). All engagements for non-audit services will be determined on a case-by-case basis.

Report of the Audit Committee (continued)

Annual Report for the year ended 31 May 2016

In relation to the financial statements for the year ended 31 May 2016 the following significant issues were considered by the Committee:

Significant issue	How the issue was addressed
Valuation and ownership of the Company's investments	The Directors have appointed Henderson to perform the valuation of the assets of the Company in accordance with its responsibilities under the AIFMD rules. As required under the AIFMD rules, Henderson has adopted a written valuation policy, which may be modified from time to time. Actively traded investments are valued using stock exchange prices provided by third party pricing vendors. Ownership of listed investments is verified by reconciliation to the Custodian's records.
Correct calculation of the performance fee	The performance fee calculation is prepared by the Administrators (BNP Paribas Securities Services) and reviewed by Henderson and reviewed in depth by the Committee, all with reference to the investment management agreement.
Compliance with Section 1158 of the Corporation Tax Act 2010	The Committee regularly considers the controls in place to ensure that the regulations for ensuring investment trust status are observed at all times, receiving supporting documentation from Henderson and BNP Paribas Securities Services.
Maintaining internal controls	The Committee receives regular reports on internal controls from Henderson, BNP Paribas Securities Services and HSBC and its delegates and has access to the relevant personnel of Henderson who have a responsibility for risk management and internal audit.
Recognition of income	Income received is accounted for in line with the Company's accounting policies (as set out on page 45) and is reviewed by the Committee at each meeting.

The Committee is satisfied that the Annual Report for the year ended 31 May 2016, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

External Audit, Review and Re-appointment

In 2014 the Company invited tenders for the Company's audit. After full consideration of the proposals, and the Auditors' performance, the Committee recommended to the Board that PricewaterhouseCoopers LLP continue as Auditors to the Company.

The Committee discuss the audit process with the Auditors without representatives of Henderson present and consider the effectiveness of the audit process after each audit. The Audit Committee remains satisfied with the effectiveness of the audit provided by PricewaterhouseCoopers LLP.

The Committee is satisfied that the Auditors are independent of the Company. The Auditors are required to rotate partners every five years and this is the third year that the current partner has been in place.

Resolutions to confirm the re-appointment of PricewaterhouseCoopers LLP as Auditors to the Company and to authorise the Directors to determine their remuneration will be proposed at the Annual General Meeting.

Audit Tendering

PricewaterhouseCoopers LLP and its predecessor firms have been the Company's auditors for many years. As a Public Interest Entity listed on the London Stock Exchange, the Company will in future be subject to the mandatory auditor rotation requirements of the European Union. Subject to the detailed implementation of the European requirements in the UK, this is likely to mean that the Company will put the external audit out to tender at least every ten years, and change Auditors at least every twenty years. This legislation will require the Company to put the audit out to tender for the 2021 year end. The Audit Committee will, however, continue to consider annually the need to go to tender for audit quality or independence reasons.

Beatrice Hollond
Audit Committee Chairman
10 August 2016

Independent Auditors' Report to the Members of The Henderson Smaller Companies Investment Trust plc

Report on the financial statements

Our opinion

In our opinion, The Henderson Smaller Companies Investment Trust plc's financial statements (the "financial statements"):

- give a true and fair view of the state of the Company's affairs as at 31 May 2016 and of its loss and cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

What we have audited

The financial statements, included within the Annual Report, comprise:

- the Balance Sheet as at 31 May 2016;
- the Statement of Comprehensive Income for the year then ended;
- the Cash Flow Statement for the year then ended;
- the Statement of Changes in Equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

Certain required disclosures have been presented elsewhere in the Annual Report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

The financial reporting framework that has been applied in the preparation of the financial statements is IFRSs as adopted by the European Union, and applicable law.

Our audit approach

Overview

- Overall materiality: £5.4 million which represents 1% of Net Assets.

- The Company is a standalone Investment Trust Company and engages Henderson Investment Funds Limited (the "Manager") to manage its assets.
- We conducted our audit of the financial statements using information from BNP Paribas Securities Services (the "Administrator") to whom the Manager has, with the consent of the Directors, delegated the provision of certain administrative functions.
- We tailored the scope of our audit taking into account the types of investments within the Company, the involvement of the third parties referred to above, the accounting processes and controls, and the industry in which the Company operates.

- Valuation and existence of investments.
- Dividend Income.

Independent Auditors' Report to the Members of The Henderson Smaller Companies Investment Trust plc (continued)

The scope of our audit and our areas of focus

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)").

We designed our audit by determining materiality and assessing the risks of material misstatement in the financial statements. In particular, we looked at where the Directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits we also addressed the risk of management override of internal controls, including evaluating whether there was evidence of bias by the Directors that represented a risk of material misstatement due to fraud.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are identified as "areas of focus" in the table below. We have also set out how we tailored our audit to address these specific areas in order to provide an opinion on the financial statements as a whole, and any comments we make on the results of our procedures should be read in this context. This is not a complete list of all risks identified by our audit.

Area of focus	How our audit addressed the area of focus
Valuation and existence of investments The investment portfolio at the year end comprised of listed equity investments valued at £595.9 million. We focused on the valuation and existence of investments because investments represent the principal element of the net asset value as disclosed on the Balance Sheet in the financial statements.	We tested the valuation of the listed equity investments by agreeing the prices used in the valuation to independent third party sources. No misstatements were identified by our testing which required reporting to those charged with governance. We tested the existence of the investment portfolio by agreeing the holdings for investments to an independent custodian confirmation from HSBC Bank plc. No differences were identified which required reporting to those charged with governance.
Dividend Income We focused on the accuracy and completeness of dividend income recognition and its presentation in the Statement of Comprehensive Income as set out in the requirements of The Association of Investment Companies Statement of Recommended Practice (the "AIC SORP"). This is because incomplete or inaccurate income could have a material impact on the Company's net asset value and dividend cover.	We assessed the accounting policy for income recognition for compliance with accounting standards and the AIC SORP and performed testing to check that dividend income had been accounted for in accordance with this stated accounting policy. We found that the accounting policies implemented were in accordance with accounting standards and the AIC SORP, and that dividend income has been accounted for in accordance with the stated accounting policy. We understood and assessed the design and implementation of relevant controls surrounding dividend income recognition. In addition, we tested dividend receipts by agreeing the dividend rates from investments to independent third party sources. No misstatements were identified by our testing which required reporting to those charged with governance. To test for completeness, we tested that the appropriate dividends had been received in the year by reference to independent data of dividends declared by investment holdings in the portfolio. Our testing did not identify any unrecorded dividends. We tested the allocation and presentation of dividend income between the revenue and capital return columns of the Statement of Comprehensive Income in line with the requirements set out in the AIC SORP. We then tested the validity of special dividends to independent third party sources. We did not find any special dividends that were not treated in accordance with the AIC SORP.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the geographic structure of the Company, the accounting processes and controls, and the industry in which the Company operates.

Independent Auditors' Report to the Members of The Henderson Smaller Companies Investment Trust plc (continued)

The Company's accounting is delegated to the Administrator who maintain their own accounting and controls.

As part of our risk assessment, we assessed the control environment in place at both the Manager and the Administrator to the extent relevant to our audit. This assessment of the operating and accounting structure in place at both organisations involved obtaining and reading the relevant control reports issued by the independent auditor of the Manager and the Administrator in accordance with generally accepted assurance standards for such work. We then identified those relevant controls at the Administrator on which we could place reliance to provide audit evidence.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Overall materiality	£5.4 million (2015: £5.6 million).
How we determined it	1% of Net Assets.
Rationale for benchmark applied	We have applied this benchmark, a generally accepted auditing practice for investment trust audits.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £273,000 (2015: £281,000) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Going concern

Under the Listing Rules we are required to review the Directors' statement, set out on page 26, in relation to going concern. We have nothing to report having performed our review.

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to the Directors' statement about whether they considered it appropriate to adopt the going concern basis in preparing the financial statements. We have nothing material to add or to draw attention to.

As noted in the Directors' statement, the Directors have concluded that it is appropriate to adopt the going concern basis in preparing the financial statements. The going concern basis presumes that the Company has adequate resources to remain in operation, and that the Directors intend it to do so, for at least one year from the date the financial statements were signed. As part of our audit we have concluded that the Directors' use of the going concern basis is appropriate. However, because not all future events or conditions can be predicted, these statements are not a guarantee as to the Company's ability to continue as a going concern.

Other required reporting

Consistency of other information

Companies Act 2006 opinion

In our opinion the information given in the Strategic Report and the Report of the Directors for the financial year for which the financial statements are prepared is consistent with the financial statements.

ISAs (UK & Ireland) reporting

Under ISAs (UK & Ireland) we are required to report to you if, in our opinion:

▪ information in the Annual Report is: – materially inconsistent with the information in the audited financial statements; or – apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Company acquired in the course of performing our audit; or – otherwise misleading.	We have no exceptions to report.

Independent Auditors' Report to the Members of The Henderson Smaller Companies Investment Trust plc (continued)

▪ the statement given by the Directors on page 26, in accordance with provision C.1.1 of the UK Corporate Governance Code (the "Code"), that they consider the Annual Report taken as a whole to be fair, balanced and understandable and provides the information necessary for members to assess the Company's position and performance, business model and strategy is materially inconsistent with our knowledge of the Company acquired in the course of performing our audit.	We have no exceptions to report.
▪ the section of the Annual Report on pages 33 and 34, as required by provision C.3.8 of the Code, describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.	We have no exceptions to report.

The Directors' assessment of the prospects of the Company and of the principal risks that would threaten the solvency or liquidity of the Company

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to:

▪ the Directors' confirmation on page 18 of the Annual Report, in accordance with provision C.2.1 of the Code, that they have carried out a robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity.	We have nothing material to add or to draw attention to.
▪ the disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.	We have nothing material to add or to draw attention to.
▪ the Directors' explanation on pages 18 and 19 of the Annual Report, in accordance with provision C.2.2 of the Code, as to how they have assessed the prospects of the Company, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.	We have nothing material to add or to draw attention to.

Under the Listing Rules we are required to review the Directors' statement that they have carried out a robust assessment of the principal risks facing the Company and the Directors' statement in relation to the longer-term viability of the Company. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the Directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the Code; and considering whether the statements are consistent with the knowledge acquired by us in the course of performing our audit. We have nothing to report having performed our review.

Adequacy of accounting records and information and explanations received

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

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

We have no exceptions to report arising from this responsibility.

Directors' remuneration

Directors' Remuneration Report – Companies Act 2006 opinion

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

Other Companies Act 2006 reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of Directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

Independent Auditors' Report to the Members of The Henderson Smaller Companies Investment Trust plc (continued)

Corporate governance statement

Under the Listing Rules we are required to review the part of the Corporate Governance Statement relating to ten further provisions of the Code. We have nothing to report having performed our review.

Responsibilities for the financial statements and the audit

Our responsibilities and those of the Directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 26, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What an audit of financial statements involves

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 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.

We primarily focus our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Jeremy Jensen (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
10 August 2016

Statement of Comprehensive Income

Notes		Year ended 31 May 2016 Revenue return £'000	Year ended 31 May 2016 Capital return £'000	Year ended 31 May 2016 Total £'000	Year ended 31 May 2015 Revenue return £'000	Year ended 31 May 2015 Capital return £'000	Year ended 31 May 2015 Total £'000
2	Investment income	13,621	–	13,621	12,838	–	12,838
3	Other income	91	–	91	207	–	207
10	(Losses)/gains on investments held at fair value through profit or loss	–	(15,596)	(15,596)	–	89,494	89,494
	Total income/(expense)	**13,712**	**(15,596)**	**(1,884)**	**13,045**	**89,494**	**102,539**
	Expenses						
4	Management and performance fees	(565)	(1,319)	(1,884)	(538)	(3,256)	(3,794)
5	Other expenses	(487)	–	(487)	(472)	–	(472)
	Profit/(loss) before finance costs and taxation	**12,660**	**(16,915)**	**(4,255)**	**12,035**	**86,238**	**98,273**
6	**Finance costs**	(755)	(1,764)	(2,519)	(789)	(1,841)	(2,630)
	Profit/(loss) before taxation	**11,905**	**(18,679)**	**(6,774)**	**11,246**	**84,397**	**95,643**
7	Taxation	(9)	–	(9)	(12)	–	(12)
	Profit/(loss) for the year and total comprehensive income/(expense)	**11,896**	**(18,679)**	**(6,783)**	**11,234**	**84,397**	**95,631**
8	Earnings per ordinary share – basic and diluted	15.92p	(25.00p)	(9.08p)	15.04p	112.98p	128.02p

The total column of this statement represents the Statement of Comprehensive Income, prepared in accordance with IFRS as adopted by the European Union.

The revenue return and capital return columns are supplementary to this and are prepared under guidance published by the Association of Investment Companies.

The notes on pages 44 to 59 form part of these financial statements.

Statement of Changes in Equity

Notes		Year ended 31 May 2016 Share capital £'000	Capital redemption reserve £'000	Retained earnings Capital reserves £'000	Revenue reserve £'000	Total equity £'000
	Total equity at 1 June 2015	18,676	26,745	501,974	15,926	563,321
	Total comprehensive income:					
	(Loss)/profit for the year	–	–	(18,679)	11,896	(6,783)
	Transactions with owners, recorded directly to equity:					
9	Ordinary dividends paid	–	–	–	(10,458)	(10,458)
	Total equity at 31 May 2016	**18,676**	**26,745**	**483,295**	**17,364**	**546,080**

Notes		For the year ended 31 May 2015 Share capital £'000	Capital redemption reserve £'000	Retained earnings Capital reserves £'000	Revenue reserve £'000	Total equity £'000
	Total equity at 1 June 2014	18,676	26,745	417,577	13,283	476,281
	Total comprehensive income:					
	Profit for the year	–	–	84,397	11,234	95,631
	Transactions with owners, recorded directly to equity:					
9	Ordinary dividends paid	–	–	–	(8,591)	(8,591)
	Total equity at 31 May 2015	**18,676**	**26,745**	**501,974**	**15,926**	**563,321**

The notes on pages 44 to 59 form part of these financial statements.

Balance Sheet

Notes		At 31 May 2016 £'000	At 31 May 2015 £'000
	Non current assets		
10	Investments held at fair value through profit or loss	595,927	605,776
	Current assets		
12	Receivables	2,612	2,734
	Tax recoverable	23	12
	Cash and cash equivalents	10,224	10,183
		12,859	**12,929**
	Total assets	608,786	618,705
	Current liabilities		
13	Payables	(791)	(3,179)
14	Financial liabilities	–	(20,000)
15	Bank loans	(32,107)	(32,201)
		(32,898)	**(55,380)**
	Total assets less current liabilities	575,888	563,325
	Non current liabilities		
14	Financial liabilities	(29,808)	(4)
	Net assets	**546,080**	**563,321**
	Equity attributable to equity shareholders		
16	Share capital	18,676	18,676
17	Capital redemption reserve	26,745	26,745
	Retained earnings:		
17	Capital reserve	483,295	501,974
18	Revenue reserve	17,364	15,926
	Total equity	**546,080**	**563,321**
19	**Net asset value per ordinary share**	731.0p	754.1p

These financial statements on pages 40 to 59 were approved by the Board of Directors on 10 August 2016 and were signed on its behalf by:

Jamie Cayzer-Colvin
Chairman

The notes on pages 44 to 59 form part of these financial statements.

Cash Flow Statement

Notes		Year ended 31 May 2016 £'000	Year ended 31 May 2015 £'000
	Operating activities		
	(Loss)/profit before taxation	(6,774)	95,643
	Add back interest payable	2,519	2,630
10	Losses/(gains) on investments held at fair value through profit or loss	15,596	(89,494)
	Purchases of investments	(158,484)	(135,283)
	Sales of investments	152,700	138,553
	Increase in receivables	(150)	(696)
	Decrease in amounts due from brokers	61	640
	Decrease in accrued income	211	9
	(Decrease)/increase in payables	(2,350)	1,517
	(Decrease)/increase in amounts due to brokers	(242)	584
	Taxation on investment income	(20)	(7)
	Net cash inflow from operating activities before interest and taxation	**3,067**	**14,096**
	Interest paid	(2,511)	(2,647)
	Net cash inflow from operating activities	**556**	**11,449**
	Financing activities		
9	Equity dividends paid	(10,458)	(8,591)
	(Repayment)/drawdown of bank loans	(94)	6,171
14	Repayment of 10.5% Debenture Stock	(20,000)	–
14	Issue of Unsecured Loan Notes	30,000	–
	Net cash outflow from financing activities	**(552)**	**(2,420)**
	Increase in cash and cash equivalents	4	9,029
	Cash and cash equivalents at the start of the year	10,183	1,154
	Exchange movements	37	–
	Cash and cash equivalents at the end of the year	**10,224**	**10,183**

The notes on pages 44 to 59 form part of these financial statements.

Notes to the Financial Statements

1 Accounting policies

a) Basis of preparation

The Henderson Smaller Companies Investment Trust plc (the "Company") is a company incorporated and domiciled in the United Kingdom under the Companies Act 2006. The financial statements of the Company for the year ended 31 May 2016 have been prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. These comprise standards and interpretations approved by the International Accounting Standards Board ("IASB"), together with interpretations of the International Accounting Standards and Standing Interpretations Committee approved by the IFRS Interpretations Committee ("IFRS IC") that remain in effect, to the extent that IFRS have been adopted by the European Union.

The financial statements have been prepared on a going concern basis and on the historical cost basis, except for the revaluation of certain financial instruments held at fair value through profit or loss. The principal accounting policies adopted are set out below. These policies have been applied consistently throughout the year. Where presentational guidance set out in the Statement of Recommended Practice (the "SORP") for investment trusts issued by the Association of Investment Companies (the "AIC") in November 2014 is consistent with the requirements of IFRS, the Directors have sought to prepare the financial statements on a basis consistent with the recommendations of the SORP.

Accounting standards

(i) New and amended standards adopted by the Company

There were no new or amended standards adopted by the Company during the year.

(ii) New standards, amendments and interpretations issued but not effective for the current financial year and not early adopted by the Company

- IAS 1, 'Presentation of financial statements' (effective for annual periods beginning on or after 1 January 2015) – These amendments are as part of the IASB initiative to improve presentation and disclosure in financial reports, effective for annual periods beginning on or after 1 January 2016. The Company does not expect the amendments to IAS 1 to have a significant impact on the financial statements.
- IFRS 9, 'Financial instruments' (effective for annual periods beginning on or after 1 January 2018) – addresses the classification, measurement and recognition of financial assets and financial liabilities. IFRS 9 was issued in November 2009 and October 2010. It replaces the parts of IAS 39 that relate to the classification and measurement of financial instruments. IFRS 9 requires financial assets to be classified into two measurement categories: those measured as at fair value and those measured at amortised cost. The determination is made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument. For financial liabilities, the standard retains most of the IAS 39 requirements. The main change is that, in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than the income statement, unless this creates an accounting mismatch. The Company is yet to assess IFRS 9's full impact and intends to adopt IFRS 9 no later than the accounting period beginning on or after 1 January 2018, subject to endorsement by the EU.
- IAS 7, 'Statement of cash flows' (effective for annual periods beginning on or after 1 January 2017) – introduces an additional disclosure that will enable users of financial statements to evaluate changes in liabilities arising from financing activities, subject to endorsement by the EU. The Company is yet to assess the full impact of the amendments to IAS 7 on the financial statements but does not expect these to be significant.

(iii) New standards, amendments and interpretations issued but not effective for the current financial year and not relevant to the Company's operations.

A number of new standards, amendments and interpretations have been issued that are not effective for the current financial year end and not relevant to the Company's operations. They will therefore have no impact on the Company's financial statements when they become effective.

In addition, there are changes to a number of standards under the Annual Improvements to IFRSs 2012-2014 Cycle which are effective for annual periods beginning on or after 1 January 2016.

b) Going concern

The Company's shareholders are asked every three years to vote for the continuation of the Company. An ordinary resolution to this effect was put to the Annual General Meeting ("AGM") held on 4 October 2013 and passed by a substantial majority of the shareholders. The assets of the Company consist almost entirely of securities that are listed (or listed on AIM) and, accordingly, the Directors believe that the Company has adequate financial resources to continue in operational existence for at least twelve months from the date of approval of the financial statements. Having assessed these factors, the principal risks and other matters discussed in connection with the Viability Statement, the Board has decided that it is appropriate for the financial statements to be prepared on a going concern basis.

Notes to the Financial Statements (continued)

1 Accounting policies (continued)

c) Investments held at fair value through profit or loss

All investments are designated upon initial recognition as held at fair value through profit or loss. Investment transactions are accounted for on a trade date basis. Assets are de-recognised at the trade date of the disposal. Proceeds are measured at fair value, which is regarded as the proceeds of sale less any transaction costs. The fair value of the financial instruments is based on their quoted bid price at the balance sheet date, without deduction of the estimated future selling costs. Unquoted investments are valued by the Directors using primary valuation techniques such as earnings multiples, recent transactions and net assets. Where fair value cannot be reliably measured the investment will be carried at the previous reporting date value unless there is evidence that the investment has since been impaired, in which case the value will be reduced.

Changes in the fair value of investments held at fair value through profit or loss and gains and losses on disposal are recognised in the Statement of Comprehensive Income as "Gains or losses on investments held at fair value through profit or loss". Also included within this caption are transaction costs in relation to the purchase or sale of investments, including the difference between the purchase price of an investment and its bid price at the date of purchase.

d) Presentation of the Statement of Comprehensive Income

In order to better reflect the activities of an investment trust company, and in accordance with guidance issued by the Association of Investment Companies ("the AIC"), supplementary information which analyses the Statement of Comprehensive Income between items of a revenue and capital nature has been presented alongside the Statement of Comprehensive Income. In accordance with the Company's status as a UK investment company under section 833 of the Companies Act 2006, net capital returns are no longer prohibited to be distributed by way of dividend where authority is given within the Company's Articles of Association. Additionally, the net revenue is the measure the Directors believe appropriate in assessing the Company's compliance with certain requirements set out in section 1158 of the Corporation Tax Act 2010.

e) Income

Dividends receivable on equity shares are recognised as revenue for the year on an ex-dividend basis. Special dividends are treated as revenue return or as capital return, depending on the facts of each individual case. Interest is recognised using the effective interest rate method. Interest from debt securities is accounted for on an accruals basis.

Where the Company enters into a commitment to sub-underwrite an issue of securities in exchange for the receipt of commission, a derivative financial instrument is created. Any such derivatives are recognised initially at fair value. They are re-measured subsequently at fair value, with the related gains and losses being reflected in the Statement of Comprehensive Income. Net losses arising from these derivatives, where the actual or expected loss from taking up the securities underwritten exceeds the commission income, are allocated to the capital return. Net gains are allocated to the revenue return.

Income distributions from UK Real Estate Investment Trusts (UK REITs) will be split into two parts, a Property Income Distribution (PID) made up of rental revenue and a non-PID element, consisting of non-rental revenue. The PID element is subject to corporation tax as schedule A revenue, while the non-PID element will be treated as franked revenue.

f) Expenses

All expenses are accounted for on an accruals basis. The Board has determined that the capital return should reflect the indirect costs of earning capital returns. Since 1 June 2013, the Company has allocated 70% of its management fees and finance costs to the capital return of the Statement of Comprehensive Income with the remaining 30% being allocated to the revenue return.

All other administrative expenses are charged to the revenue return of the Statement of Comprehensive Income.

Any performance fees are charged wholly to the capital return.

Expenses which are incidental to the purchase or sale of an investment are recognised immediately in the capital return of the Statement of Comprehensive Income, and are included within the gains or losses on investments held at fair value through profit or loss.

Notes to the Financial Statements (continued)

1 Accounting policies (continued)

g) Taxation

The tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on the taxable profit for the period. Taxable profit differs from net profit 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 Company's liability for current tax is calculated using tax rates that were applicable at the balance sheet date.

The tax effect of different items of expenditure is allocated between the capital and the revenue using the Company's effective rate of tax for the year. 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. Investment trusts which have approval as such under section 1158 of the Corporation Tax Act 2010 are not liable for taxation on capital gains.

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.

h) Foreign currency

For the purposes of the financial statements, the results and financial position are expressed in pounds sterling, which is the functional currency and presentational currency of the Company. Sterling is the functional currency because it is the currency of the primary economic environment in which the Company operates.

Transactions recorded in overseas currencies during the year are translated into sterling at the appropriate daily exchange rates. Monetary assets and liabilities and investments held at fair value through profit or loss which are denominated in overseas currencies at the balance sheet date are translated into sterling at the exchange rates ruling at that date. Gains and losses arising on the retranslation of investments held at fair value through profit or loss are included within the "Gains or losses on investments held at fair value through profit or loss". Any foreign currency gains and losses are taken to capital in the Statement of Comprehensive Income.

i) Cash and cash equivalents

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

j) Borrowings

Interest-bearing bank loans, overdrafts, unsecured loan notes, Debenture Stock and Preference Stock are recorded initially at fair value, being the proceeds received, net of direct issue costs. They are subsequently measured at amortised cost. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accruals basis in the Statement of Comprehensive Income using the effective interest rate method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

The Preference Stock has been classified as a liability as it represents a contractual obligation on behalf of the Company to deliver to the stockholders a fixed and determinable amount at the date of redemption.

Notes to the Financial Statements (continued)

1 Accounting policies (continued)

k) Operating segments

Under IFRS 8, operating segments are considered to be components of an entity about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The Directors meet regularly to consider investment strategy and to monitor the Company's performance. The Fund Manager, who has been appointed to manage the Company's investments, attends all Board meetings at which investment strategy and performance are discussed.

The Directors consider that the Company has one operating segment, being the activity of investing in shares and securities primarily for capital appreciation in accordance with the Company's published investment objective. The Company operates within the United Kingdom.

l) Dividends payable to shareholders

Dividends payable to shareholders are recognised in the financial statements when they are paid or, in the case of final dividends, when they are approved by shareholders. Dividends are recorded in the Statement of Changes in Equity. Dividends can be paid from both realised capital profits and the revenue reserve.

m) Capital and reserves

Capital reserve arising on investments sold

The following are accounted for in this reserve:

- gains and losses on the disposals of investments;
- expenses and finance costs allocated to capital net of tax relief;
- realised foreign exchange differences of a capital nature; and
- costs of repurchasing ordinary share capital.

Capital reserve arising on revaluation of investments held

The following are accounted for in this reserve:

- increases and decreases in the valuation of investments held at the year end; and
- unrealised foreign exchange differences of a capital nature.

Revenue reserve

The revenue reserve represents accumulated revenue profits retained by the Company that have not currently been distributed to shareholders as a dividend.

Capital redemption reserve

The capital redemption reserve represents the nominal value of ordinary shares repurchased and cancelled.

n) Distributable reserves

The Company's capital reserve arising on investments sold (i.e. realised capital profits) and revenue reserve may be distributed by way of a dividend.

o) Share capital

Ordinary shares are classified as equity. Mandatorily redeemable preference shares are classified as liabilities. Incremental costs directly attributable to the issue of new ordinary shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Where the Company purchases its own equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company's equity holders until the shares are cancelled or reissued. Where such ordinary shares are subsequently reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Company's equity holders.

Share capital represents the nominal value of ordinary shares issued.

p) Key estimates and assumptions

Estimates and assumptions used in preparing the financial statements are reviewed on an ongoing basis and are based on historical experience and various other factors that are believed to be reasonable under the circumstances. The results of these estimates and assumptions form the basis of making judgements about carrying values of assets and liabilities that are not readily apparent from other sources.

There are no estimates and assumptions that may cause material adjustment to the carrying value of assets and liabilities as described in note 15.

Notes to the Financial Statements (continued)

2 Investment income

	2016 £'000	2015 £'000
Franked income from companies listed or quoted in the United Kingdom:		
Dividends	11,740	10,873
Special dividends	443	1,499
Unfranked income from companies listed or quoted in the United Kingdom:		
Dividends	914	411
Property income distributions	524	55
Total investment income	**13,621**	**12,838**

3 Other income

	2016 £'000	2015 £'000
Bank and other interest	1	2
Underwriting income (allocated to revenue)[1]	90	205
	91	**207**

1 None of the income receivable from sub-underwriting commitments was allocated to capital during the year (2015: £nil).

4 Management and performance fees

	2016			2015		
	Revenue return £'000	Capital return £'000	Total return £'000	Revenue return £'000	Capital return £'000	Total return £'000
Management fee	565	1,319	1,884	538	1,256	1,794
Performance fee	–	–	–	–	2,000	2,000
	565	**1,319**	**1,884**	**538**	**3,256**	**3,794**

A summary of the management agreement is given on pages 4 and 5 of the Strategic Report.

5 Other expenses

	2016 £'000	2015 £'000
Directors' fees (see the Directors' Remuneration Report on pages 27 and 28)	130	114
Auditors' remuneration for the audit of the Company and the financial statements	25	24
Other professional fees	70	55
FCA and London Stock Exchange fees	30	29
Registration costs	13	13
Annual and half year reports and shareholder circulars: printing and distribution	21	21
Insurances	5	7
AIC subscriptions	21	22
Custody and other bank charges	29	27
Bank facilities: commitment fees	28	50
Charitable donations	5	5
Depositary charges[1]	49	41
Other expenses payable to the management company[2]	33	41
Share price listings in newspapers and websites	7	6
Other expenses[3]	21	17
	487	**472**

1 Depository appointed on 22 July 2014 to meet the requirements of the AIFMD
2 Other expenses payable to the management company ("Henderson") relate to sales and marketing services
3 Other expenses includes VAT payable on Auditors' remuneration

All transactions with Directors are disclosed in the Directors' Remuneration Report and are related party transactions.

All the above expenses include VAT where VAT is applied to them except for Auditors' remuneration (see footnote 3 above).

Notes to the Financial Statements (continued)

6 Finance costs

	2016			2015		
	Revenue return £'000	Capital return £'000	Total return £'000	Revenue return £'000	Capital return £'000	Total return £'000
Bank overdraft and loan interest	118	276	394	159	371	530
Interest on unsecured loan notes	7	18	25	–	–	–
Interest on debentures	630	1,470	2,100	630	1,470	2,100
	755	**1,764**	**2,519**	**789**	**1,841**	**2,630**

7 Taxation

a) Analysis of charge for the year

	2016			2015		
	Revenue return £'000	Capital return £'000	Total return £'000	Revenue return £'000	Capital return £'000	Total return £'000
Overseas tax suffered	9	–	9	12	–	12
Current and total tax charge for the year	**9**	**–**	**9**	**12**	**–**	**12**

b) Factors affecting the tax charge for the year

UK corporation tax is charged at 20% (2015: effective rate 20.83%). Approved investment trusts are exempt from corporation tax on chargeable gains made by the investment trust.

The tax assessed for the year is lower than the average standard rate of corporation tax in the UK of 20% (2015: 20.83%) for the year ended 31 May 2016.

	2016			2015		
	Revenue return £'000	Capital return £'000	Total return £'000	Revenue return £'000	Capital return £'000	Total return £'000
Net profit/(loss) on ordinary activities before taxation	**11,905**	**(18,679)**	**(6,774)**	**11,246**	**84,397**	**95,643**
Corporation tax at 20% (2015: 20.83%)	2,381	(3,736)	(1,355)	2,343	17,579	19,922
Effects of:						
Non-taxable UK dividends	(2,442)	–	(2,442)	(2,577)	–	(2,577)
Non-taxable overseas dividends	(183)	–	(183)	(86)	–	(86)
Excess management expenses and loan deficits	244	616	860	319	1,062	1,381
Overseas withholding tax	9	–	9	12	–	12
Disallowed expenses	–	–	–	1	–	1
Non-taxable capital items	–	3,120	3,120	–	(18,641)	(18,641)
Current and total tax charge for the year	**9**	**–**	**9**	**12**	**–**	**12**

c) Provision for deferred taxation

No provision has been made for deferred tax on income outstanding at the end of the year and this will be covered by unrelieved business charges.

Due to the Company's status as an investment trust, and the intention to continue meeting the conditions required to maintain approval of such status in the foreseeable future, the Company has not provided for deferred tax on capital gains or losses arising on the revaluation or disposal of investments.

d) Factors that may affect future tax charges

The Company has not recognised a deferred tax asset of £14,821,000 (2015: £13,931,000) arising as a result of having unutilised management expenses and deficits on loan relationships. These expenses will only be utilised if the tax treatment of the Company's income and chargeable gains changes or if the Company's investment profile changes.

Notes to the Financial Statements (continued)

8 Earnings per ordinary share

The earnings per ordinary share figure is based on the net loss for the year of £6,783,000 (2015: gain of £95,631,000) and on 74,701,796 (2015: 74,701,796) ordinary shares, being the weighted average number of ordinary shares in issue during the year.

The earnings per ordinary share figure detailed above can be further analysed between revenue and capital, as below:

The Company has no securities in issue that could dilute the return per ordinary share. Therefore the basic and diluted earnings per ordinary share are the same.

	2016 £'000	2015 £'000
Net revenue profit	11,896	11,234
Net capital (loss)/profit	(18,679)	84,397
Net total (loss)/profit	**(6,783)**	**95,631**
Weighted average number of ordinary shares in issue during the year	74,701,796	74,701,796

	2016 pence	2015 pence
Revenue earnings per ordinary share	15.92	15.04
Capital earnings per ordinary share	(25.00)	112.98
Total earnings per ordinary share	**(9.08)**	**128.02**

9 Dividends

	Record Date	Pay Date	2016 £'000	2015 £'000
Final dividend: 10.0p (2014: 8.0p) for the year ended 31 May 2015	21 September 2015	9 October 2015	7,470	5,976
Interim dividend: 4.0p (2015: 3.5p) for the year ended 31 May 2016	15 February 2016	4 March 2016	2,988	2,615
			10,458	**8,591**

The final dividend of 10.0p per ordinary share in respect of the year ended 31 May 2015 was paid on 9 October 2015 to shareholders on the register of members at the close of business on 21 September 2015. The dividend paid amounted to £7,470,000 in total.

Subject to approval at the Annual General Meeting, the proposed final dividend of 11.0p per ordinary share will be paid on 30 September 2016 to shareholders on the register of members at the close of business on 2 September 2016.

The proposed final dividend for the year ended 31 May 2016 has not been included as a liability in these financial statements. Under IFRS, the final dividend is not recognised until approved by the shareholders. All dividends have been paid or will be paid out of revenue profits.

The total dividends payable in respect of the financial year which form the basis of the test under section 1158 of the Corporation Tax Act 2010 are set out below:

	2016 £'000	2015 £'000
Revenue available for distribution by way of dividends for the year	11,896	11,234
Interim dividend for the year ended 31 May 2016: 4.0p (2015: 3.5p) per ordinary share	(2,988)	(2,615)
Final dividend for the year ended 31 May 2015: 10.0p (based on 74,701,796 shares in issue at 3 August 2015)	–	(7,470)
Proposed final dividend for the year ended 31 May 2016: 11.0p (based on 74,701,796 shares in issue at 9 August 2016)	(8,217)	–
Retained revenue for year	**691**	**1,149**

Notes to the Financial Statements (continued)

10 Investments held at fair value through profit or loss

	2016 £'000	2015 £'000
Cost at start of year	356,478	300,392
Investment holding gains at start of year	249,298	219,160
Valuation at start of year	**605,776**	**519,552**
Movements in the year:		
Acquisitions at cost	158,484	135,283
Disposals at cost	(109,452)	(79,197)
Movement in investment holding gains	(58,881)	30,138
Valuation at end of year	**595,927**	**605,776**
Cost at end of year	405,510	356,478
Investment holding gains	190,417	249,298
Valuation at end of year	**595,927**	**605,776**

Purchase and sale transaction costs for the year ended 31 May 2016 were £543,000 and £141,000 respectively (2015: transaction costs of purchases £391,000; transaction costs of sales £144,000). These comprise mainly stamp duty and commission.

Analysis of investments at fair value

	2016 £'000	2015 £'000
Equity investments:		
Listed on London Stock Exchange	514,187	551,965
Listed on Alternative Investment Market	81,740	53,811
	595,927	**605,776**

All the investments are listed in the United Kingdom. The above categories are based on information obtained from the Stock Exchange Daily Official list.

Total capital gains from investments

	2016 £'000	2015 £'000
Gains on the sale of investments based on historical cost	43,248	59,356
Revaluation gains recognised in previous years	(44,581)	(43,669)
(Losses)/gains on investments sold in the year based on the carrying value at the previous balance sheet date	**(1,333)**	**15,687**
Investment holding (losses)/gains	(14,300)	73,807
Exchange gains	37	–
(Losses)/gains on investments held at fair value through profit or loss	**(15,596)**	**89,494**

All capital (losses)/gains are from investments that are listed (or listed on AIM) in the United Kingdom.

Notes to the Financial Statements (continued)

11 Substantial interests

The Company held interests of 3% or more of any class of share capital in four investee companies (2015: three investee companies). These investments are not considered by the Directors to be significant in the context of these financial statements.

	Valuation £'000	% of voting rights
e2v Technologies	14,418	3.3
WYG	4,389	4.8
Digital Barriers	2,668	3.8
Koovs	2,299	4.0

12 Receivables

	2016 £'000	2015 £'000
Securities sold for future settlement	670	731
Prepayments and accrued income	1,942	2,003
	2,612	**2,734**

13 Payables

	2016 £'000	2015 £'000
Securities purchased for future settlement	437	679
Performance fee	–	2,000
Accruals and deferred income	354	500
	791	**3,179**

14 Financial liabilities

	2016 £'000	2015 £'000
Debenture Stock:		
10.5% Debenture Stock 2016 (redeemed at par on 31 May 2016)	–	20,000
Unsecured Loan Notes:		
3.33% Unsecured Loan Notes 2036 (redeemable at par on 23 May 2036)	29,804	–
Preference Stock:		
4,257 Preference Stock units of £1 each (2015: 4,257)	4	4
	29,808	**20,004**

The Preference Stock Units carry the right to receive a non-cumulative dividend at a final rate of 0.001% payable on 1 June each year. On a winding-up of the Company, preference stockholders are entitled to repayment of the capital paid up thereon. The Preference Stock does not entitle the holder to attend or vote at any General Meeting of the Company except where the dividend is six months in arrears or on a resolution to liquidate the Company.

On 31 May 2016, the Company redeemed the £20,000,000 Debenture Stock at par.

On 23 May 2016, the Company issued £30,000,000 (nominal) 3.33% unsecured loan notes, net of issue costs totalling £196,000. The issue costs will be amortised over the life of the notes.

Notes to the Financial Statements (continued)

15 Risk management policies and procedures

The Directors manage investment risk principally through setting an investment policy (that is approved by shareholders) which incorporates risk parameters (see page 4), by contracting management of the Company's investments to an investment manager (Henderson) under a contract which incorporates appropriate duties and restrictions and by monitoring performance in relation to these. The Board's relationship with Henderson is discussed on page 31. Internal control and the Board's approach to risk is also on page 31. There have been no material changes to the management or nature of the Company's investment risks from the prior year.

The main risks arising from the Company's pursuit of its investment objective are market risk, credit risk and liquidity risk. The effects of these can also be increased by gearing.

The Board and Henderson co-ordinate the Company's risk management and there are various risk management systems in place as detailed below:

- Straight-through processing via a deal order and management system ("OMS") is utilised for listed securities.
- Portfolio modelling and investment management functions (including order-raising, dealing and trade execution) are performed using one of, or a combination of, the following third-party software applications: Charles River Development OMS and/or Imagine.
- Fund pricing and accounting services are outsourced to a third-party administrator (currently BNP Paribas Securities Services) which utilises Hiportfolio software.
- The IT tools to which the Henderson risk, compliance and operations teams have access for independent monitoring and risk measurement purposes include:
  - Charles River Compliance module for investment restrictions monitoring;
  - ArcLogics operational risk database;
  - RiskMetrics, UBS Delta, Style Research, Finanalytica and Barra Aegis for market risk measurement;
  - Bloomberg for market data and price-checking; and
  - Hiportfolio for portfolio holdings and valuations.

a) Market risk

The fair value of a financial instrument held by the Company may fluctuate due to changes in market prices. This market risk comprises market price risk (see note 15 (b)), currency risk (see note 15 (c)) and interest rate risk (see note 15 (d)). The Board reviews and agrees policies for managing these risks. Henderson assesses the exposure to market risk when making each investment decision and monitors the overall level of market risk on the whole of the investment portfolio on an ongoing basis.

b) Market price risk

Market price risk (i.e. changes in market prices other than those arising from interest rate risk or currency risk) may affect the fair value of the investments. The Company's investments are susceptible to market price risk arising from uncertainties about the future prices of the investments.

Management of the risk

The Board manages the risks inherent in the investment portfolio by ensuring full and timely access to relevant information from Henderson. The Board regularly reviews investment performance. The Board monitors Henderson's compliance with the Company's objectives and is directly responsible for investment strategy.

The Company's exposure to changes in market prices at 31 May 2016 on its equity investments was £595,927,000 (2015: £605,776,000).

Concentration of exposure to market price risk

An analysis of the Company's investments is shown on pages 14 and 15 and a sector analysis is set out on page 8. At 31 May 2016 all the investments were in companies listed or quoted in London, most of them being companies established in and operating from the United Kingdom. Accordingly, there is a concentration of exposure to the UK, although it is recognised that an investment's country of domicile or of listing does not necessarily equate to its exposure to the economic conditions in that country.

Notes to the Financial Statements (continued)

15 Risk management policies and procedures (continued)

Market price risk sensitivity

The sensitivity of (a) the return after taxation for the year and (b) the Company's net assets to an increase or decrease of 25% in the fair values of the Company's investments at each balance sheet date is given below. This level of change is considered to be reasonably possible, based on observation of current market conditions.

The impact of a 25% increase in the value of the investments on the revenue return as at 31 May 2016 is a decrease of £157,000 (2015: £159,000) and on the capital return is an increase of £148,617,000 (2015: £151,073,000). Accordingly, the total impact on shareholders' funds is an increase of £148,460,000 (2015: £150,914,000).

The impact of a 25% decrease in the value of the investments on the revenue return as at 31 May 2016 is an increase of £157,000 (2015: £159,000) and on the capital return is a decrease of £148,617,000 (2015: £151,073,000). Accordingly, the total impact is a decrease of £148,460,000 (2015: £150,914,000).

c) Currency risk

The Company is not itself materially exposed to currency risk, although some of the investments will be in companies that have operations that involve currency risk.

As at 31 May 2016, the Company did not hold any non-sterling denominated investments (2015: nil).

d) Interest rate risk

Interest rate movements may affect:

- the level of income receivable from cash at bank and on deposit; and
- the interest payable on the Company's short term borrowings.

Interest rate changes may also have an impact on the market value of the Company's equity investments. In particular, the effect of interest rate changes on the earnings of companies held within the portfolio may have a significant impact on the valuations of those companies.

Management of the risk

The possible effects on the fair value of the investments that could arise as a result of changes in interest rates are taken into account when making investment decisions and borrowing decisions. The Company rarely holds significant cash balances but finances part of its investment activity through borrowings at levels approved and monitored by the Board. At 31 May 2016 the Company had committed bank borrowing facilities for a total of £32.1 million; borrowings are drawn down for short periods at rates of interest that are determined by reference to the market rates applicable at the time of borrowing.

Interest rate exposure

The Company's financial liabilities at 31 May 2016 that give exposure to fixed interest rate risk are set out in note 14.

The exposure to floating interest rates can be found on the Balance Sheet (cash and cash equivalents and bank loans).

These amounts are not necessarily representative of the exposure to interest rates during the year, as the level of exposure changes as investments are made, borrowings are drawn down or repaid, and the mix of borrowings subject to floating or to fixed interest rates changes.

Interest rate sensitivity

The Company is not materially exposed to changes in interest rates. As at 31 May 2016 the Company's bank facility allowed borrowings to a maximum of £40 million the interest rate exposure on which is 0.80% plus LIBOR; the interest payable on the Company's £30 million issue of unsecured loan notes is fixed at 3.33%.

Notes to the Financial Statements (continued)

15 Risk management policies and procedures (continued)

e) Liquidity risk

This is the risk that the Company will encounter difficulty in meeting obligations associated with its financial liabilities.

Management of the risk

Liquidity risk is not significant as the majority of the Company's assets are investments in quoted equity securities that are readily realisable. The Company has borrowed £30 million by its issue in 2016 of 3.33% Unsecured Loan Notes 2036. The Company is able to draw short term borrowings of up to £40 million from its committed borrowing facility which expires on 10 February 2017 with National Australia Bank. There were borrowings of £32,107,000 drawn down under the facility at 31 May 2016 (2015: £32,201,000).

Accordingly, the Company has access to borrowings of up to £70 million: the £30 million of fixed debt represented by the issue of Unsecured Loan Notes and a committed bank facility of £40 million.

The Board gives guidance to Henderson as to the maximum amount of the Company's resources that should be invested in any one company. The policy is that the Company should remain fully invested in normal market conditions and that short term borrowings should be used to fund short term cash requirements.

Liquidity risk exposure

The remaining contractual maturities of the financial liabilities at 31 May 2016, based on the earliest date on which payment could be required, was as follows:

	2016			2015	
	Due within 1 year £'000	Due between 1 and 5 years £'000	Due more than 5 years £'000	Due within 1 year £'000	Due between 1 and 5 years £'000
Debenture Stock[1]	–	–	–	22,100	–
Preference Stock[2]	–	–	–	–	–
Unsecured loan notes[3]	999	3,996	44,985	–	–
Bank loans and interest	32,214	–	–	32,300	–
Payables	748	–	–	3,119	–
	33,961	**3,996**	**44,985**	**57,519**	**–**

1 The amounts due include Debenture Stock interest
2 See also note 14 on page 52. The Company has in issue Preference Stock without a set redemption date with a total par value of £4,000 (2015: £4,000) which has a negligible ongoing finance cost
3 The amounts due include unsecured loan notes interest

f) Credit risk

The failure of the counterparty to a transaction to discharge its obligations under that transaction could result in the Company suffering a loss.

Management of the risk

The risk is not significant, and is managed as follows:

- investment transactions are carried out with a large number of brokers, whose credit standard is reviewed regularly by Henderson, and limits are set on the amount that may be due from any one broker; and
- cash at bank is held only with reputable banks with high quality external credit ratings.

In summary, the maximum exposure to credit risk at 31 May 2016 was to cash and cash equivalents of £10,224,000 (2015: £10,183,000), and to receivables of £2,612,000 (2015: £2,734,000) (see note 12).

None of the Company's financial assets are past their due date or impaired.

Notes to the Financial Statements (continued)

15 Risk management policies and procedures (continued)

g) Fair values of financial assets and financial liabilities

The investments are held at fair value through profit or loss. All the net current liabilities are held in the Balance Sheet at a reasonable approximation of fair value. At 31 May 2016 the Debenture Stock had been repaid and so there was no fair value (2015: £21,511,000). The fair value of the Debenture Stock at 31 May 2015 was calculated using the prices quoted on the exchange on which the instrument trades. The Debenture Stock is carried in the Balance Sheet at par. At 31 May 2016 the fair value of the Preference Stock was £4,000 (2015: £4,000). The fair value of the Preference Stock is estimated using the prices quoted on the exchange on which the investment trades. The Preference Stock is carried in the Balance Sheet at par.

The Unsecured Loan Notes are carried in the Balance Sheet at par less the issue expenses which are amortised over the life of the notes. The fair value of the Unsecured Loan Notes is estimated to be its par value.

h) Fair value hierarchy disclosures

The table below sets out fair value measurements using the IFRS 13 fair value hierarchy.

Categorisation within the hierarchy has been determined on the basis of the lowest level of input that is significant to the fair value measurement of the relevant asset, as follows:

Level 1: valued using quoted prices in active markets for identical assets.

Level 2: valued by reference to valuation techniques using observable inputs other than quoted prices.

Level 3: valued by reference to valuation techniques using inputs that are not based on observable market data.

The valuation techniques used by the Company are explained in note 1(c) on page 45.

Fair value hierarchy – 2016

	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
Equity investments	595,927	–	–	595,927
	595,927	**–**	**–**	**595,927**

Fair value hierarchy – 2015

	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
Equity investments	605,776	–	–	605,776
	605,776	**–**	**–**	**605,776**

There have been no transfers during the year between any of the levels.

i) Capital management policies and procedures

The Company's capital management objectives are:

- to ensure that it will be able to continue as a going concern; and
- to secure long term capital growth for the shareholders by investment in quoted securities in the UK.

This is to be achieved through an appropriate balance of equity capital and gearing. The Company's policy is that its borrowings must not exceed 30% of the shareholders' funds.

The Company's total capital at 31 May 2016 was £608,191,000 (2015: £615,526,000) comprising £32,107,000 (2015: £32,201,000) of unsecured bank loans, £nil (2015: £20,000,000) of Debenture Stock, £30,000,000 (2015: £nil) of Unsecured Loan Notes, £4,000 (2015: £4,000) of Preference Stock and £546,080,000 (2015: £563,321,000) of equity share capital and reserves.

At 31 May 2016 the Company had a two year revolving credit facility with National Australia Bank. The Company had drawn down £32,107,000 under these facilities as at 31 May 2016. The Company was fully compliant with the terms of the facility, as it existed, for the period 1 June 2015 to the date of this Annual Report.

Notes to the Financial Statements (continued)

16 Share capital

	2016 £'000	2015 £'000
Allotted, issued, authorised and fully paid:		
74,701,796 ordinary shares of 25p each (2015: 74,701,796)	18,676	18,676

During the year the Company made no purchases of its own issued ordinary shares (2015: nil) at a cost of £nil (2015: £nil). Since 31 May 2016 the Company has not purchased any ordinary shares.

17 Capital redemption reserve and capital reserve

2016	Capital redemption reserve £'000	Capital reserve arising on revaluation of investments held £'000	Capital reserve arising on investments sold £'000	Capital reserves £'000
At 1 June 2015	26,745	249,298	252,676	501,974
Transfer on disposal of investments (see note 10)	–	(44,581)	44,581	–
Net capital gains for the year	–	(14,300)	(1,333)	(15,633)
Exchange gains	–	–	37	37
Expenses charged to capital	–	–	(3,083)	(3,083)
At 31 May 2016	**26,745**	**190,417**	**292,878**	**483,295**

2015	Capital redemption reserve £'000	Capital reserve arising on revaluation of investments held £'000	Capital reserve arising on investments sold £'000	Capital reserves £'000
At 1 June 2014 as previously reported	26,745	218,507	199,070	417,577
Adjustment for investments previously written down to nil value	–	653	(653)	–
At 1 June 2014 adjusted	**26,745**	**219,160**	**198,417**	**417,577**
Transfer on disposal of investments (see note 10)	–	(43,669)	43,669	–
Net capital gains for the year	–	73,807	15,687	89,494
Expenses charged to capital	–	–	(5,097)	(5,097)
At 31 May 2015	**26,745**	**249,298**	**252,676**	**501,974**

18 Revenue reserve

	2016 £'000	2015 £'000
At 1 June	15,926	13,283
Ordinary dividend paid	(10,458)	(8,591)
Revenue profit for the year	11,896	11,234
At 31 May	**17,364**	**15,926**

Notes to the Financial Statements (continued)

19 Net asset value per ordinary share

The net asset value per ordinary share is based on the net assets attributable to the ordinary shares of £546,080,000 (2015: £563,321,000) and on 74,701,796 ordinary shares in issue at 31 May 2016 (2015: 74,701,796).

An alternative net asset value per ordinary share can be calculated by deducting from the total assets less current liabilities of the Company, the Preference Stock, Debenture Stock and the Unsecured Loan Notes at their market (or fair) values rather than at their par (or book) values (see note 15 (g) on page 56). The net asset value per ordinary share at 31 May 2016 calculated on this basis was 731.0p (2015: 752.1p). Since the redemption of the Debenture Stock, these net asset values are identical because there is no difference between the carrying value and fair value of the remaining debt liabilities.

The Company has no securities in issue that could dilute the net asset value per ordinary share.

The movement during the year of the net assets attributable to the ordinary shares was as follows:

	2016 £'000	2015 £'000
Net assets attributable to the ordinary shares at 1 June	563,321	476,281
Net (losses)/gains for the year	(6,783)	95,631
Ordinary dividend paid in the year	(10,458)	(8,591)
Net assets attributable to the ordinary shares at 31 May	**546,080**	**563,321**

20 Capital commitments and contingent liabilities

Capital commitments
There were no capital commitments as at 31 May 2016 (2015: £nil).

Contingent liabilities
There were no contingent liabilities in respect of sub-underwriting commitments as at 31 May 2016 (2015: £nil).

21 Transactions with the Manager and Related Parties

Under the terms of an agreement effective from 22 July 2014 (which replaced the agreement dated 29 September 2006 in order to reflect the appointment of an Alternative Investment Fund Manager in accordance with the requirements of the Alternative Investment Fund Managers Directive), the Company has appointed a wholly owned subsidiary company of Henderson Group plc ("Henderson") to provide investment management, accounting, secretarial and administrative services. Henderson has contracted with BNP Paribas Securities Services to provide accounting and administration services.

Details of the fee arrangements for these services are given on pages 4 and 5. The management fees payable to Henderson under the management agreement in respect of the year ended 31 May 2016 were £1,884,000 (2015: £1,794,000) of which £152,000 was a prepayment at 31 May 2016 (2015: accrual of £310,000). VAT is no longer payable on management (including performance) fees.

The performance fee payable to Henderson in respect of the year ended 31 May 2016 is £nil (2015: £2,000,000).

In addition to the above services, Henderson has provided the Company with sales and marketing services. The total fees paid or payable for these services for the year ended 31 May 2016 amounted to £33,000 (2015: £41,000 including VAT), of which £10,000 was outstanding at 31 May 2016 (2015: £19,000).

The compensation payable to key management personnel in respect of short term employment benefits was £130,000. The disclosure relates wholly to the fees of £130,000 payable to the Directors in respect of the year (2015: £114,000); the Directors are all non-executive and receive no other compensation. The Directors' Remuneration Report on pages 27 and 28 provides more detail.
The Company has no employees.

Notes to the Financial Statements (continued)

22 Value Added Tax on management fees

A decision of the European Court of Justice in 2007 that Value Added Tax ("VAT") should not be charged on fees paid for management services provided to investment trust companies, resulted in the Company receiving, over the three financial years up to 31 May 2010, refunds of VAT totalling £2,943,000 (relating to management fees paid during the periods 1990 to 1996 and 2000 to 2007) and £985,000 of simple interest on those VAT refunds. The write-backs of VAT were allocated between revenue return and capital return according to the allocation of the amounts originally paid. The interest paid by HM Revenue & Customs ("HMRC") on the VAT recovered was included in other income.

There remain outstanding claims relating to the period 1996 to 2000 and claims for compound interest from 1990 onwards. No amounts have been recognised in respect of these claims as it is currently uncertain whether any further amounts will be recovered. The Company is a participant in on-going action against HMRC to recover these amounts.

23 Post balance sheet events

On 23 June 2016 the UK electorate voted to leave the European Union. This decision commences a process that is likely to take a minimum of two years to complete, and during this time the UK remains a member of the European Union. There will be a resulting period of uncertainty for the UK economy with increased volatility expected in financial markets. This does not impact the fair value of assets and liabilities reported at the balance sheet date of 31 May 2016.

As at the close of business on the balance sheet date, the net asset value per ordinary share was 731.0p. The net asset value per ordinary share on 5 August 2016 was 713.5p. This represents a decrease of 2.4% compared to the year end net asset value per ordinary share.

General Shareholder Information

AIFMD Disclosures

In accordance with the Alternative Investment Fund Managers Directive ("AIFMD"), information in relation to the Company's leverage and remuneration of Henderson, as the Company's Alternative Investment Fund Manager ("AIFM") are required to be made available to investors. These disclosures, including those on the AIFM's remuneration policy, are contained in a Key Investor Information Document (KIID) which can be found on the Company's website **www.hendersonsmallercompanies.com**

BACS

Dividends can be paid by means of BACS (Bankers' Automated Clearing Services); mandate forms for this purpose are available from the Registrar. Alternatively, shareholders can write to the Registrar (the address is given on page 17) to give their instructions; these must include the bank account number, the bank account title and the sort code of the bank to which payments are to be made.

Common Reporting Standard

With effect from 1 January 2016 new tax legislation under The Organisation for Economic Co-operation and Development Common Reporting Standard for Automatic Exchange of Financial Account Information is being introduced. The legislation will require the Company to provide personal information to HMRC on certain investors who purchase shares in investment trusts. This information will have to be provided annually to the local tax authority of the tax residencies of a number of non-UK based certificated shareholders and corporate entities.

Equality Act 2010

Copies of this report and other documents issued by the Company are available from the Corporate Secretary. If needed, copies can be made available in a variety of formats, including Braille or larger type as appropriate.

You can contact the Registrar, Computershare Investor Services PLC, which has installed textphones to allow speech and hearing impaired people who have their own textphone to contact them directly, without the need for an intermediate operator by dialling 0370 702 0005. Specially trained operators are available during normal business hours to answer queries via this service. Alternatively, if you prefer to go through a "typetalk" operator (provided by the Royal National Institute for Deaf People) dial 18001 followed by the number you wish to dial.

History

The Company was incorporated under the Companies Acts 1862 to 1886 on 16 December 1887 with the name of The Trustees, Executors and Securities Insurance Corporation, Limited. The name was changed in August 1917 to The Trustees Corporation Limited, in April 1982 to TR Trustees Corporation PLC, in October 1990 to TR Smaller Companies Investment Trust PLC and in September 1997 to The Henderson Smaller Companies Investment Trust plc. Whilst the Trustee Department operated until June 1978, the principal business of the Company has been that of an investment trust company.

ISA

The Company intends to continue to manage its affairs in order to qualify as an eligible investment for a stocks and shares ISA.

Non-Mainstream Pooled Investments (NMPI) Status

The Company currently conducts its affairs so that its ordinary shares of 25p each can be recommended by IFAs to ordinary retail investors in accordance with the Financial Conduct Authority's ("FCA") rules in relation to non-mainstream investment products and intends to continue to do so for the foreseeable future. The shares are excluded from the FCA's restrictions which apply to non-mainstream investment products because they are shares in an investment trust.

Performance Details/Share Price information

Details of the Company's share price and NAV per share can be found on the website **www.hendersonsmallercompanies.com**. The Company's NAV is published daily.

Shareholder Details

Shareholders who hold their shares in certificated form can check their shareholding with the Registrar, via **www.computershare.com**. Please note that to gain access to your details on the Computershare site you will need the holder reference number shown on your share certificate.

Share Price Listings

The market price of the Company's ordinary shares is published daily in The Financial Times, which also shows figures for the estimated net asset value ("NAV") per share and discount.

Warning to shareholders

Many companies are aware that their shareholders have received unsolicited phone calls or correspondence concerning investment matters. These are typically from overseas based "brokers" who target UK shareholders offering to sell them what often turn out to be worthless or high risk shares in US or UK investments. They can be very persistent and extremely persuasive. Shareholders are therefore advised to be very wary of any unsolicited advice, offers to buy shares at a discount or offers of free company reports.

Please note that it is very unlikely that either the Company or the Company's Registrar, Computershare Investor Services PLC, would make unsolicited telephone calls to shareholders and that any such calls would relate only to official documentation already circulated to shareholders and never in respect of investment "advice".

If you are in any doubt about the veracity of an unsolicited phone call, please call the Corporate Secretary at the number provided on page 17.

The Henderson Smaller Companies Investment Trust plc
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