

THE HENDERSON SMALLER COMPANIES INVESTMENT TRUST PLC

Strategic Report 2016



MANAGED BY

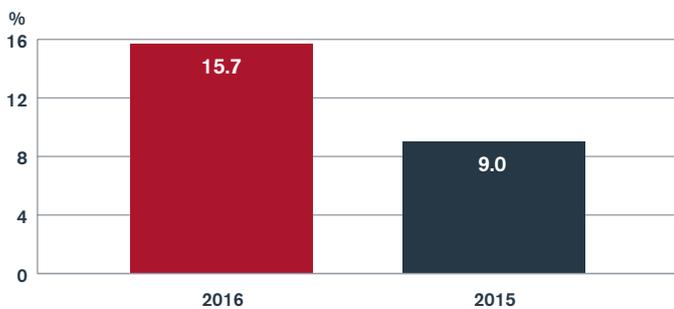
Henderson
GLOBAL INVESTORS

Performance Highlights

Total Return Performance over the year to 31 May 2016



Discount at year end⁴



Discount⁵



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

Performance Highlights (continued)

NAV per share at year end

2016 **731.0p** 2015 **754.1p**

Discount at year end

2016 **15.7%** 2015 **9.0%**

Share price at year end

2016 **616.5p** 2015 **686.0p**

Gearing at year end

2016 **9.1%** 2015 **7.5%**

Dividend for year

2016 **15.0p**⁸ 2015 **13.5p**

Dividend yield⁹

2016 **2.4%** 2015 **2.0%**

Ongoing Charge¹⁰

2016 **0.44%** 2015 **0.46%**

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

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.

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).

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

Historical Performance and Financial Information

Total Return Performance over the 10 years to 31 May 2016



Financial Information

At 31 May	Net assets £'000	NAV per ordinary share		Mid- market price per ordinary share p	Discount		Profit/ (loss) for year £'000	Revenue return p	Capital return p	Total return p	Dividend p	Expenses ⁴ %
		With debt at par p	With debt at market value p		With debt at par %	With debt at market value %						
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)
2016⁵	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

Portfolio Information

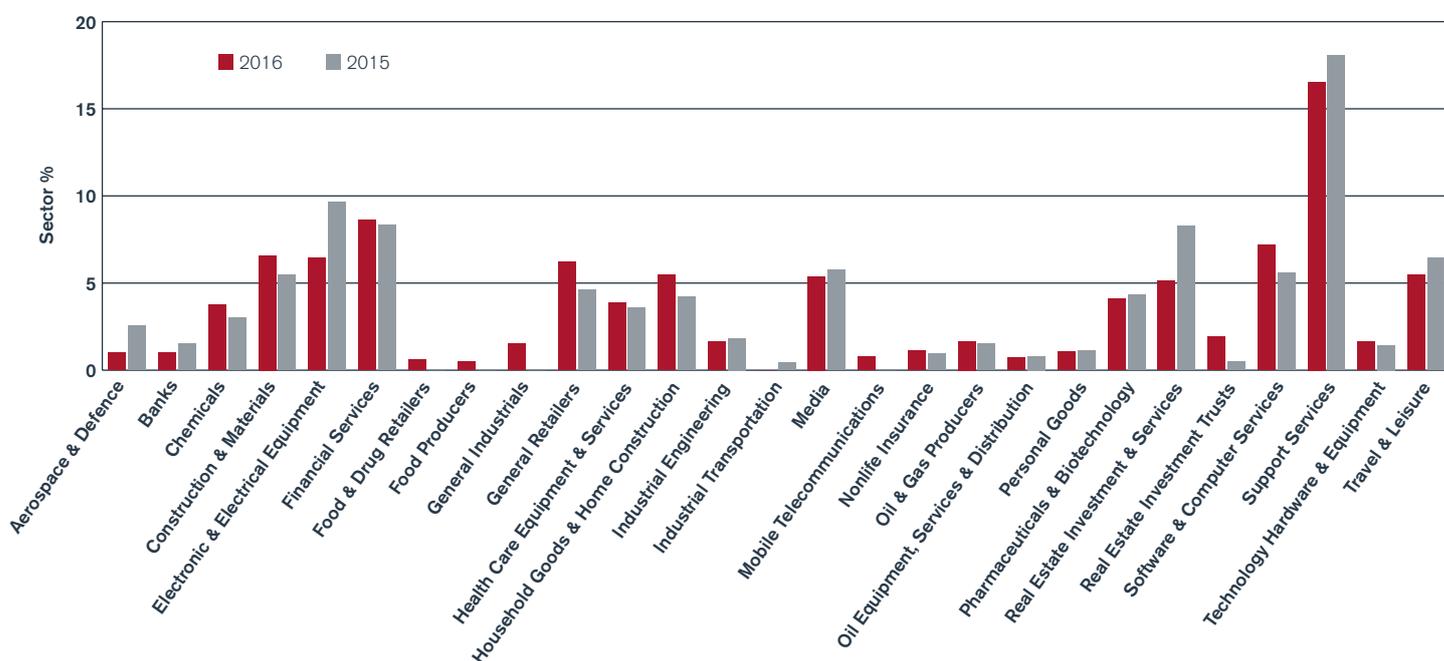
Performance Attribution

	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

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 Skril 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.

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

¹Included 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.

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'être 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.

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.

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

Investment Portfolio at 31 May 2016 (continued)

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

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.

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

Depository 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

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

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

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

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 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.

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.

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.

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.

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.

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
Registered as an investment company in England and Wales
Registration Number 25526
Registered Office 201 Bishopsgate, London EC2M 3AE

ISIN number/SEDOL Ordinary Shares: GB0009065060/0906506
London Stock Exchange (TIOM) Code: HSL
Global Intermediary Identification Number (GIIN): WZD8S799999.SL.826
Legal Entity Identifier (LEI): 213800NE2NCQ67M2M998

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The Association of
Investment Companies



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