



# JPMorgan Fleming European Fledgeling Investment Trust plc

ANNUAL REPORT & ACCOUNTS – YEAR ENDED 31st MARCH 2006

# Features

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## OBJECTIVE

Capital growth from smaller European companies (excluding the UK).

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## POLICIES

To invest in a diversified portfolio of smaller companies in Europe, excluding the United Kingdom.

To manage liquidity and borrowings to increase potential returns to shareholders.

To emphasise capital growth rather than income. Shareholders should not therefore expect a dividend.

It should be noted that the Company invests in smaller companies which tend to be more volatile than larger companies and the Company's shares should therefore be regarded as carrying greater than average risk.

To invest no more than 15% of gross assets in other UK listed investment companies (including investment trusts).

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## BENCHMARK

The performance benchmark is the HSBC Smaller European Companies (ex UK) Index in Sterling terms.

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## CAPITAL STRUCTURE

The Company has an authorised share capital of 280,000,000 ordinary shares of 25p each, of which 52,781,517\* were in issue at the year end.

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## MANAGEMENT COMPANY

The Company employs JPMorgan Asset Management (UK) Limited (JPMAM) to manage its assets.

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## AITC

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

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\*includes 175,000 shares held in treasury (2005: nil)

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# Results

**+72.0%** Return to shareholders<sup>1</sup> (2005: +50.3%)

**+68.6%** Return on net assets<sup>2</sup> (2005: +41.4%)

**+51.6%** Benchmark return<sup>3,4</sup> (2005: +31.8%)

## Long Term Performance

	Return to shareholders <sup>1</sup>	Return on net assets <sup>2</sup>	Benchmark return <sup>3,4</sup>
<b>3 Year Performance</b> (1st April 2003 – 31st March 2006)	<b>340.3%</b>	<b>261.1%</b>	<b>219.1%</b>
<b>5 Year Performance</b> (1st April 2001 – 31st March 2006)	<b>123.3%</b>	<b>125.8%</b>	<b>127.6%</b>
<b>10 Year Performance</b> (1st April 1996 – 31st March 2006)	<b>421.8%</b>	<b>424.7%</b>	<b>234.5%</b>

<sup>1</sup>Change in share price with net dividends (if any) reinvested (Source: Standard & Poor's – www.funds-sp.com).

<sup>2</sup>Change in net asset value per share with net dividends (if any) reinvested. (Source: Fundamental Data Ltd).

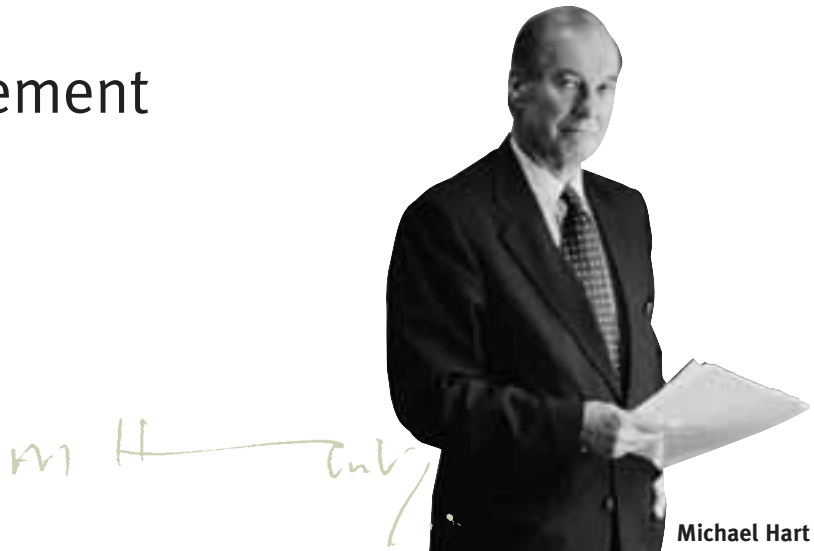
NAV total returns are now calculated on a bid to bid basis. Historic NAVs have been adjusted to a bid basis by using an average factor compiled from the previous 12 month end valuations. This adjustment may vary from that shown in the accounts.

<sup>3</sup>Change in value with net dividends (if any) reinvested (Source: HSBC).

<sup>4</sup>The Company's benchmark is the HSBC Smaller European Companies (Ex UK) Index (in Sterling terms).

Comparison of the Company's performance is made with this benchmark. The benchmark is a recognised index of stocks which should not be taken as wholly representative of the Company's investment universe. The Company's investment strategy does not track this benchmark and consequently, there may be some divergence between its performance and that of the Company.

# Chairman's Statement



**Michael Hart** CHAIRMAN

## Review of the year

For the third year running I am delighted to report that the Company has returned a positive performance. As with the previous years, this has been due to strong results from Continental Europe and the investment managers' consistent stock picking abilities. Over a three year period, the return to shareholders which the Company has produced are +70.2% (year to 31st March 2004), +50.3% (year to 31st March 2005) and +72.0% (year to 31st March 2006). I am sure you will agree that these are excellent returns.

At the end of the year under review, the net asset value per share was 709.0p which was 68.6% higher than the previous year end. This represented a substantial 17% outperformance of the Company's benchmark, the HSBC Smaller European Companies (ex UK) Index, which returned +51.6%.

The Company's 17% outperformance can be analysed by use of the underlying attribution data, which is calculated net of fees and the expenses from the running of the Company. This shows that the investment managers stock selection during the year added +13.6%, and this was further enhanced by the positive impact of the Company's gearing in a rising market. Full details of the performance attribution, together with the investment managers review of the year and a market outlook, are given in the investment managers' report on pages 5 to 8.

The Board regularly discusses gearing with the investment managers and it is the Board's current intention to keep gearing within a range of 10% cash to 15% geared under normal market

conditions. During the year the investment managers have used gearing skillfully and the gearing range has varied between 101% and 112%. It is important to note that having the ability to gear is an advantage of the investment trust structure over other collective investment vehicles.

The discount on the Company's share price to net asset value per share during the year ranged from -6.1% to -16.0%, and ended the year at -10.3% (12.3% year to 31st March 2005), the narrowing discount no doubt reflecting the Company's positive performance. The Board regularly reviews the discount level and wishes to avoid discount volatility returning to the levels seen previously.

At the 2005 AGM, your Board sought shareholder approval subject to certain conditions to reissue shares from treasury at a discount to net asset value. Your Board continues to believe that the ability to reissue, rather than cancel, shares bought in the market is in the interests of shareholders as it has the effect of improving liquidity in the Company's shares, managing any imbalance between the supply and demand, minimising the volatility and absolute levels of the discount and enhancing the net asset value by selling shares at a narrower discount than that at which they were purchased. During the year your Board has fully demonstrated the advantage of treasury shares as in January 2006 it purchased 300,000 shares into treasury at a discount of 10.65% and a cost of £5.40 per share, this purchase was necessary due to an imbalance in the market between supply and demand. The demand for the Company's shares increased and they were subsequently reissued in three tranches in accordance with the Board's guidelines. The first

tranch was for 125,000 shares on 24th February 2006 at a price of £6.13 which equated to a discount of 6.33%. The second was for 100,000 shares on 19th April 2006 at a price of £6.62 which equated to a discount of 6.50% and the last was for 75,000 shares on 20th April 2006 at a price of £6.71 which equated to a discount of 6.00%. The use of treasury shares also resulted in a modest net positive contribution to the relative return, please refer to page 6. Following the year end, the Company again experienced an imbalance in the supply and demand of its shares and between 5th May 2006 and 22nd May 2006 a further 1,020,000 were bought into treasury at an average weighted discount of 11.45%.

Your Board continues to believe that the use of treasury shares will benefit shareholders as a whole and is therefore putting forward resolutions to shareholders at the forthcoming AGM seeking approval to renew the necessary powers. It is important to note that the Board will maintain the policy of constraining the Company's ability to reissue treasury shares, by imposing a strict limit to the dilution associated with the reissue at a discount to a maximum of 0.5% of net asset value in any year.

The Company operates in accordance with the corporate governance best practice and the Board is committed to the highest standards of corporate governance as applicable to investment trust companies. I would like to draw your attention to the comprehensive compliance statements in the Corporate Governance section of this Report on pages 25 to 29. A new requirement is for the Company to include a business review in the

Directors' Report, and this has been included on pages 19 to 24.

I would like to report that during the year the Board has carried out a formal review of the investment manager, company secretarial and marketing services provided to the Company by JPMAM. This review included their investment performance record, management processes, investment style, resources and risk control mechanisms. Due to the volatile nature of this asset class the investment performance needs to be reviewed over the medium to longer term, an investment horizon of three to ten years. As can be seen from the comparative performance against the benchmark, the investment managers have performed well against this measure. After a full consideration of all aspects of the services provided, the Board concluded that the continued appointment of JPMAM for the provision of these services is in the best interest of shareholders.

On 3rd May 2005 the investment manager changed its name from J.P. Morgan Fleming Asset Management (UK) Limited to JPMorgan Asset Management (UK) Limited. We have been informed that the 'Fleming' name will no longer be used in the general promotions of companies in the JPMorgan investment trust range. In view of this, the Board considers it appropriate to change the name of the Company to JPMorgan European Fledgeling Investment Trust plc. We will be seeking shareholders' approval for this change at the forthcoming AGM.

I would like to announce my intention to stand down from the Board at the forthcoming AGM having served as a Director of the Company since October 1997 and Chairman since July 1998. It has been

## Chairman's Statement continued

a pleasure and a privilege to serve as a Director. I am delighted to inform you that Liz Airey will succeed me as Chairman following the conclusion of the forthcoming AGM. Liz has been a Director of the Company since January 2002 and has all the skills necessary to be an excellent Chairman. During 2005, your Board conducted a search for a new Director prior to my retirement. Liz Airey and Michael Wrobel interviewed a number of candidates. On the 1st December 2005 the Board decided to appoint two new directors Paul Manduca and Federico Marescotti having concluded that both brought considerable expertise to the Company, but from different angles. Paul has extensive knowledge of the investment trust industry and European equity markets and was until recently Chief Executive Officer of Deutsche Asset management whilst Federico has considerable knowledge of the European small cap market and is currently a Managing Partner of an Italian private equity Management company. This means that following my retirement the Board will increase by one in number. To accommodate this and any future rise in Directors' fees shareholders will be asked to approve an increase in the maximum aggregate Directors' fees to £175,000.

Your Directors and I very much look forward to welcoming you to the Company's AGM which will be held at The Library, JPMorgan, 60 Victoria Embankment, London EC4Y 0JP. The investment managers will review the past year and comment on the outlook for the current year. If you have any detailed questions, you may wish to raise these in advance with the Company Secretary at Finsbury Dials, 20 Finsbury Street, London EC2Y 9AQ. Shareholders who are unable to attend the AGM in person are encouraged to use their proxy votes. Shareholders who hold their shares through CREST are able to lodge their proxy votes electronically. More details are given in the notes to the Notice of Meeting on pages 32 and 33.

**Michael Hart**

Chairman

2nd June 2006

# Investment Managers' Report



## Francesco Conte

has been managing the Company's assets since 1999

INVESTMENT MANAGER

## Jim Campbell

has been managing the Company's assets since 1995

INVESTMENT MANAGER

### Investment Review

The twelve months to 31st of March 2006 was one of the strongest periods in the Company's history. The prolonged run of low interest rates finally had its desired impact and economic growth began to gain momentum. In combination with the corporate restructuring of prior years, this led to dynamic earnings growth. Markets rose sharply despite minor setbacks in April and October.

The blue chip FTSE World Europe (ex UK) Index rose by 36.0% over the year. Smaller company performance was even stronger and the HSBC Smaller European Companies Index (ex UK) increased by 51.6%. The Company significantly outperformed, and the net asset value per share rose by 68.6% in the period and the share price jumped by 72.0% as the discount narrowed. Stock selection was the key driver to outperformance. Positions which contributed the most included offshore engineering specialist Aker Kvaerner, oil services supplier Subsea 7 and construction business Veidekke, all in Norway, as well as the French steel company Vallourec. The Company's 11.6% position in the JP Morgan Europe Micro Cap Fund, formerly known as Fleming Frontier European Discovery Fund (also managed by the same management team), continued to add value with an increase of 54.8% in the year.

The economic background of low interest rates and recovering economic growth was ideal for growth companies. The best performing investment style factors during the year were high earnings momentum – companies where forecast earnings are being revised upwards, high price momentum – companies whose share prices had risen most

over the previous twelve months continuing to rise fastest over the next twelve months, and high growth companies whose earnings are expected to grow the fastest. For the first time in several years buying stocks which were valued cheaper than the market in itself failed to add significantly to performance.

### Investment Process

The objective of the Company is to achieve capital growth from a portfolio of quoted smaller companies in Europe, excluding the United Kingdom. The investment universe is defined at the time of purchase by the countries and market capitalisation range of the constituents of the benchmark index which, at the end of March 2006, consisted of 1000 companies with a market value of between £70 million and £2,627 million across fifteen countries.

The investment process is driven by bottom-up stock selection focusing on a combination of growth companies with strong operational momentum and value companies with a catalyst for rerating. The large universe of potential investments is screened using a proprietary multi-factor model to the results of which we apply extensive fundamental analysis. The portfolio is constructed within a framework where risk is managed relative to the benchmark index style characteristics of earnings growth, valuation, earnings revisions and price momentum. Investments are sold when there is a fundamental change in business prospects or the valuation is regarded as excessive. The policy is not to hedge the currency exposure of the portfolio's assets. The

## Investment Managers' Report continued

Board has set a liquidity range of 10% cash to 15% gearing within which the Managers may operate.

### Portfolio

In the period the most notable change to the portfolio was the increased weighting in value cyclicals. This was largely the result of increasing further the already significant overweight in construction from 8.2% to 11.6% and in insurance from 5.5% to 8.4%. During the year we took profits in oil and gas, which was one of the strongest performing sectors, so that by the end of the period the 2.7% overweight was turned into a 3.6% underweight. We also reduced the exposure to growth cyclical sectors such as IT hardware where the portfolio ended the year 4.9% underweight and media at 2.5% underweight, such sectors struggling to regain their pricing power. The high exposure to construction and insurance was rewarded as these were the best performing sectors for the Company.

<b>Performance attribution for the year to 31st March 2006</b>		1 Year
		%
Portfolio total return		68.6
Benchmark total return		51.6
<b>Relative return</b>		<b>17.0</b>
<b>Analysis of relative return</b>		
– Selection effect		13.6
– Currency effect		2.0
– Gearing/cash effect		1.6
– Allocation effect		1.7
– Bid valuation adjustment		0.3
– Buybacks		0.2
– Fees/expenses		-1.7
– Residual item		-0.7
<b>Relative return</b>		<b>17.0</b>

Source: Xamin/HSBC/JPMAM

#### Definitions

**Performance attribution:** Analyses how the Company achieved its recorded performance relative to its benchmark.

**Currency effect:** Measures the impact of currency exposure differences between the Company's portfolio and its benchmark. It also identifies the effects of holding forward currency contracts or currency futures.

**Allocation effect:** Measures the impact of allocating assets differently to those in the benchmark, via the portfolio's weighting in different sectors or asset types.

**Bid Valuation adjustment effect:** Measures the effect of change from mid to bid valuation.

**Stock selection effect:** Measures the effect of investing in securities to a greater or lesser extent than their weighting in the benchmark, or of investing in securities outside the benchmark.

**Gearing/cash effect:** Measures the impact on returns of borrowings, cash balances or cash substitutes on the Company's relative performance.

**Buybacks:** Measures the net effect on relative performance of buying back shares at a discount to NAV for cancellation.

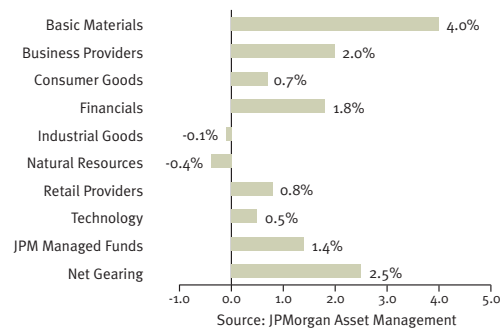
**Fees and other expenses:** The payment of fees and expenses reduces the level of total assets, and therefore has a negative effect on relative performance.

**Residual item:** Arises when there is a divergence between total return as calculated by the AITC/Fundamental Data, and total return as calculated by the attribution generating system. This is a result of methodology differences with respect to the treatment of income and cashflows and timing differences.

**HSBC Smaller European Companies (ex UK)  
Index sector performance over the 12 months to  
31st March 2006**

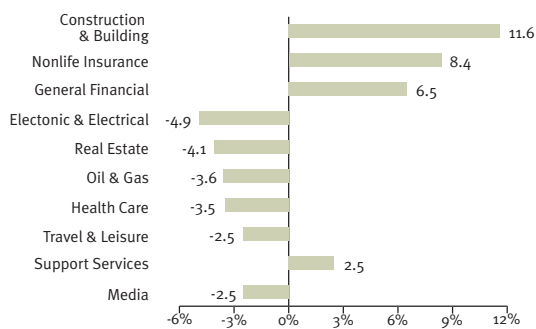
Sector	Index Weight %	Performance %
Financials	19.2	55.4
Consumer Goods	13.5	45.4
Natural Resources	5.7	71.2
Basic Materials	11.7	71.3
Industrial Goods	11.4	56.4
Retail Providers	7.9	41.7
Business Providers	19.7	40.7
Technology	10.7	44.4

**Sector performance attribution for the year to  
31st March 2006**

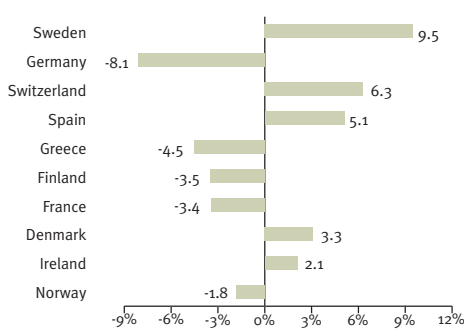


**Top 10 active positions relative to the benchmark index as at 31st March 2006\***

**Industry**



**Country**



\*excluding cash and JPMorgan Europe Micro Cap Fund  
Source: JPMorgan Asset Management, Factset, HSBC

## Investment Managers' Report continued

The country exposure changed markedly in the period with the overweight position in the Netherlands replaced by Sweden and the underweight in Italy being replaced by Germany. The countries which added most value to portfolio returns included Sweden, Norway, the Netherlands and France. The portfolio was modestly geared at around 5% throughout the year, contributing positively to performance in a rising market.

### **Outlook**

With interest rates on an upward but manageable path, strong earnings growth and corporate takeover activity accelerating to levels not seen in many years, the outlook for equities remains positive. However, enthusiasm should be tempered. Sectors such as basic materials now command valuations which assume that the current high levels and in some cases unprecedented margins can be maintained over the long term. Appetite for risk, consistent with a prolonged period of low interest rates, is at a high level and a meaningful weakening of bond yields may lead to a reassessment of the risk premium.

Overall we remain confident that by maintaining a disciplined stockpicking approach, focusing on cheap stocks with good operational momentum, we can continue to add value for shareholders.

**Jim Campbell**  
**Francesco Conte**

Investment Managers

2nd June 2006

# Summary of Results

	2006	2005	
<b>TOTAL RETURNS</b>			
for the year to 31st March			
Return to shareholders <sup>1</sup>	<b>+72.0%</b>	+50.3%	
Return on net assets <sup>2</sup>	<b>+68.6%<sup>2</sup></b>	+41.4% <sup>2</sup>	
HSBC Smaller European Companies (ex UK) Index <sup>3,4</sup>	<b>+51.6%</b>	+31.8%	
			% change
<b>ASSETS</b> at 31st March			
Total net assets (£'000)	<b>372,970</b>	225,934	+65.1
Net asset value per share	<b>709.0p</b>	421.8p	+68.1 <sup>2</sup>
Share price	<b>636.0p</b>	369.8p	+72.0
Discount to net asset value	<b>10.3%</b>	12.3%	
HSBC Smaller European Companies (ex UK) Index (capital only) <sup>5</sup>	<b>47.6%</b>	28.8%	
<b>REVENUE</b> for the year ended 31st March			
Gross revenue return (£'000)	<b>4,898</b>	4,218	+16.1
Revenue return attributable to ordinary shareholders (£'000)	<b>216</b>	91	
Revenue return per ordinary share	<b>0.41p</b>	0.17p	
Dividend per ordinary share	<b>nil</b>	nil	
<b>GEARING FACTOR</b>			
Actual <sup>6</sup>	<b>103.8</b>	104.9	
Potential <sup>7</sup>	<b>113.0</b>	115.0	
<b>TOTAL EXPENSE RATIO<sup>8</sup></b>	<b>1.00%</b>	0.98%	

<sup>1</sup> Change in share price with net dividends (if any) reinvested (Source: Standard & Poor's – www.funds-sp.com).

<sup>2</sup> Change in net asset value per share with net dividends (if any) reinvested. (Source: Fundamental Data Ltd). NAV total returns are now calculated on a bid to bid basis. Historic NAVs have been adjusted to a bid basis by using an average factor compiled from the previous 12 month end valuations. This adjustment may vary from that shown in the accounts. The movement in NAV in the table above is based on the NAV as stated in the accounts for the year ended 31st March 2005. This NAV has not been restated for the adoption of bid prices and therefore the returns will differ.

<sup>3</sup> Change in value with net dividends (if any) reinvested (Source: HSBC).

<sup>4</sup> The Company's benchmark is the HSBC Smaller European Companies (Ex UK) Index (in sterling terms). Comparison of the Company's performance is made with this benchmark. The benchmark is a recognised index of stocks which should not be taken as wholly representative of the Company's investment universe. The Company's investment strategy does not track this benchmark and consequently, there may be some divergence between its performance and that of the Company.

<sup>5</sup> Source: Datastream.

<sup>6</sup> Actual gearing means investments expressed as a percentage of shareholders' funds but treats investments in government bonds and liquidity funds as cash.

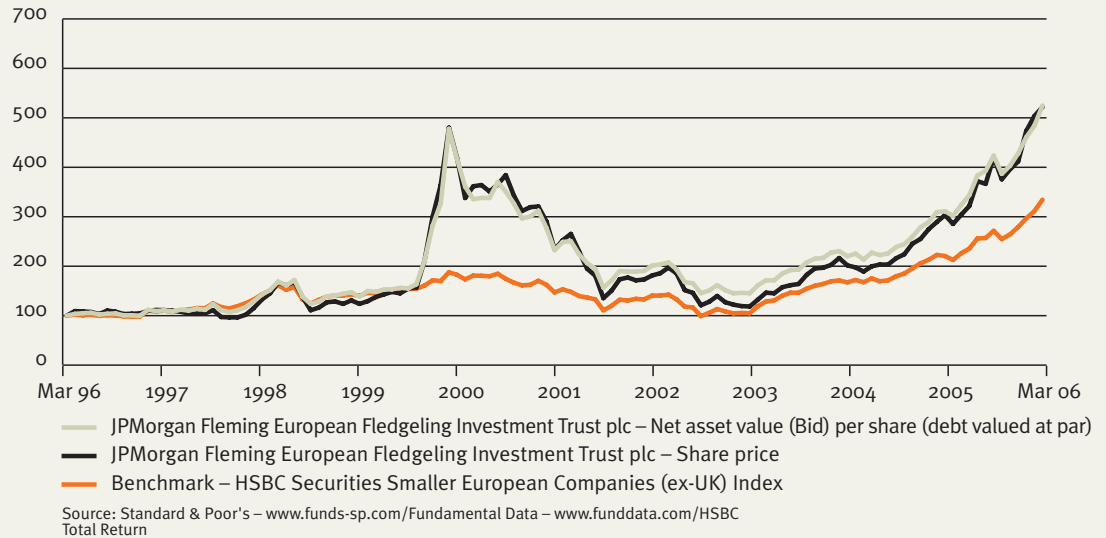
<sup>7</sup> Potential gearing means total assets, including any undrawn facilities, less current liabilities expressed as a percentage of shareholders' funds.

<sup>8</sup> Management fees and all other operating expenses (including tax relief, where allowable) expressed as a percentage of average net assets over the year.

# Performance

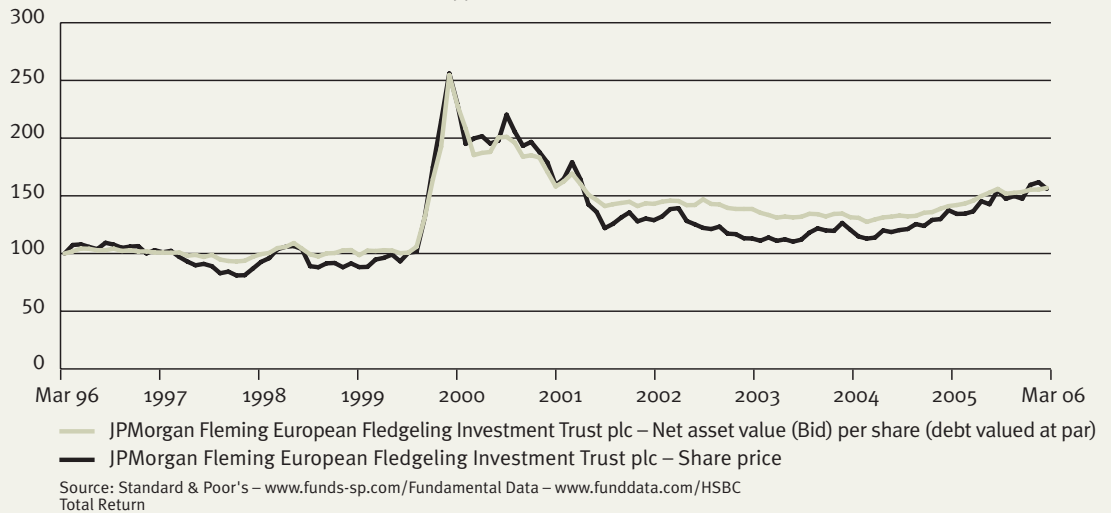
## Ten Year Performance

Figures have been rebased to 100 at 31st March 1996



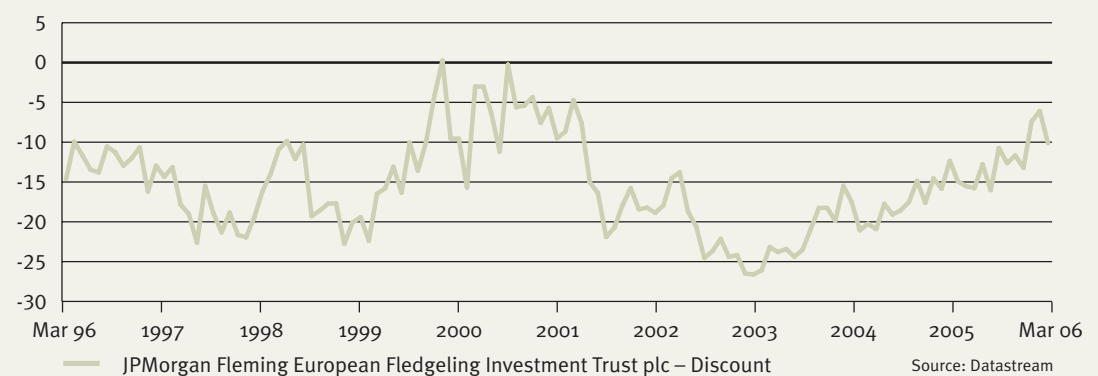
## Performance Relative to Benchmark Index

Figures have been rebased to 100 at 31st March 1996



The benchmark index is represented by the bold horizontal line.

## Discount to Net Asset Value



# Financial Record

## Financial Record

<b>As at 31st March</b>	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	<b>2006</b>
Total assets less current liabilities (£m)	84.6	94.7	129.9	140.3	412.9	221.9	181.9	116.0	162.6	225.9	<b>373.0</b>
Ordinary shareholders' funds (£m)	76.7	86.7	120.6	117.2	346.0	192.9	158.9	107.6	162.6	225.9	<b>373.0</b>
Warrant price (p) <sup>3</sup>	23.5	37.0	-	-	-	-	-	-	-	-	-
Discount (%)	10.4	9.7	16.1	19.4	9.5	9.5	18.9	26.6	17.5	12.3	<b>10.3</b>
Actual gearing <sup>4</sup>	107.8	110.4	114.6	117.1	118.7	114.1	110.7	104.9	107.8	104.9	<b>103.8</b>
Potential gearing <sup>4</sup>	110.4	109.2	107.7	119.7	119.3	115.0	114.5	107.7	116.0	115.0	<b>113.0</b>
Total expense ratio (%) <sup>4</sup>	0.75	0.87	0.92	0.97	1.06	1.60	1.29	1.10	0.99	0.98	<b>1.00</b>

### Year to 31st March

Gross revenue return (£'000)	1,280	1,794	1,661	2,494 <sup>3</sup>	1,641	2,074	2,779	3,572	3,446	4,218	<b>4,898</b>
Revenue return per ordinary share (p)	(0.44)	(0.31)	(0.99)	(0.32)	(3.93)	(8.26)	(2.94)	0.48	1.59	0.17	<b>0.41</b>
Dividend per ordinary share (net) (p)	nil	nil	nil	nil	nil	nil	nil	nil	nil	nil	<b>nil</b>

### Rebased to 100 at 31st March 1996

Net asset value per ordinary share – total return <sup>1,3</sup>	100.0	110.9	142.3	138.3	416.8	232.4	201.0	145.3	220.0	311.3	<b>524.7</b>
Ordinary share price – total return <sup>1</sup>	100.0	111.3	132.6	123.8	418.8	233.7	181.3	118.5	201.7	303.3	<b>521.8</b>
HSBC Smaller European Companies (ex-UK) Index (expressed in Sterling) – total return <sup>1</sup>	100.0	110.1	143.1	140.3	182.6	147.0	140.6	104.9	167.4	220.6	<b>334.5</b>

<sup>1</sup> Source: Standard & Poor's – [www.funds-sp.com/Fundamental Data Ltd/HSBC](http://www.funds-sp.com/Fundamental Data Ltd/HSBC).

<sup>2</sup> Figures have been restated where necessary to comply with FRS16. The figures for 1998 and prior years have not been restated.

<sup>3</sup> Dealings in warrants ceased on 31st July 1997. Historic net asset value is therefore disclosed on a fully diluted basis.

<sup>4</sup> Definitions shown on page 9.

# Ten Largest Investments

at 31st March 2006

<b>Company</b>	<b>Country</b>	<b>Value £'000</b>	<b>%<sup>1</sup> assets</b>
JPM Europe Micro Cap Fund	Luxembourg	44,374	11.6
Cementos Portland Valderrivas	Spain	11,759	3.1
Fuchs Petrolub	Germany	11,109	2.9
Cermaq	Norway	8,894	2.3
Topdanmark	Denmark	8,845	2.3
JM	Sweden	8,816	2.3
Lindex	Sweden	8,781	2.3
Groupo Catalana Occidente	Spain	8,497	2.2
Rockwool	Denmark	8,317	2.2
Transcom Worldwide	Sweden	8,007	2.1
<b>TOTAL</b>		<b>127,399</b>	<b>33.3</b>

<sup>1</sup>Based on total assets less current liabilities of £383.4m after adding back Euro 15m loan.

As at 31st March 2005, the value of the ten largest investments amounted to £69,198,000 representing 26.6% of total assets less current liabilities.

# Investment Activity

## Investment Activity\*

for the year ended 31st March 2006

	Value at 31st March 2005 (Restated)		Purchases £'000	Sales £'000	Changes <sup>1</sup> in value £'000	Value at 31st March 2006	
	£'000	%				£'000	%
Sweden	7,293	2.8	48,664	11,995	16,296	<b>60,258</b>	<b>15.7</b>
Luxembourg	33,003	12.7	–	–	11,371	<b>44,374</b>	<b>11.6</b>
Switzerland	10,742	4.1	49,463	25,903	9,650	<b>43,952</b>	<b>11.5</b>
Italy	13,348	5.1	60,016	47,617	9,699	<b>35,446</b>	<b>9.2</b>
Spain	22,224	8.5	22,436	23,484	13,757	<b>34,933</b>	<b>9.1</b>
France	24,128	9.3	45,722	50,503	13,606	<b>32,953</b>	<b>8.6</b>
Netherlands	35,978	13.8	58,410	77,635	15,770	<b>32,523</b>	<b>8.5</b>
Denmark	6,481	2.5	41,262	30,657	13,873	<b>30,959</b>	<b>8.1</b>
Norway	22,199	8.5	21,203	38,136	19,079	<b>24,345</b>	<b>6.3</b>
Ireland	15,769	6.1	5,963	10,867	3,899	<b>14,764</b>	<b>3.9</b>
Germany	15,535	6.0	31,554	39,598	3,618	<b>11,109</b>	<b>2.9</b>
Finland	14,795	5.7	24,766	45,916	14,226	<b>7,871</b>	<b>2.1</b>
Austria	2,965	1.1	8,736	6,745	2,892	<b>7,848</b>	<b>2.0</b>
Belgium	–	–	17,019	10,242	(899)	<b>5,878</b>	<b>1.5</b>
Greece	9,826	3.8	11,452	24,744	3,466	–	–
Portugal	2,747	1.0	–	2,707	(40)	–	–
<b>Total portfolio</b>	<b>237,033</b>	<b>91.1</b>	<b>446,666</b>	<b>446,749</b>	<b>150,263</b>	<b>387,213</b>	<b>101.0</b>
Net current assets/(liabilities)	23,291	8.9	–	–	–	<b>(3,778)</b>	<b>(1.0)</b>
<b>Total net assets</b>	<b>260,324</b>	<b>100.0</b>	<b>446,666</b>	<b>446,749</b>	<b>150,263</b>	<b>383,435</b>	<b>100.0</b>

<sup>1</sup>This includes impact of change in accounting policy.

\*Based on total assets less current liabilities of £383.4m (2005: based on £260.3m), after adding back Euro 15m loan (2005: Euro 15m loan).

# Analysis of Portfolio

Geographic	31st March 2006		31st March 2005	
	Portfolio*	Index	Portfolio*	Index
(“Look through” basis)	%	%	(Restated) %	(Restated) %
Sweden	17.4	9.2	5.7	8.9
Switzerland	12.0	8.2	5.4	9.1
Italy	10.5	11.7	6.2	13.3
France	10.4	13.3	10.4	13.3
Spain	9.8	5.2	8.5	6.2
Netherlands	9.3	7.5	14.4	7.4
Denmark	8.6	5.3	3.2	4.6
Norway	7.0	6.8	9.1	4.0
Ireland	3.8	2.3	6.1	2.7
Germany	3.7	12.8	6.7	11.7
Finland	3.1	5.8	6.7	6.0
Austria	2.6	3.0	1.4	2.8
Belgium	1.7	3.4	0.5	3.1
Greece	0.6	4.5	5.0	4.6
Portugal	–	1.0	1.1	1.3
Luxembourg	–	–	–	1.0
Net current (liabilities)/ assets	(0.5)	–	9.6	–
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	100.0	100.0

Based on total assets less current liabilities of £383.4m (2005: £260.3m).

Euro 15m of the Euro 70m loan facility has been added back into 2006 net current assets/(liabilities) figure and Euro 50m in 2005.

\*This has been calculated on a “look through” basis to take into account that the JPM Europe Micro Cap Fund is invested in a number of countries. This has consequently also affected the net current assets/(liabilities) figure.

Sector	31st March 2006		31st March 2005	
	Portfolio	Index	Portfolio	Index
	%	%	(Restated) %	(Restated) %
Finance	22.3	17.8	11.5	19.0
Industrial Services	18.8	8.3	14.8	6.4
Investment Companies	11.6	–	12.7	–
Consumer Non-Durables	7.5	5.5	–	5.6
Producer Manufacturing	6.9	11.8	10.2	11.5
Process Industries	5.6	7.0	6.6	5.6
Technology Services	4.9	4.4	5.7	4.9
Commercial Services	4.0	4.3	5.3	3.9
Transportation	3.5	5.6	1.2	4.9
Consumer Services	3.1	5.6	3.2	7.1
Retail Trade	3.0	3.4	3.9	4.8
Non-energy Minerals	3.1	4.5	–	4.6
Energy/Minerals	2.9	1.3	1.2	1.4
Health Technology	1.8	5.5	2.7	5.4
Distribution Services	1.5	2.2	3.8	2.6
Electronic Technology	0.5	5.4	1.5	5.3
Consumer Durables	–	3.5	5.3	3.5
Communications	–	1.2	1.4	1.5
Health Services	–	1.0	–	0.8
Utilities	–	1.7	–	1.2
Net current (liabilities)/ assets	(1.0)	–	9.0	–
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	100.0	100.0

Based on total assets less current liabilities of £383.4m (2005: £260.3m).

Euro 15m of the Euro 70m loan facility has been added back into 2006 net current assets/(liabilities) figure and Euro 50m in 2005.

# List of Investments

at 31st March 2006

	£'000		£'000
<b>Austria</b>		<b>Germany</b>	
Andritz	7,848	Fuchs Petrolub	11,109
Total	7,848	Total	11,109
<b>Belgium</b>		<b>Ireland</b>	
Omega Pharma	5,878	Kingspan	7,354
Total	5,878	F.B.D.	7,410
<b>Denmark</b>		Total	14,764
Topdanmark	8,845	<b>Italy</b>	
Rockwool	8,317	Creditor Emiliano	7,652
FLSmidth	6,972	Valentino Fashion Group	7,583
Sydbank	6,825	Davide Campari	6,347
Total	30,959	Guala Closures	5,872
<b>Finland</b>		Recordati	5,352
Yit	7,871	Marr	2,640
Total	7,871	Total	35,446
<b>France</b>		<b>Luxembourg</b>	
SR Teleperformance	6,337	JPM Europe Micro Cap Fund*	44,374
Scor	6,087	Total	44,374
Groupe Steria	5,842		
Pierre & Vacances	5,728		
GFI Informatique	5,380		
Latecoere	2,081		
Ipsen	1,498		
Total	32,953		

\*Formerly known as Fleming Frontier European Discovery Fund

## List of Investments continued

at 31st March 2006

	£'000		£'000
<b>Netherlands</b>		<b>Sweden</b>	
Nutreco	7,828	JM	8,816
Royal Vopak	7,550	Lindex	8,781
Buhrmann	5,936	Transcom Worldwide	8,007
Smit	5,673	HIQ	7,720
Royal Boskalis Westminster	5,536	Holmen	7,439
Total	32,523	Cardo	7,317
		D.Carnegie	6,226
		Invik	5,952
		Total	60,258
<b>Norway</b>			
Cermaq	8,894		
Veidekke	7,785		
Aker Kvaerner	7,666		
Total	24,345		
<b>Spain</b>		<b>Switzerland</b>	
Cementos Portland Valderrivas	11,759	Kuoni Reisen	6,215
Grupo Catalana Occidente	8,497	Sika	6,210
Banco Pastor	7,359	Geberit	5,963
Fadesa Inmobiliaria	7,318	George Fisher	5,882
Total	34,933	St Galler Kantonalbank	5,795
		Banque Cantonale Vaudoise	5,754
		Rieter	5,317
		Baloise	1,923
		Publicgroupe	893
		Total	43,952
		<b>Total Portfolio</b>	<b>387,213</b>

# Shareholder Analysis

at 31st March 2006

	Number of shares	% held
Pension Funds	14,382,960	27.2
Unit Trusts	7,297,880	13.8
Investment Trusts <sup>1</sup>	1,629,213	3.1
Insurance Companies	1,430,424	2.7
Other Institutions	1,142,251	2.2
Charities	828,859	1.6
UK Government	34,658	0.1
<b>Total Institutions</b>	<b>26,746,245</b>	<b>50.7</b>
<b>Treasury Shares</b>	<b>175,000</b>	<b>0.3</b>
Retail Investors holding shares directly or through nominee accounts*	8,193,202	15.5
Private Client Brokers	10,932,500	20.7
Individuals in the Investment Trust Share Plan <sup>2</sup>	3,535,594	6.7
Individuals in the Investment Trust Personal Equity Plan <sup>2</sup>	1,437,973	2.7
Individuals in the Investment Trust Individual Savings Account <sup>2</sup>	976,468	1.9
Individuals in the Investment Trust Pension Account <sup>2</sup>	784,535	1.5
<b>Total Retail Holdings</b>	<b>25,860,272</b>	<b>49.0</b>
<b>Total shares in issue<sup>3</sup></b>	<b>52,781,517</b>	<b>100.0</b>

*Nominee accounts have been allocated to their appropriate category.*

\*Includes shares below threshold of 10,000 shares

<sup>1</sup>Includes 800,000 shares held by JPMorgan Elect plc

<sup>2</sup>Savings products managed by JPMorgan

Source: Thomson Financial

# Board of Directors



**Michael Hart\*\* (Chairman of the Board and Nomination Committee)**

Age 69

A Director since October 1997

Appointed Chairman in 1998

Formerly Chief Executive of Sun Life and Provincial plc. Chairman of Furness Building Society, a Director of Home & Legacy Insurance Services Limited and Premierline Direct Ltd.



**Elisabeth Airey\*\***

Age 47

A Director since January 2000

A Director of Harrison Lovegrove & Co, AMEC plc and Dunedin Enterprise Investment Trust plc, and Chairman of Zetex plc.



**Anthony Davidson\*\* (Chairman of the Audit Committee)**

Age 58

A Director since May 2005

A Director of Britannic Assurance plc, Century Life plc and RLG with-profits Holdings Limited and Sun Life Assurance Company of Canada (UK) Limited. Formerly Chief Executive of Provincial Insurance plc and Chairman of JPMorgan Fleming Worldwide Income Investment Trust plc.



**Jacques Drossaert\*\***

Age 68

A Director since January 1999

Formerly Managing Director of PanEuroLife, a Luxembourg life and pensions company.



**Paul Manduca\*\***

Age 54

A Director since December 2005

Formerly the Chief Executive Officer of Deutsche Asset Management Limited, a Director of The Henderson Smaller Companies Investment Trust plc, Development Securities plc, UNIQ Pension Scheme Trustees Limited and WM Morrison Supermarkets plc.



**Federico Marescotti\*\***

Age 49

A Director since December 2005

A Managing Partner of Vela Capital and Vice Chairman of Friulia, Italy, a Director of Ecofin Water & Power Opportunities plc.



**Michael Wrobel\*\***

Age 51

A Director since April 2003

Head of Investment Trusts at F&C Management, a Director of Aberdeen European Investment Trust plc, Geit Offer plc and The German Investment Trust plc.

\*Member of Audit Committee.

†Member of Nomination Committee.

‡Considered independent by the Board

# Directors' Report

The Directors present their report for the year ended 31st March 2006.

## Business Review

### Business of the Company

The Company carries on business as an investment trust and was approved by the Inland Revenue as an investment trust in accordance with Section 842 of the Income and Corporation Taxes Act 1988 for the year ended 31st March 2005. In the opinion of the Directors, the Company has subsequently conducted its affairs so that it should continue to qualify. The Company will continue to seek approval under Section 842 of the Income and Corporation Taxes Act 1988 each year. Approval for the year ended 31st March 2005 is subject to review should there be any subsequent enquiry under Corporation Tax Self Assessment. The Company is an investment company within the meaning of Section 266 of the Companies Act 1985. The Company is not a close company for taxation purposes.

### Investment Objective and Policies

The Company's objective is to achieve capital growth from smaller European companies (excluding the UK) by consistent out-performance of the Company's benchmark index, HSBC Smaller European Companies (ex UK) Index expressed in sterling terms, by taking carefully controlled risks through an investment method that is clearly communicated to shareholders (details of which are given in the Investment Managers' Report on pages 5 and 6).

In order to achieve this objective, the Company invests in a diversified portfolio of smaller companies in Europe, excluding the United Kingdom, emphasising capital rather than income growth, so shareholders should not therefore expect to receive a dividend. Liquidity and borrowings are managed with the aim of increasing returns to shareholders. The Company does not invest more than 15% of its gross assets in other UK listed investment companies (including investment trusts).

### Performance

In the year to 31st March 2006, the Company produced a total return to shareholders of +72.0%

and a total return on net assets of +68.6%. This compares with the return on the Company's benchmark index of +51.6%. As at 31st March 2006, the value of the Company's investment portfolio was £387m. The Investment Managers' Report on pages 5 to 8 includes a review of developments during the year as well as information on investment activity within the Company's portfolio.

### Revenue and Dividends

Gross revenue for the year totalled £4,898,000 (2005: £4,218,000) and distributable revenue after deducting interest, administrative expenses and taxation amounted to £216,000 (2005: £91,000). The Company is unable to pay a dividend due to a £8,683,000 deficit on the Revenue Account (2005: £8,899,000).

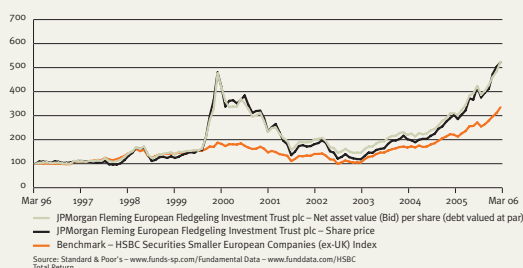
### Key Performance Indicators ('KPIs')

The Board uses a number of financial KPIs to monitor and assess the performance of the Company. The principal KPIs are:-

- Performance against the benchmark index:  
This is the most important KPI by which performance is judged.

### Ten Year Performance

Figures have been rebased to 100 at 31st March 1996



### Performance Relative to Benchmark Index

Figures have been rebased to 100 at 31st March 1996



- Performance against the Company's peers*  
The principal objective is to achieve capital growth relative to the benchmark. However, the Board also monitors the performance relative to a broad range of competitor funds.
- Performance Attribution*  
The purpose of performance attribution analysis is to assess how the Company achieved its performance relative to its benchmark index, i.e. to understand the impact on the Company's relative performance of the various components such as asset allocation and stock selection. Details of the attribution analysis for the year ended 31st March 2006 are given in the Investment Managers' Report on pages 5 to 8.
- Discount to net asset value ("NAV")*  
The Board has a share repurchase programme in place which, when necessary, seeks to address imbalances in supply and demand of the Company's shares within the market and thereby minimise the volatility and absolute level of the discount to NAV at which the Company's shares trade. The Board also has the ability to purchase shares into treasury and to issue them at a later date at a narrower discount. Further details on treasury shares can be found in the Chairman's Statement on pages 2 to 4. In the year to 31st March 2006, the discount ranged between 6.1% and 16.0%.

- Total expense ratio ("TER")*  
The total expense ratio ("TER") is an expression of the Company's management fees and all other operating expenses (including tax relief, where allowable) as a percentage of average net assets over the year. The TER for the year ended 31st March 2006 was 1.00% (2005: 0.98%). The Board reviews the TER of the Company regularly and, on an annual basis, reviews its TER against other companies with similar investment objectives and policies.

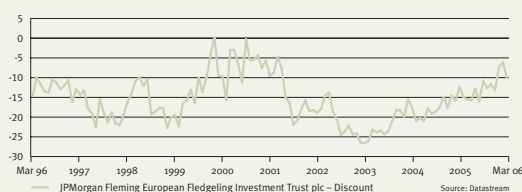
*Share Capital*

Further to resolutions passed on 14th July 2005, the Company re-purchased 785,000 ordinary shares for cancellation during the year, representing 1.46% of the Company's issued share capital at the beginning of the financial year, for a consideration of £2,765,000. Since the end of the year the Company has not repurchased any further ordinary shares for cancellation. The Company purchased a total of 300,000 ordinary shares into treasury during the year and 125,000 these were sold, at a discount to NAV on 24th February 2006. Following the year end 100,000 were sold on 19th April 2006 and the remaining 75,000 were sold on 20th April 2006. In both cases the sale was on a smaller discount to NAV than that on which they were purchased. The Company has subsequently purchased 870,000 ordinary shares into treasury.

Resolutions to renew the authority to repurchase shares, and to sell shares from treasury at a discount to NAV is due to be put to shareholders at the forthcoming Annual General Meeting. The full text of these resolutions is set out in the Notice of Annual General Meeting on pages 32 and 33.

The Company did not issue any new shares during the year.

Discount to Net Asset Value



### *Principal Risks*

With the assistance of the Manager, the Board has drawn up a risk matrix, which identifies the key risks to the Company. These key risks fall broadly under the following categories:

- **Investment and Strategy:** An inappropriate investment strategy, for example asset allocation or the level of gearing, may lead to under-performance against the Company's benchmark index and peer companies, which may result in the Company's shares trading on a wider discount. The Board manages these risks by diversification of investments through its investment restrictions and guidelines which are monitored and reported on. JPMAM provides the Directors with timely and accurate management information, including performance data and attribution analyses, revenue estimates, liquidity reports and shareholder analyses. The Board monitors the implementation and results of the investment process with the Investment Managers, who attend all Board meetings, and reviews data which shows statistical measures of the Company's risk profile. The Investment Manager employs the Company's gearing tactically, within a strategic range set by the Board. The Board holds a separate meeting devoted to strategy each year.
- **Accounting, Legal and Regulatory:** In order to qualify as an investment trust, the Company must comply with Section 842 of the Income and Corporation Taxes Act 1988 ('Section 842'). Details of the Company's approval are given under "Business of the Company" above. Should the Company breach Section 842, it may lose investment trust status and as a consequence gains within the Company's portfolio would be subject to Capital Gains Tax. The Section 842 qualification criteria are continually monitored by JPMAM and the results reported to the Board each month. The Company must also comply with the provisions of The Companies Act 1985 and, as its shares

are listed on the London Stock Exchange, the UKLA Listing Rules. A breach of the Companies Act could result in the Company and/or the Directors being fined or the subject of criminal proceedings. Breach of the UKLA Listing Rules may result in the Company's shares being suspended from listing which in turn would breach Section 842. The Board relies on the services of its Company Secretary, JPMAM, and its professional advisers to ensure compliance with The Companies Act 1985 and The UKLA Listing Rules.

- **Corporate Governance and Shareholder Relations:** Details of the Company's compliance with Corporate Governance best practice, including information on relations with shareholders, are set out in the Corporate Governance report on pages 25 to 29.
- **Operational:** Disruption to, or failure of, JPMAM's accounting, dealing or payments systems or the custodian's records may prevent accurate reporting and monitoring of the Company's financial position. Details of how the Board monitors the services provided by JPMAM and its associates and the key elements designed to provide effective internal control are included with the Internal Control section of the Corporate Governance report on pages 25 to 29.
- **Financial:** The Company's investment activities expose it to a variety of financial risks that include market price risk, cash flow interest rate risk, foreign currency risk and liquidity risk. Further details are disclosed in note 15 on pages 50 and 51.

### *Future Developments*

Clearly the future development of the Company is much dependent upon the success of the Company's investment strategy in the light of economic and equity market developments, but the Investment Managers discuss the outlook in their report on page 8.

## Directors' Report continued

### Management

The Manager and Secretary, JPMorgan Asset Management (UK) Limited ('JPMAM'), changed its name from J.P. Morgan Fleming Asset Management (UK) Limited with effect from 3rd May 2005.

JPMAM is employed under a contract terminable on one year's notice, without penalty. If the Company wishes to terminate the contract on shorter notice, the balance of remuneration is payable by way of compensation.

JPMAM is a wholly-owned subsidiary of JPMorgan Chase Bank which, through other subsidiaries, also provides banking, dealing and custodian services to the Company.

### Management Fee

The management fee is charged at the rate of 1.3% of the Company's market capitalisation and is calculated and paid monthly in arrears. If the Company invests in funds managed or advised by JPMAM or any of its associated companies, those investments are excluded from the calculation and therefore attract no fee.

### Going Concern

The Directors consider that the Company has adequate resources, an appropriate financial structure and suitable arrangements in place for its management to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

### Payment Policy

It is the Company's policy to obtain the best terms for all business and therefore there are no standard payment terms. In general the Company agrees with its suppliers the terms on which business will take place and it is the Company's policy to abide by these terms. As at 31st March 2006, the Company had no outstanding trade creditors.

### Directors

The Directors of the Company who held office at the end of the year, together with their beneficial interests in the Company's ordinary share capital, are given below:

	31st March 2006	1st April 2005 or at date of appointment
Michael Hart	14,661	14,661
Elisabeth Airey	18,538	18,538
Anthony Davidson <sup>2</sup>	4,011	–
Jacques Drossaert	11,538	11,538
Paul Manduca <sup>1</sup>	–	–
Federico Marescotti <sup>1</sup>	–	–
Michael Wrobel	4,408	4,408

<sup>1</sup> Appointed on 1st December 2005

<sup>2</sup> Appointed on 13th May 2005

Subsequent to the year end Jacques Drossaert sold 3,000 shares on 4th May 2006. There have been no other changes in the above holdings since the year end.

In accordance with the Company's Articles of Association, Paul Manduca and Federico Marescotti, having been appointed on 1st December 2005, offer themselves for election and the Directors retiring by rotation at the Annual General Meeting will be Michael Wrobel who, being eligible, offers himself for re-election by shareholders and Michael Hart who is not seeking re-election.

An insurance policy is maintained by the Company which indemnifies the Directors of the Company against certain liabilities arising in the conduct of their duties.

### Notifiable Share Interests

At the date of this report the Company was aware of the following interests in excess of 3% or more of its issued share capital:

Shareholders	Number of shares held	%
Ordinary shares		
Puddle Dock Nominees <sup>1,2</sup>	5,965,350	11.30
JPMorgan Asset Management (UK) Ltd <sup>2</sup>	3,607,222	6.83
Lattice Group Pension Scheme	2,852,879	5.41
Legal & General Investment Management	1,948,156	3.32
Lazard Asset Management LLC	1,628,300	3.08
East Riding of Yorkshire Council	1,600,000	3.03

<sup>1</sup> Held on behalf of JPMAM ISA, PEP and Share Plan participants.

<sup>2</sup> Non-beneficial.

### Independent Auditors

PricewaterhouseCoopers LLP have expressed their willingness to continue in office as auditor to the Company and a resolution proposing their re-appointment, and to authorise the Directors to determine their remuneration for the ensuing year, will be put to shareholders at the Annual General Meeting.

### Accounting Policies

From 1st January 2005, International Financial Reporting Standards (IFRS) came into force for all listed companies that prepare group accounts. Other companies are permitted to adopt these standards voluntarily. As a company, rather than adopt IFRS, the Company has continued to follow the UK accounting framework, albeit amended for new accounting standards which were released by the UK Accounting Standards Board as the first part of the IFRS convergence programme. This approach is consistent with that of most other investment trust companies which do not prepare group accounts.

These revised accounting standards have been applied to all periods being reported in the

accounts. The main changes to prior years include the requirement to value investments at 'fair value' (taken to be bid value) rather than last trade price and the requirement to disclose transaction costs on the purchase and sale of investments. The accounts also include a new primary statement, the Reconciliation of Movements in Shareholders' Funds, which can be found on page 38.

Further details can be found in the notes to the accounts; in particular the accounting policies notes on pages 41 and 42.

### Annual General Meeting

Resolutions relating to the following items of special business will be proposed at the forthcoming Annual General Meeting:

*(i) Authority to Repurchase the Company's Shares (resolution 7)*

The authority to repurchase up to 14.99 per cent of the Company's issued share capital, granted by shareholders at the 2005 AGM, will expire on 13th January 2007 unless renewed at the forthcoming AGM. The Directors consider that the renewing of the authority is in the interests of shareholders as a whole, as the repurchase of shares at a discount to the underlying NAV enhances the NAV of the remaining shares.

The Board will seek shareholder approval at the AGM to renew this authority, which will last until 11th January 2008 or until the whole of the 14.99 per cent has been acquired, whichever is the earlier. The full text of the resolution is set out in the Notice of Meeting on pages 32 and 33. Repurchases will be made at the discretion of the Board, and will only be made in the market at prices below the prevailing Net Asset Value per share as and when market conditions are appropriate.

The Directors consider that the renewal of the share repurchase authority is in the interests of shareholders as a whole and unanimously recommend all shareholders to vote in favour.

*(ii) Treasury shares/disapplication of pre-emption rights (resolutions 8 and 9)*

With effect from 1st December 2003, the Companies Act has been amended to permit the Company to repurchase up to 10 per cent. of its own shares into treasury (for reissue or cancellation at a future date) as an alternative to repurchasing for immediate cancellation. The Board considers that circumstances could arise in which it would be in shareholders' interests for such powers to be exercised. This 10 per cent. would form part of the 14.99 per cent. referred to in (i) above.

The Board believes that the effective use of treasury shares could assist the Company in improving liquidity and discount in the Company's shares, of managing any imbalance between supply and demand and minimising the volatility and absolute level of the discount at which the Company's shares trade to their net asset value ('NAV') for the benefit of shareholders.

Accordingly, shareholders will also be asked at the Annual General Meeting to approve resolutions 8 and 9 which will allow the Company to sell shares from treasury at a discount to NAV and disapply the statutory pre-emption rights respectively. This will enable the Company to sell shares held in treasury without having to make a pro rata offer to existing shareholders.

Should the resolutions be passed by shareholders, the Company would purchase shares at a discount to their prevailing NAV, hold them in treasury, available for reissue when market demand is identified. Reissues would be made at a discount narrower than the weighted average discount at which purchases are made.

This process ensures that the enhancement in net asset value associated with share purchases exceeds the dilution in net asset value associated with the reissue of treasury shares at a discount.

The Board is mindful that shareholders may be concerned about the dilution in net asset value associated with the reissue of treasury shares at a discount. It is therefore proposed that the reissue of shares from treasury at a discount be limited so that in the year to the Company's 2007 Annual General Meeting, the aggregate dilution in net asset value per share arising on such reissues does not exceed 3.54 pence per share, being approximately 0.5% of the net asset value per share as at 31st March 2006.

*(iii)* That in accordance with the Company's Article 90 of the Articles of Association, the maximum aggregate Directors' fees payable be increased from £125,000 to £175,000 per annum with immediate effect.

*(iv) Change of Company Name*

The Directors recommend that the Company's name be changed to 'JPMorgan European Fledgeling Investment Trust plc'.

The full text of all the resolutions are set out as in the Notice of Meeting on pages 32 and 33.

By order of the Board  
Hilary Lowe, for and on behalf of  
JPMorgan Asset Management (UK) Limited,  
Secretary  
2nd June 2006

# Corporate Governance

## **Compliance**

The Company is committed to high standards of corporate governance. This statement, together with the Statement of Directors' Responsibilities on page 31, indicates how the Company has applied the principles of good governance of the revised Combined Code published in 2003 (the 'Combined Code') and the AITC's Code of Corporate Governance, also published in 2003 (the 'AITC Code'), which complements the Combined Code and provides a framework of best practice for investment trusts.

The Board is responsible for ensuring the appropriate level of Corporate Governance and considers that the Company has complied with the best practice provisions of the Combined Code, other than in respect of the provision relating to the appointment of a senior independent director, and the AITC Code throughout the year under review.

## **Role of the Board**

A management agreement between the Company and JPMAM sets out the matters over which the Manager has authority. This includes management of the Company's assets and the provision of accounting, company secretarial, administration, and some marketing services. All other matters are reserved for the approval of the Board.

A formal schedule of matters reserved for Board decision has been approved during the year. This includes determination and monitoring of the Company's investment objectives and policy and its future strategic direction, gearing policy, management of the capital structure, appointment and removal of third party service providers, review of key investment and financial data and the Company's corporate governance and risk control arrangements.

The Board meets at least five times during the year and additional meetings are arranged as necessary. Full and timely information is provided to the Board to enable it to function effectively and to allow Directors to discharge their responsibilities.

There is an agreed procedure for Directors to take independent professional advice if necessary and at the Company's expense. This is in addition to the access that every Director has to the advice and services of the Company Secretary, JPMAM, which is responsible to the Board for ensuring that Board procedures are followed and that applicable rules and regulations are complied with.

## **Board Composition**

The Board consists of seven non-executive Directors, all of whom are regarded by the Board as independent of the Company's Manager, including the Chairman. The Directors have a breadth of investment, business and financial skills and experience relevant to the Company's business and biographical details of each Director are set out on page 18.

A review of Board composition and balance is included as part of the annual performance evaluation of the Board, details of which may be found below. The Board has considered whether a senior independent director should be appointed and has concluded that, as the Board comprises entirely of non-executive directors, this is unnecessary at present. The Board nominates one Director to lead the evaluation of the Chairman. Last year this was Liz Airey.

## **Tenure**

Directors are initially appointed until the following Annual General Meeting when, under the Company's Articles of Association, it is required that they be elected by shareholders. Thereafter, a Director's appointment will run for a maximum term of three years. Subject to the performance evaluation carried out each year, the Board will agree whether it is appropriate for the Director to seek an additional term. The Board does not believe that length of service in itself necessarily disqualifies a Director from seeking re-election but, when making a recommendation, the Board will take into account the ongoing requirements of the Combined Code, including the need to refresh the Board and its Committees. The Company's Articles

## Corporate Governance continued

of Association require that Directors stand for re-election at least every three years. Any Director who has served for a period of more than nine years will stand for annual re-election thereafter.

The terms and conditions of Directors' appointments are set out in formal letters of appointment, copies of which are available for inspection on request at the Company's registered office and at the AGM.

The Board recommends the election of Paul Manduca and Federico Marescotti, who were appointed on 1st December 2005. As a result of the Board's evaluation process described below, Michael Wrobel, who retires by rotation at this year's AGM, continues to be an effective Director and demonstrates commitment to his role and the Board recommends his re-election. Michael Hart retires by rotation but will not be seeking re-election.

### Meetings and Committees

The Board delegates certain responsibilities and functions to committees. Details of membership of committees are shown with the Directors' profiles on page 18.

The table below details the number of Board and Committee meetings attended by each Director. During the year there were five Board meetings, two Audit Committee meetings and one Nomination Committee meeting.

Director	Board Meetings attended	Audit Committee Meetings attended	Nomination Committee Meetings attended
Michael Hart	5	2	1
Elisabeth Airey	5	2	1
Anthony Davidson	5	2	1
Jacques Drossaert	5	2	1
Paul Manduca <sup>2</sup>	2	–	1
Federico Marescotti <sup>2</sup>	2	–	1
John Thornton <sup>1</sup>	3	1	–
Michael Wrobel	5	2	1

<sup>1</sup> retired 14th July 2005

<sup>2</sup> appointed 1st December 2005

### Training and Appraisal

On appointment, the Manager and Company Secretary provide all Directors with induction training if appropriate. Thereafter regular briefings are provided on changes in regulatory requirements that affect the Company and Directors. Directors are encouraged to attend industry and other seminars covering issues and developments relevant to investment trusts.

The Board has agreed procedures for the formal evaluation of the Manager, its own performance and of that of its committees and individual Directors. Questionnaires, drawn up by the Board, are completed by each Director, the responses are collated and then discussed at a private meeting. The evaluation of individual Directors is led by the Chairman, and a Director leads the evaluation of the Chairman's performance. The Board as a whole evaluates the Manager, its own performance and that of its committees.

## **Board Committees**

### **Nomination Committee**

The Nomination Committee, chaired by Michael Hart, consists of all of the Directors and meets at least annually to ensure that the Board has an appropriate balance of skills and experience to carry out its fiduciary duties and to select and propose suitable candidates for appointment when necessary. A variety of sources, including the use of external search consultants, may be used to ensure that a wide range of candidates are considered.

External Search Consultants were used in connection with the appointments of Federico Marescotti and Paul Manduca.

The Committee undertakes an annual performance evaluation to ensure that all members of the Board have devoted sufficient time and contributed adequately to the work of the Board. The Committee also reviews Directors' fees and makes recommendations to the Board as and when required.

### **Audit Committee**

The Audit Committee, chaired by Tony Davidson and whose membership is set out on page 18, meets at least twice each year. The members of the Audit Committee consider that they have the requisite skills and experience to fulfil the responsibilities of the Committee.

The Committee reviews the actions and judgements of the managers in relation to the interim and annual financial statements and the Company's compliance with the Combined Code. It reviews the terms of the management agreement and examines the effectiveness of the Company's internal control systems and receives information from the Managers' Compliance department. It also reviews the scope and results of the external audit, its cost effectiveness and the independence and objectivity of the external auditors, including the provision of non-audit services. Representatives of the Company's auditors attend the Committee meeting at which the draft Annual Report and

Accounts are considered. Each year, the Audit Committee reviews the independence of the Auditors and at present considers them to be independent. Following a recommendation by the Audit Committee, the Board approved an increase in the auditor's fees for the audit of these Financial Statements to £17,600 (2005: £16,000). This increase was approved as the time and costs associated with auditing investment trusts have increased due to the complexities of corporate governance and regulatory requirements.

The Directors' statement on the Company's system of internal control is set out below.

### **Terms of Reference**

Both the Nomination Committee and the Audit Committee have written terms of reference which define clearly their respective responsibilities, copies of which are available for inspection on request at the Company's registered office and at the Company's Annual General Meeting.

### **Relations with Shareholders**

The Board regularly monitors the shareholder profile of the Company. It aims to provide shareholders with a full understanding of the Company's activities and performance and reports formally to shareholders twice a year by way of the Annual Report and Accounts and the Interim Report. These are supplemented by the daily publication, through the London Stock Exchange, of the net asset value of the Company's shares.

All shareholders have the opportunity, and are encouraged, to attend the Company's Annual General Meeting at which the Directors and representatives of the Manager are available in person to meet shareholders and answer their questions. In addition, a presentation is given by the Investment Managers who review the Company's performance. During the year the Company's brokers, the Investment Managers and JPMAM hold regular discussions with larger shareholders. The Directors are made fully aware of their views. The Chairman and Directors make themselves available as and when required to

## Corporate Governance continued

address shareholder queries. The Directors may be contacted through the Company Secretary whose details are shown on page 52.

The Company's Annual Report and Accounts is published in time to give shareholders at least 20 working days' notice of the Annual General Meeting. Shareholders wishing to raise questions in advance of the meeting are encouraged to write to the Company Secretary at the address shown on page 52.

### **Internal Control**

The Combined Code requires the Directors, at least annually, to review the effectiveness of the Company's system of internal control and to report to shareholders that they have done so. This encompasses a review of all controls, which the Board has identified to include business, financial, operational, compliance and risk management controls.

The Directors are responsible for the Company's system of internal control, which is designed to safeguard the Company's assets, maintain proper accounting records and ensure that financial information used within the business, or published, is reliable. However, such a system can only be designed to manage rather than eliminate the risk of failure to achieve business objectives and therefore can only provide reasonable, but not absolute, assurance against fraud, material mis-statement or loss.

Since investment management, custody of assets and all administrative services are provided to the Company by JPMAM and its associates, the Company's system of internal control mainly comprises monitoring the services provided by JPMAM and its associates, including the operating controls established by them, to ensure they meet the Company's business objectives. The Company does not have an internal audit function of its own, but relies on the internal audit department of JPMAM. The key elements designed to provide effective internal control are as follows:

**Financial Reporting** – Regular and comprehensive review by the Board of key investment and financial data, including management accounts, revenue projections, analysis of transactions and performance comparisons.

**Management Agreement** – Appointment of a manager and custodian regulated by the Financial Services Authority (FSA), whose responsibilities are clearly defined in a written agreement.

**Management Systems** – The Managers' system of internal control includes organisational agreements which clearly define the lines of responsibility, delegated authority, control procedures and systems. These are monitored by JPMAM's Compliance Department which regularly monitors compliance with FSA rules.

**Investment Strategy** – Authorisation and monitoring of the Company's investment strategy and exposure limits by the Board.

The Board, either directly or through the Audit Committee, keeps under review the effectiveness of the Company's system of internal control by monitoring the operation of the key operating controls of the Manager and its associates by reviewing:

- the terms of the management agreement and receives regular reports from JPMAM's Compliance department;
- the report on the internal controls and the operations of its custodian, JPMorgan Chase Bank, which is itself independently reviewed; and
- every six months an independent report on the internal controls and the operations of JPMAM.

By means of the procedures set out above, the Board confirms that it has reviewed the effectiveness of the Company's system of internal control for the year ended 31st March 2006 and to the date of approval of this Annual Report and Accounts.

### **Corporate Governance and Voting Policy**

The Company delegates responsibility for voting to JPMAM. The following is a summary of JPMAM's policy statement on corporate governance and voting policy which has been noted by the Board. The full policy is available from JPMAM on request, or can be downloaded from [www.jpmorgan.com](http://www.jpmorgan.com):

*JPMAM is committed to delivering superior investment performance to its clients worldwide. We believe that one of the drivers of investment performance is an assessment of the corporate governance principles and practices of the companies in which we invest our clients' assets and we expect those companies to demonstrate high standards of governance in the management of their business.*

*Proxy voting is an important part of the corporate governance process, and we view seriously our obligation to manage the voting rights of the shares entrusted to us as we would manage any other asset. It is the policy of JPMAM to vote in a prudent and diligent manner, based exclusively on our reasonable judgement of what will best serve the financial interests of our clients. So far as is practicable we will vote at all of the meetings called by companies in which we are invested.*

*In order to do this we have formulated detailed guidelines for each region, which set out our stance on a variety of key corporate governance issues, including disclosure and transparency, board composition and independence, control structures, remuneration, as well as social and environmental issues (see below). These guidelines form the basis of our proxy voting decisions, although it should be noted that JPMAM makes all of its voting decisions on a case by case basis, taking into account the individual circumstances of each vote.*

### **Corporate Social Responsibility**

The following is a summary of JPMAM's policy statement on corporate social responsibility which has been noted by the Board:

*We believe it is our primary duty to act in the best financial interests of our clients and to achieve good financial returns consistent with an acceptable level of risk. We recognise that non-financial issues, such as social and environmental issues, can have an economic impact and that any company run in the long-term interests of its shareholders will need to manage effectively relationships with its employees, suppliers and customers, to behave ethically and to have regard to the environment and society as a whole. Our investment managers take these factors into account as part of any investment decision.*

# Directors' Remuneration Report

The Board has prepared this report in accordance with the requirements of Schedule 7A to the Companies Act 1985. An ordinary resolution to approve this report will be put to the members at the forthcoming Annual General Meeting.

The law requires the Company's auditors to audit certain of the disclosures provided. Where disclosures have been audited they are indicated as such. The auditors' opinion is included in their report on pages 35 and 36.

Directors' fees were last increased on 1st April 2005 and for the year under review are set out in the table below:

## Directors' Remuneration (Audited information)

Director's Name	2006 <sup>1</sup> £	2005 <sup>1</sup> £
Michael Hart	22,000	18,000
Elisabeth Airey	16,000	13,500
Anthony Davidson	15,559	–
Jacques Drossaert	16,000	13,500
John Thornton <sup>2</sup>	5,192	15,500
Paul Manduca <sup>3</sup>	5,333	–
Federico Marescotti <sup>3</sup>	5,333	–
Michael Wrobel	16,000	13,500
<b>Total</b>	<b>101,417</b>	<b>74,000</b>

<sup>1</sup>Audited information.

<sup>2</sup>Retired as a Director on 14th July 2005.

<sup>3</sup>Appointed as a Director on 1st December 2005.

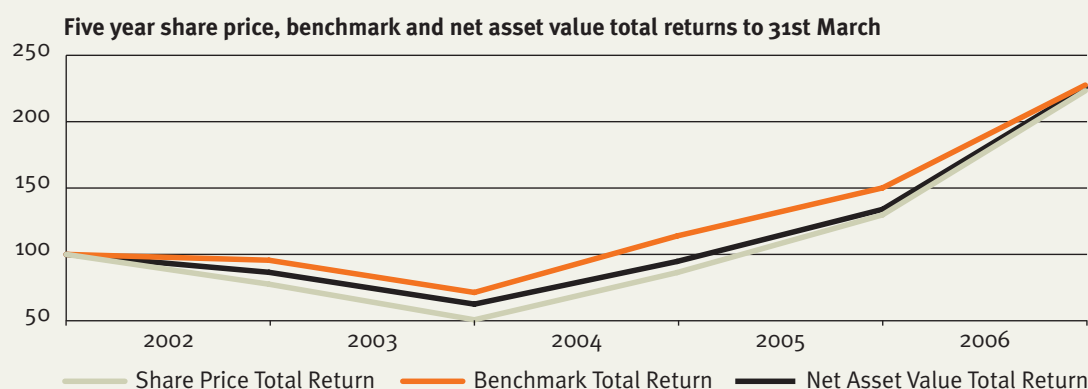
The total Directors fee of £101,417 (2004: £74,000) in respect of aggregate emoluments have been paid to Directors. Total fees of £nil (2004: £nil) have been paid to third parties for making available the

services of Directors. Having carried out a full fee review, the Board has agreed to increase the fees with effect from 1st April 2006 to: Chairman £25,000 per annum, Chairman of Audit Committee £20,000 per annum and other Directors £18,000 per annum.

As all of the Directors are non-executive, the Board has not established a Remuneration Committee. Instead, the Nomination Committee reviews Directors' fees on a regular basis and makes recommendations to the Board as and when appropriate. Reviews are based on information provided by the Manager, JPMAM, and relevant third parties on the level of fees paid to the directors of the Company's peers and within the investment trust industry generally. The Directors' fees are not performance-related. The Articles stipulate that aggregate fees must not exceed £125,000 per annum. The Directors have agreed to increase this aggregate fee level to £175,000 and have included a resolution in the forthcoming AGM. Any increase in the maximum aggregate amount requires both Board and shareholder approval.

The Company does not operate any type of incentive or pension scheme and therefore no Directors receive bonus payments or pension contributions from the Company or hold options to acquire shares in the Company. Directors are not paid compensation for loss of office. No other payments are made to Directors, other than the reimbursement of reasonable out-of-pocket expenses incurred in connection with attending the Company's business.

A graph showing the Company's share price and net asset value total returns compared with its benchmark index, the HSBC Smaller European Companies (ex UK) Index<sup>1</sup>, over the last five years is shown below.



<sup>1</sup>The Company's benchmark is the HSBC Smaller European Companies (ex UK) Index. This is a recognised index of stocks that has been selected by the Board as the benchmark against which the Company's performance is judged, although it should not be taken as wholly representative of the Company's investment universe.

By order of the Board  
Hilary Lowe, for and on behalf of  
JPMorgan Asset Management (UK) Limited, Secretary  
2nd June 2006

# Statement of Directors' Responsibilities in Respect of the Accounts

Company law requires the Directors to prepare accounts for each financial year in accordance with United Kingdom Generally Accepted Accounting Practice which give a true and fair view of the state of affairs of the Company as at the end of the year and of the revenue for the year. In preparing those accounts, the Directors are required to:

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

The Directors confirm that the accounts comply with the above requirements. The Directors are responsible for ensuring that proper accounting records are kept which disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the accounts comply with the Companies Act 1985. 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.

Pursuant to Section 5234 ZA (2) of the Companies Act 1985, each of the Directors confirm that:

- so far as they are aware, there is no relevant information of which the Company's Auditors are not aware; and
- they have taken all steps they ought to have taken to make themselves aware of any relevant audit information and to establish that the Company's Auditors are aware of such information.

# Notice of Annual General Meeting

Notice is hereby given that the seventeenth Annual General Meeting of JPMorgan Fleming European Fledgeling Investment Trust plc will be held at The Library, JPMorgan, 60 Victoria Embankment, London EC4Y 0JP on Wednesday 12th July 2006 at 12.00 noon for the following purposes:

- 1 To receive the Directors' Report, the Annual Accounts and the Auditors' Report for the year ended 31st March 2006.
- 2 To approve the Remuneration Report for the year ended 31st March 2006.
- 3 To elect Paul Manduca as a Director of the Company.
- 4 To elect Federico Marescotti as a Director of the Company.
- 5 To re-elect Michael Wrobel as a Director of the Company.
- 6 To re-appoint PricewaterhouseCoopers LLP as Auditors to the Company and to authorise the Directors to determine their remuneration.

## Special Business

To consider the following special resolutions:

Authority to repurchase shares

- 7 THAT the Company be generally and subject as hereinafter appears unconditionally authorised in accordance with Section 166 of the Companies Act 1985 (the 'Act') to make market purchases (within the meaning of Section 163 of the Act) of its issued ordinary shares of 25 pence each in the capital of the Company.

PROVIDED ALWAYS THAT

- (i) the maximum number of ordinary shares hereby authorised to be purchased shall be 7,911,949 or if less, that number of ordinary shares which is equal to 14.99% of the Company's issued share capital as at the date of the passing of this resolution;
- (ii) the minimum price which may be paid for an ordinary share shall be 25 pence;
- (iii) the maximum price which may be paid for an ordinary share shall be an amount equal to 105 per cent of the average of the middle market quotations for an ordinary share taken from and calculated by

reference to the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the ordinary share is purchased or (b) the price of the last independent trade; or (c) the highest current independent bid;

- (iv) any purchase of ordinary shares will be made in the market for cash at prices below the prevailing net asset value per ordinary share (as determined by the Directors) at the date following not more than seven days before the date of purchase;
- (v) the authority hereby conferred shall expire on 11th January 2008 unless the authority is renewed at the Company's Annual General Meeting in 2007 or at any other general meeting prior to such time; and
- (vi) the Company may make a contract to purchase ordinary shares under the authority hereby conferred prior to the expiry of such authority and may make a purchase of ordinary shares pursuant to any such contract notwithstanding such expiry.

Authority to sell ordinary shares from treasury

- 8 THAT the Directors of the Company be authorised, for the purposes of paragraph 21.21 of the Listing Rules of the United Kingdom Listing Authority, to sell ordinary shares of 25p each in the capital of the Company at a price below the net asset value per share of the existing ordinary shares in issue, provided always that such issue will be limited to:
  - (i) up to an aggregate nominal amount of £1,319,538, representing approximately 10% of the total ordinary share capital in issue as at the date of the passing of this resolution;
  - (ii) the sale of shares which, immediately before such sale, were held by the Company as treasury shares; and
  - (iii) such number of ordinary shares and such reissue prices that the aggregate dilution associated with all the reissues does not exceed 3.54 pence per share, being approximately 0.5% of the net asset value per share as at 31st March 2006.

**9 Authority to disapply pre-emption rights on sale of ordinary shares from treasury**  
THAT subject to the passing of Resolution 12 set out above, the Directors of the Company be and they are hereby empowered pursuant to Section 95 of the Act to allot (within the meaning of Section 94(3A) of the Act) equity securities (within the meaning of Section 94(2) of the Act) wholly for cash as if Section 89(1) of the Act did not apply to any such sale, provided that this power shall be limited to the allotment (within the meaning of Section 94(3A) of the Act) of equity securities for cash out of treasury up to an aggregate nominal amount of £1,319,538, representing approximately 10% of the Company's total ordinary share capital in issue as at the date of the passing of this resolution and shall expire on the earlier of the conclusion of the Annual General Meeting of the Company to be held in 2007, or fifteen months after the date of the passing of this resolution, save that the Company may before such expiry make offers, agreements or arrangements which would or might require equity securities to be allotted after such expiry and so that the Directors of the Company may allot equity securities in pursuance of such offers, agreements or arrangements as if the power conferred hereby had not expired.

- 10 Authority to increase the maximum aggregate Directors' fees**  
THAT in accordance with the Company's Article 90 of the Articles of Association, the maximum aggregate Directors' fees payable be increased from £125,000 to £175,000 per annum with immediate effect.
- 11 Authority to change the name of the Company**  
THAT subject to the consent of the Registrar of Companies the name of the Company be changed to 'JPMorgan European Fledgeling Investment Trust plc'.

By order of the Board  
Hilary Lowe, for and on behalf of  
JPMorgan Asset Management (UK) Limited,  
Secretary  
2nd June 2006

## Notice of Annual General Meeting continued

### Notes

- 1** A member entitled to attend and vote at the above meeting is entitled to appoint one or more proxies to attend and on a poll vote on their behalf. A proxy need not be a member of the Company. The lodging of a form of proxy does not prevent a member from attending and voting if he so wishes.
- 2** Any instrument appointing a proxy, to be valid, must be lodged at the Company's Registrar not less than 48 hours before the time of the meeting.
- 3** To be entitled to attend and vote at the Meeting (and for the purpose of the determination by the Company of the number of votes they may cast), members must be entered on the Company's register of members as at 6.00 p.m. on 18th July 2006 (the 'specified time'). If the meeting is adjourned to a time not more than 48 hours after the specified time applicable to the original meeting, that time will also apply for the purpose of determining the entitlement of members to attend and vote (and for the purpose of determining the number of votes they may cast) at the adjourned meeting. If however the meeting is adjourned for a longer period then, to be so entitled, members must be entered on the Company's register of members as at 6.00 p.m. two days prior to the adjourned meeting or, if the Company gives notice of the adjourned meeting, at the time specified in that notice.
- 4** Entry to the above Meeting will be restricted to shareholders, with guests admitted only by prior arrangement.  

A corporation, which is a shareholder, may appoint an individual to act as its representative and to vote in person at the meeting. The appointment must comply with section 375 of the Companies Act 1985. The representative should bring to the meeting evidence of his or her appointment, including any authority under which it is signed, unless previously given to the Company's registrars.
- 5** The register of interests of the Directors and connected persons in the share capital of the Company is available for inspection at the Company's registered office during usual business hours on any weekday (Saturdays and public holidays excepted). It will also be available for inspection at the Annual General Meeting.

- 6** No Director has any contract of service with the Company.

#### *Electronic appointment – CREST members*

CREST members who wish to appoint a proxy or proxies by utilising the CREST electronic proxy appointment service may do so for the Meeting and any adjournment(s) thereof by using the procedures described in the CREST Manual. CREST personal members or other CREST sponsored members, and those CREST members who have appointed (a) voting service provider(s) who will be able to take the appropriate action on their behalf.

In order for a proxy appointment made using the CREST service to be valid, the appropriate CREST message (a 'CREST Proxy Instruction') must be properly authenticated in accordance with CRESTCo's CREST Manual. The CREST message must be transmitted so as to be received by the issuer's agent (ID7RA01) by not later than 48 hours before the time appointed for the holding of the meeting or the adjourned meeting. For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp applied to the CREST message by the CREST Applications Host) from which the issuer's agent is able to retrieve the CREST message by enquiry to CREST in the manner prescribed by CREST. After this time any change of instructions to proxies appointed through CREST should be communicated to the appointee through other means.

CREST members and, where applicable, their CREST sponsors or voting service provider(s), should note that CRESTCo does not make available special procedures in CREST for any particular messages. Normal system timing and limitations will therefore apply in relation to the input of CREST Proxy Instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member(s) is/are a CREST personal member or sponsored member or has appointed (a) voting service provider(s), to procure that the CREST sponsor or voting service provider takes) such action as shall be necessary to ensure that a CREST message is transmitted by means of the CREST system by any particular time. In this connection, CREST members and, where applicable, their CREST sponsors or voting service provider(s) is/are referred, in particular, to those sections of the CREST Manual concerning practical limitations of the CREST system and timings.

The Company may treat as invalid a CREST Proxy Instruction in the circumstances set out in Regulation 35(5) (a) of the Uncertificated Securities Regulations 2001.

# Independent Auditors' Report<sup>1</sup>

## **To the shareholders of JPMorgan Fleming European Fledgeling Investment Trust plc**

We have audited the accounts of the JPMorgan Fleming European Fledgeling Investment Trust plc for the year ended 31st March 2006 which comprise the Income Statement, the Reconciliation of Movements in Shareholders' Funds, the Balance Sheet, the Cash Flow Statement and the related notes. These accounts have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

## **Respective Responsibilities of Directors' and Auditors**

The Directors' responsibilities for preparing the Annual Report and the accounts in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities. The Directors are also responsible for preparing the Directors' Remuneration Report.

Our responsibility is to audit the accounts and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, 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.

We report to you our opinion as to whether the accounts give a true and fair view and whether the accounts and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the

Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is consistent with the accounts, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and other transactions is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Company's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited accounts. The other information comprises only the Chairman's Statement, the Investment Managers' Report, the Directors' Report, the Corporate Governance Statement and the unaudited part of the Directors' Remuneration Report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts. Our responsibilities do not extend to any other information.

## **Basis of Audit Opinion**

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the accounts, and of whether

## Independent Auditors' Report<sup>1</sup> continued

the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts and the part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts and the part of the Directors' Remuneration Report to be audited.

### **Opinion**

In our opinion:

- the accounts give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 31st March 2006 and of its net return and cash flows for the year then ended;
- the accounts and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the accounts.

### **PricewaterhouseCoopers LLP**

Chartered Accountants and  
Registered Auditors  
London  
2nd June 2006

<sup>1</sup> The accounts are published on the [www.jpmorgan.com/its](http://www.jpmorgan.com/its) website, which is a website maintained by the Company's Manager, JPMorgan Asset Management (UK) Limited ('JPMAM'). The maintenance and integrity of the website maintained by JPMAM or any of its subsidiaries is, so far as it relates to the Company, the responsibility of JPMAM. The work carried out by the auditors does not involve consideration of the maintenance and integrity of this website or any other website upon which the accounts may be published and accordingly, the auditors accept no responsibility for any changes that may occur to the accounts following presentation on a website. Visitors to any website containing the accounts need to be aware that legislation in the United Kingdom governing the preparation and dissemination of the accounts may differ from legislation in their jurisdiction.

# Income Statement

for the year ended 31st March 2006

	Notes	Revenue Return £'000	2006 Capital Return £'000	Total Return £'000	Revenue Return £'000	2005 Capital Return £'000	Total Return £'000
Realised gains on investments	7,11	–	54,938	54,938	–	26,087	26,087
Unrealised gains on investments	7,11	–	96,077	96,077	–	40,786	40,786
Currency gains/(losses) on cash and short term deposits held during the year	11	–	240	240	–	(823)	(823)
Unrealised loss on currency hedge	11	–	(7)	(7)	–	(39)	(39)
Realised currency losses on Euro loans		–	–	–	–	(393)	(393)
Other capital charges	11	–	(54)	(54)	–	–	–
Income from investments	1	4,667	–	4,667	4,156	–	4,156
Other income	1	231	–	231	62	–	62
<b>Gross revenue and capital return</b>		<b>4,898</b>	<b>151,194</b>	<b>156,092</b>	4,218	65,618	69,836
Management fee	2	(3,159)	–	(3,159)	(1,899)	–	(1,899)
Other administrative expenses	3	(592)	–	(592)	(439)	–	(439)
<b>Net return before finance costs and taxation</b>		<b>1,147</b>	<b>151,194</b>	<b>152,341</b>	1,880	65,618	67,498
Finance costs	4	(525)	–	(525)	(970)	–	(970)
<b>Net return before taxation</b>		<b>622</b>	<b>151,194</b>	<b>151,816</b>	910	65,618	66,528
Taxation	5	(406)	–	(406)	(819)	–	(819)
<b>Total return attributable to ordinary shareholders</b>		<b>216</b>	<b>151,194</b>	<b>151,410</b>	91	65,618	65,709
<b>Return per ordinary share</b>	6	<b>0.41p</b>	<b>286.38p</b>	<b>286.79p</b>	0.17p	121.70p	121.87p

All revenue and capital items in the above statement derive from continuing operations. No operations were acquired or discontinued in the year.

The total column of this statement is the Profit and Loss Account of the Company, and the revenue and capital columns represent supplementary information. The capital column represents all the information that is required to be disclosed in a 'Statement of Total Recognised Gains and Losses (STRGL)'. For this reason a STRGL has not been presented.

*The notes on pages 41 to 51 form part of these accounts.*

# Reconciliation of Movements in Shareholders' Funds

for the year ended 31st March 2006

	Called up Share Capital £'000	Share Premium £'000	Capital redemption reserve £'000	Other reserve £'000	Capital reserve – realised £'000	Capital reserve – unrealised £'000	Revenue reserve £'000	Total £'000
<b>At 31st March 2004</b>	13,629	–	2,007	32,912	95,665	27,350	(8,990)	<b>162,573</b>
Shares bought back and cancelled	(238)	–	238	(2,348)	–	–	–	<b>(2,348)</b>
Net capital return from ordinary activities	–	–	–	–	37,833	27,785	–	<b>65,618</b>
Net revenue return from ordinary activities	–	–	–	–	–	–	91	<b>91</b>
<b>At 31st March 2005</b>	13,391	–	2,245	30,564	133,498	55,135	(8,899)	<b>225,934</b>
Adjustment to reflect the adoption of bid prices	–	–	–	–	–	(752)	–	<b>(752)</b>
Repurchase of shares into treasury	–	–	–	(1,623)	–	–	–	<b>(1,623)</b>
Sale of shares from treasury	–	91	–	675	–	–	–	<b>766</b>
Shares bought back and cancelled	(196)	–	196	(2,765)	–	–	–	<b>(2,765)</b>
Net capital return from ordinary activities	–	–	–	–	82,717	68,477	–	<b>151,194</b>
Net revenue return from ordinary activities	–	–	–	–	–	–	216	<b>216</b>
<b>At 31st March 2006</b>	<b>13,195</b>	<b>91</b>	<b>2,441</b>	<b>26,851</b>	<b>216,215</b>	<b>122,860</b>	<b>(8,683)</b>	<b>372,970</b>

# Balance Sheet

at 31st March 2006

	Notes	2006 £'000	2005 £'000
<b>Fixed assets</b>			
Investments at fair value through profit or loss	7	<b>387,213</b>	237,033
<b>Current assets</b>			
Debtors	8	<b>10,098</b>	28,952
Cash and short term deposits		<b>2,417</b>	13,825
		<b>12,515</b>	42,777
<b>Creditors: Amounts falling due within one year</b>	9	<b>(26,758)</b>	(53,876)
<b>Net current liabilities</b>		<b>(14,243)</b>	(11,099)
<b>Total assets less current liabilities</b>		<b>372,970</b>	225,934
<b>Total net assets attributable to shareholders</b>		<b>372,970</b>	225,934
<b>Capital and reserves</b>			
Called-up share capital	10	<b>13,195</b>	13,391
Share premium account	11	<b>91</b>	–
Capital redemption reserve	11	<b>2,441</b>	2,245
Other reserve	11	<b>26,851</b>	30,564
Capital reserve – realised	11	<b>216,215</b>	133,498
Capital reserve – unrealised	11	<b>122,860</b>	55,135
Revenue reserve	11	<b>(8,683)</b>	(8,899)
<b>Total equity shareholders' funds</b>		<b>372,970</b>	225,934
<b>Net asset value per share</b>	12	<b>709.0p</b>	421.8p

The accounts on pages 37 to 51 were approved by the Directors on 2nd June 2006 and are signed on their behalf by:

Michael Wrobel  
Director

*The notes on pages 41 to 51 form part of these accounts.*

# Cash Flow Statement

for the year ended 31st March 2006

	Notes	2006 £'000	2005 £'000
<b>Operating activities</b>			
Cash received from investments		4,128	3,261
Deposit interest received		168	10
Stocklending fees received		63	52
Management fee paid		(2,761)	(1,642)
Directors' fees paid		(101)	(74)
Other cash payments		(944)	(588)
<b>Net cash inflow from operating activities</b>	13	553	1,019
<b>Servicing of finance</b>			
Interest paid		(556)	(1,025)
<b>Net cash outflow from servicing of finance</b>		(556)	(1,025)
<b>Taxation</b>			
Overseas tax recovered		184	211
<b>Total tax recovered</b>		184	211
<b>Financial investment</b>			
Purchases of investments		(445,951)	(350,094)
Sales of investments		461,768	346,407
Other capital items		(60)	10
<b>Net cash inflow/(outflow) from financial investment</b>		15,757	(3,677)
<b>Net cash inflow/(outflow) before financing</b>		15,938	(3,472)
<b>Financing</b>			
Loans (repaid)/drawn down		(23,925)	20,205
Repurchase of shares for cancellation		(2,765)	(2,348)
Repurchase of shares into treasury		(1,623)	–
Sale of shares from treasury		766	–
<b>Net cash (outflow)/inflow from financing</b>		(27,547)	17,857
<b>(Decrease)/increase in cash for the year</b>	13	(11,609)	14,385

The notes on pages 41 to 51 form part of these accounts.

# Notes to the Accounts

for the year ended 31st March 2006

## ACCOUNTING POLICIES

### **i. Basis of accounting**

The accounts are prepared under the historic cost convention, modified to include the revaluation of investments and in accordance with the Companies Act 1985, United Kingdom Generally Accepted Accounting Practice ('UK GAAP') and with the Statement of Recommended Practice 'Financial statements of investment trust companies' (SORP) as issued by the AITC in December 2005.

The Company has adopted certain new accounting policies due to the issue of new financial reporting standards (FRSs).

The SORP and the listing rules have also given rise to some changes in the presentation. The Statement of Total Return is now called the Income Statement and the total return column, as opposed to the revenue column, is now the profit and loss account of the Company. There is a new primary statement, the Reconciliation of Movements in Shareholders' Funds.

### **ii. Valuation of investments**

Investments are designated as held at fair value through profit or loss in accordance with FRS 26: 'Financial Instruments: Measurement'. Listed investments are valued at bid market prices. This represents a change in accounting policy, however in accordance with the exemption conferred by paragraph 108D of FRS 26, comparatives have not been restated. In prior years, listed investments were valued using last trade prices. The adoption of bid prices on 1st April 2005 decreased the investments by £752,000 as shown in note 7.

Where trading in the securities of an investee company is suspended, the investment is valued at the Board's estimate of its net realisable value. Realised surpluses or deficits on the disposal of investments and permanent impairments in the value of investments are taken to the capital reserve – realised. Unrealised surpluses and deficits on the revaluation of investments are taken to the capital reserve – unrealised.

### **iii. Income**

Dividends from equity shares are included in the revenue on an ex-dividend basis, with overseas dividends being accounted for gross of withholding tax.

Where the Company has elected to receive scrip dividends in the form of additional shares rather than in cash, the amount of the cash dividend foregone is recognised as income. Any excess in the value of the shares received over the amount of the cash dividend foregone is recognised in capital reserves.

Special dividends are recognised on an ex-dividend basis and treated as a capital item or an income item depending on the facts and circumstances of each dividend.

Interest receivable on deposits is recognised in revenue on an accruals basis.

Stock lending income is recognised in revenue on a receipts basis.

## Notes to the Accounts continued

### **iv. Expenses**

All expenses are accounted for on an accruals basis. Expenses are allocated wholly to revenue, with the following exceptions:

- expenses incidental to the acquisition of an investment are included within the cost of the investment, and those incidental to the sale of an investment are deducted from the sales proceeds of the investment. These expenses are commonly referred to as ‘transaction costs’, and include items such as stamp duty and broker commissions. In accordance with FRS 26 and the SORP, disclosure of transaction costs is now required and can be found in note 7.

### **v. Finance costs**

Finance costs are accounted for on an accruals basis and in accordance with the provisions of FRS 25 ‘Financial instruments: Disclosure and presentation’ and FRS 26 ‘Financial instruments: Measurement’.

Finance costs are allocated wholly to revenue.

### **vi. Financial instruments**

The Company has not utilised any derivative instruments in the current or comparative years.

Where permitted, the Company has excluded short term debtors and creditors from the analysis of financial instruments in note 15.

### **vii. Taxation**

Deferred tax is accounted for in accordance with FRS 19 ‘Deferred tax’. Deferred tax is provided on all timing differences that have originated but not reversed by the balance sheet date. Deferred tax liabilities are recognised for all taxable timing differences but deferred tax assets are only recognised to the extent that it is probable that taxable profits will be available against which those timing differences can be utilised.

### **viii. Foreign currency**

The Directors, having regard to the currency of the Company’s share capital and the predominant currency in which its shareholders operate, have determined the functional currency to be sterling.

Transactions denominated in foreign currencies are converted at actual exchange rates as at the date of the transaction. Assets and liabilities denominated in foreign currencies at the year end are translated at the rates of exchange prevailing at the year end.

Any gain or loss arising from a change in exchange rates subsequent to the date of the transaction is included as an exchange gain or loss in the capital reserve or in the revenue account depending on whether the gain or loss is of capital or revenue nature.

	<b>2006</b>	2005
	<b>£'000</b>	£'000
<b>1. Income</b>		
Income from investments		
Overseas dividends	<b>4,328</b>	4,041
Scrip dividends	<b>339</b>	115
	<b>4,667</b>	4,156
Other income		
Deposit interest	<b>168</b>	10
Stocklending fees	<b>63</b>	52
	<b>231</b>	62
Total income comprises:		
Dividends	<b>4,667</b>	4,156
Other income	<b>231</b>	62
	<b>4,898</b>	4,218
Analysis of income from investments:		
Listed overseas	<b>4,898</b>	4,156
	<b>4,898</b>	4,156
	<b>2006</b>	2005
	<b>£'000</b>	£'000
<b>2. Management fee</b>		
Management fee	<b>2,750</b>	1,653
Irrecoverable VAT thereon	<b>409</b>	246
	<b>3,159</b>	1,899
	<b>2006</b>	2005
	<b>£'000</b>	£'000
<b>3. Administrative expenses<sup>1</sup></b>		
Other administration expenses	<b>379</b>	240
Directors' fees	<b>101</b>	74
Auditors' remuneration <sup>2</sup>	<b>20</b>	18
Savings product <sup>3</sup>	<b>92</b>	107
	<b>592</b>	439

<sup>1</sup>Expenses have been adjusted to include irrecoverable VAT.

<sup>2</sup>Fees amounting to £4,000 (2005: £6,000) including VAT were payable to the auditors in respect of services not directly connected with the audit. These amounts are included in other administration expenses.

<sup>3</sup>Paid to JPMAM for the marketing of 'wrapper' products.

## Notes to the Accounts continued

	<b>2006</b>	2005
	<b>£'000</b>	£'000
<b>4. Finance costs</b>		
Overdraft interest	<b>109</b>	122
Short term loan interest	<b>416</b>	848
	<b>525</b>	970

	<b>2006</b>	2005
	<b>£'000</b>	£'000
<b>5. Taxation</b>		
UK Corporation tax at 30% (2005: 30%)	<b>464</b>	392
Relief relating to overseas taxation	<b>(464)</b>	(392)
	-	-
Overseas taxation	<b>406</b>	819
Total current tax	<b>406</b>	819

The tax assessed for the year is lower than the standard rate of corporation tax in the UK of 30%. The differences are explained below:

	<b>2006</b>	2005
	<b>£'000</b>	£'000
Net return before taxation	<b>151,816</b>	66,528
Net return before taxation multiplied by the standard rate of corporation tax of 30% (2005: 30%)	<b>45,545</b>	19,958
Non taxable capital return	<b>(45,358)</b>	(19,685)
Non taxable scrip dividends	<b>(102)</b>	(35)
Income taxed in different periods	<b>107</b>	(66)
Excess revenue expenses not relieved	<b>272</b>	220
Overseas tax relief taken	<b>(464)</b>	(392)
Overseas taxation	<b>406</b>	819
Total current tax	<b>406</b>	819

The Company has an unrecognised deferred tax asset of £3,444,000 (2005: £3,172,000). This has arisen from deductible expenses exceeding taxable income. Based on the current composition of the portfolio, these expenses are unlikely to be utilised.

	2006			2005		
	Revenue Return £'000	Capital Return £'000	Total Return £'000	Revenue Return £'000	Capital Return £'000	Total Return £'000
<b>6. Return per ordinary share</b>						
Attributable to ordinary shareholders	<b>216</b>	<b>151,194</b>	<b>151,410</b>	91	65,618	65,709
Return per ordinary share	<b>0.41p</b>	<b>286.38p</b>	<b>286.79p</b>	0.17p	121.70p	121.87p

The revenue return per ordinary share is based on the revenue on ordinary activities after taxation and on 52,794,594 (2005: 53,917,460) ordinary shares, being the weighted average number of ordinary shares in issue during the year.

The capital return per ordinary share is based on net capital returns and on 52,794,594 (2005: 53,917,460) ordinary shares, being the weighted average number of ordinary shares in issue during the year.

	2006 £'000	2005 £'000
<b>7. Investments</b>		
Listed investments	<b>387,213</b>	237,033

a) Analysis of investments:

	Listed overseas £'000
Opening book cost	<b>181,858</b>
Opening unrealised gains	<b>55,175</b>
Opening valuation	<b>237,033</b>
Movements in the year:	
Adjustment to reflect the adoption of bid prices	(752)
Purchases at cost	<b>446,666</b>
Sales – proceeds	<b>(446,749)</b>
– realised gains	<b>54,938</b>
Change in unrealised gains	<b>96,077</b>
	<b>387,213</b>
Closing book cost	<b>264,346</b>
Closing unrealised gains	<b>122,867</b>
Closing valuation	<b>387,213</b>

Transaction costs on purchases during the year amounted to £913,000 (2005: £941,000) and on sales during the year amounted to £965,000 (2005: £743,000). These costs include stamp duty and broker commission and are included in purchases and netted off against sales in the above note.

During the year £27,632,000 of prior year unrealised gains have been transferred to realised gains as disclosed in note 11.

## Notes to the Accounts continued

### 7. Investments continued

#### b) Stocklending details:

	<b>2006</b>	2005
	<b>£'000</b>	£'000
Fee income (net) from stocklending during the year	<b>63</b>	52

The aggregate value of securities on loan as at 31st March 2006 amounted to £13,744,000 (2005: £14,074,000) and the maximum value of stock on loan during the year ended 31st March 2006 was £22,513,000 (2005: £22,531,000). Collateral, with a value equivalent to a minimum of 105% of the outstanding value of stocks on loan, is obtained by JPMorgan Chase. Collateral is held in the form of certificates of deposit, letters of credit or bonds.

#### Significant interests

At 31st March 2006 the Company held 3% or more of a class of units of the following investment funds which are valued in the accounts at mid market price. The investments did not represent participating interests.

Name of Company	Country of registration	% held	
		<b>2006</b>	2005
JPM Europe Micro Cap Fund <sup>1</sup>	Luxembourg	<b>40</b>	–
Fleming Frontier European Discovery Fund	Luxembourg	–	40
HIQ	Sweden	<b>5</b>	2
Transcom Worldwide	Sweden	<b>3</b>	–
Fuchs Petrol	Germany	<b>3</b>	1

<sup>1</sup>During the year the holdings of Fleming Frontier European Discovery Fund were converted into JPM Europe Micro Cap Fund.

	<b>2006</b>	2005
	<b>£'000</b>	£'000
<b>8. Debtors</b>		
Sales for future settlement	<b>3,317</b>	18,336
Currency receivable	<b>6,359</b>	9,832
Overseas tax recoverable	<b>17</b>	65
Dividends and interest receivable	<b>358</b>	700
Other debtors	<b>47</b>	19
	<b>10,098</b>	28,952

	<b>2006</b>	2005
	<b>£'000</b>	£'000
<b>9. Creditors: Amounts falling due within one year</b>		
Purchases for future settlement	<b>9,795</b>	9,419
Currency payable	<b>6,366</b>	9,871
Loan interest payable	<b>1</b>	32
Short term loans <sup>1</sup>	<b>10,465</b>	34,390
Accrued expenses	<b>117</b>	144
Other creditors	<b>14</b>	20
	<b>26,758</b>	53,876

<sup>1</sup>The Company arranged a Euro 70 million loan facility on 16th November 2005 with ING Bank. Interest is chargeable at LIBOR plus a margin and the facility expires on 15th November 2006. As at 31st March 2006 the Company had drawn down 15 million Euros on this facility at an interest rate of 3.03%.

As at 31st March 2005 the Company had a Euro 50 million loan facility with ING Bank at an interest rate of LIBOR plus a margin. This facility expired on 17th November 2005.

At 31st March 2005, the whole Euro 50 million had been drawn down at an interest rate of 2.48%.

	<b>2006</b>	2005
	<b>£'000</b>	£'000
<b>10. Called up share capital</b>		
Authorised share capital:		
280,000,000 ordinary shares of 25p each	<b>70,000</b>	70,000
Issued and fully paid share capital:		
Opening balance	<b>13,391</b>	13,629
Repurchase of 785,000 (2005: 950,000) ordinary shares	<b>(196)</b>	(238)
Repurchase of 300,000 shares into treasury (2005: Nil)	<b>(75)</b>	–
Sale of 125,000 shares from treasury (2005: Nil)	<b>31</b>	–
Subtotal	<b>13,151</b>	13,391
Repurchase of 300,000 shares into treasury (2005: Nil)	<b>75</b>	–
Sale of 125,000 shares from treasury (2005: Nil)	<b>(31)</b>	–
Closing balance <sup>1</sup>	<b>13,195</b>	13,391

<sup>1</sup>Represented by 52,781,517 (2005: 53,566,517) ordinary shares of 25p each including 175,000 shares held in treasury (2005: nil)

## Notes to the Accounts continued

	2006					
	Share premium	Capital redemption reserve	Other reserve	Capital reserve – realised	Capital reserve – unrealised	Revenue reserve
	£'000	£'000	£'000	£'000	£'000	£'000
<b>11. Reserves</b>						
Opening balance	–	2,245	30,564	133,498	55,135	(8,899)
Adjustment at 1st April 2005 to reflect the adoption of bid prices	–	–	–	–	(752)	–
Net currency gains on cash and short-term deposits held during the year	–	–	–	240	–	–
Realised gains on investments	–	–	–	54,938	–	–
Unrealised gains on investments	–	–	–	–	96,077	–
Transfer on disposal of investments	–	–	–	27,632	(27,632)	–
Unrealised loss on currency hedge	–	–	–	–	(7)	–
Unrealised losses now realised on currency hedge	–	–	–	(39)	39	–
Repurchase of shares into treasury	–	–	(1,623)	–	–	–
Sale of shares from treasury	91	–	675	–	–	–
Shares bought back and cancelled	–	196	(2,765)	–	–	–
Other capital charges	–	–	–	(54)	–	–
Retained net revenue for the year	–	–	–	–	–	216
<b>Closing balance</b>	<b>91</b>	<b>2,441</b>	<b>26,851</b>	<b>216,215</b>	<b>122,860</b>	<b>(8,683)</b>

## 12. Net asset value per share

The net asset value per share at the year end, is as follows:

	Net asset value per share		Net asset values attributable	
	2006 p	2005 p	2006 £'000	2005 £'000
Ordinary shares	<b>709.0</b>	421.8	<b>372,970</b>	225,934

The net asset value per share is based on net assets at the year end and on 52,606,517 (2005: 53,566,517) ordinary shares, being the number of ordinary shares in issue at the year end, excluding shares held in treasury.

<b>2006</b>	2005
<b>£'000</b>	£'000

### 13. Cash flow statement

Reconciliation of net return before finance costs and taxation to net cash inflow from operating activities

Net return before finance costs and taxation	<b>152,341</b>	67,498
Capital return before finance costs and taxation	<b>(151,194)</b>	(65,618)
Scrip dividends received	<b>(339)</b>	(115)
Decrease/(increase) in accrued income	<b>342</b>	(196)
Increase in other debtors	<b>(28)</b>	(14)
(Decrease)/increase in accrued expenses	<b>(27)</b>	48
Tax suffered on overseas income received	<b>(542)</b>	(584)
Net cash inflow from operating activities	<b>553</b>	1,019

Analysis of net debt	At 1st April	Cash flow	Exchange	At 31st March
	2005		movement	2006
	£'000	£'000	£'000	£'000
Cash and short-term deposits	13,825	(11,609)	201	<b>2,417</b>
Debt due within one year	(34,390)	23,925	–	<b>(10,465)</b>
Total	(20,565)	12,316	201	<b>(8,048)</b>

### 14. Transactions with JPMorgan

Details of the management contract are set out on page 22. Investments in funds managed by JPMAM are deducted from the Company's market capitalisation used as the basis for calculating the fee. There were no amounts due to JPMAM at the year end (2005: £11,000). The management fee payable to JPMAM for the year can be found in note 2, page 43. In addition, £92,000 including VAT was payable to JPMAM for the marketing and administration of "wrapper" products (2005: £107,000). Safe custody fees and other charges amounting to £230,000 (2005: £135,000) were payable to third party custodians on behalf of JPMAM, of which £54,000 (2005: £65,000) was outstanding at the year end.

JPMAM carries out some of its dealing transactions through other group subsidiaries. These transactions are carried out at arm's length. The commission paid in the year was £34,000 (2005: £2,000). The Company has been informed that certain of its dealing transactions may be subject to soft commission arrangements.

The Company holds an investment in one fund (2005: one) managed by JPMAM. At 31st March 2006, JPM Europe Micro Cap Fund was valued at £44m (2005: Fleming Frontier European Discovery Fund £33m) and represented 11.5% of the Company's investment portfolio (2005: 14.6%). During the year the Company made sales of £4m from the holding in Fleming Frontier European Discovery Fund and the remainder of the holdings were converted into JPM Europe Micro Cap Fund. Investment income of £108,000 was received from Fleming Frontier European Discovery Fund (2005: £Nil).

The Company has received £63,000 (2005: £52,000) as a result of stocklending transactions during the year. JPMAM commissions in respect of such transactions amounted to £16,000 (2005: £13,000).

At the year end, a bank balance of £879,000 (2005: £66,000) was held with JPMorgan Chase. During the year ended 31st March 2006 the Company received a net amount of interest of £23,000 (2005: £27,000) from JPMorgan Chase.

#### 15. Financial instruments

The Company's financial instruments may comprise:

- Investments in equity shares of European companies, and shares of other European funds. These are held in accordance with the Company's investment objective and policies;
- Bank loans denominated in Euros of which the main purpose is to raise finance for the Company's operations;
- Short-term debtors, creditors and cash amounts arising directly from its operations.

As an investment trust the Company invests in securities for the long-term.

The main risk arising from the Company's financial instruments is market price risk which incorporates both foreign currency and interest rate risk. The Board's policy for managing each of these risks is summarised below. These policies have remained unchanged throughout the current and preceding years.

##### **Market price risk**

Market price risk arises mainly from uncertainty about future prices of financial instruments held. It represents the potential loss the Company might suffer through holding market positions in the face of adverse price movements.

Individual fund managers have responsibility for monitoring the existing portfolio selected in accordance with the overall asset allocation parameters set by the Board and seek to ensure that individual stocks also meet a risk reward profile that is acceptable.

The Board meets on at least five occasions during the year to consider the structure of the portfolio and, as part of its reviews, considers the risk associated with particular countries or industry sectors.

##### **Interest rate risk**

The Company finances part of its investment activities through Euro denominated short term loans at floating rates of interest. Therefore the Company's exposure to risk due to fluctuating market rates of interest is not significant.

##### **Foreign currency risk**

The income and capital value of the Company's investments can be significantly affected by exchange rate movements as the majority of the Company's assets and income are denominated in currencies other than sterling which is the Company's reporting currency.

The Board has identified three principal areas where foreign currency risk could impact the Company:

- Movements in rates affecting the value of investments;
- Movements in rates affecting short-term timing differences; and
- Movements in rates affecting the income received.

The Company does not currently hedge the sterling value of investments that are priced in other currencies, although, as set out above, it will finance part of its investment activities with foreign currency borrowings thereby hedging part of the movements in the value of investments attributable to exchange rate fluctuations.

The Company may be exposed to exchange rate movement where there is a difference between the date an investment is bought or sold and the date when settlement of the transaction occurs. This exposure is short term and therefore the risk is not significant.

## 15. Financial instruments continued

### Liquidity risk

The Company's assets comprise mainly realisable securities, which can be sold to meet funding requirements if necessary. Short-term flexibility is achieved through the use of a short term loan facility.

### Currency exposures

The following is an analysis of the Company's net assets by currency other than sterling as at 31st March:

	<b>Euro</b>	Euro	<b>Skr</b>	Skr	<b>SFr</b>	SFr	<b>Other</b>	Other	<b>Total</b>	Total
	<b>£m</b>	£m	<b>£m</b>	£m	<b>£m</b>	£m	<b>£m</b>	£m	<b>£m</b>	£m
	<b>2006</b>	2005	<b>2006</b>	2005	<b>2006</b>	2005	<b>2006</b>	2005	<b>2006</b>	2005
Investments	<b>227.7</b>	157.3	<b>60.3</b>	7.3	<b>44.0</b>	10.7	<b>55.2</b>	61.7	<b>387.2</b>	237.0
Net current (liabilities)/assets	<b>(1.7)</b>	29.6	<b>(0.3)</b>	–	<b>(1.9)</b>	0.1	<b>(0.5)</b>	(1.9)	<b>(4.4)</b>	27.8
Loans	<b>(10.5)</b>	(34.4)	–	–	–	–	–	–	<b>(10.5)</b>	(34.4)
Total currency exposure	<b>215.5</b>	152.5	<b>60.0</b>	7.3	<b>42.1</b>	10.8	<b>54.7</b>	59.8	<b>372.3</b>	230.4

### Interest rate risk profile of financial assets and financial liabilities

#### Assets

All of the Company's financial assets are equity shares or other investments which neither pay interest nor have a maturity date. The portfolio did not contain fixed interest securities at 31st March 2006 (2005: nil).

#### Liabilities

The interest rate profile of the Company's financial liabilities at 31st March is:

	<b>Euro</b>	Euro
	<b>£m</b>	£m
	<b>2006</b>	2005
Floating rate liabilities	<b>10.5</b>	34.4

The Company arranged a Euro 70 million loan facility on 16th November 2005 with ING Bank. Interest is chargeable at LIBOR plus a margin and the facility expires on 15th November 2006. As at 31st March 2006 the Company had drawn down 15 million Euros on this facility at an interest rate of 3.03%.

As at 31st March 2005 the Company had a Euro 50 million loan facility with ING Bank at an interest rate of LIBOR plus a margin. This facility expired on 17th November 2005. At 31st March 2005, the whole Euro 50 million had been drawn down on this facility at an interest rate of 2.48%.

### Fair value of financial instruments

All financial assets and liabilities are included in the Balance Sheet at fair values.

## 16. Capital commitments

At the balance sheet date there were no capital commitments (2005: £nil).

# Information about the Company

## FINANCIAL CALENDAR

<b>Financial year end</b>	31st March
<b>Interim results announced</b>	October
<b>Final results announced</b>	June
<b>Annual General Meeting</b>	July

### History

On 24th April 1990, the Company acquired the undertaking and assets of Fleming European Fledgeling Fund Limited (the 'Fund') in exchange for the issue of its shares and warrants. The Fund was an open-ended, unquoted investment company based in Jersey and formed in June 1987 with the same objectives and investment policies as the Company. The Company adopted its present name in July 2002.

### Company Numbers

Company registration number: 2431143  
London Stock Exchange code: 0341969

### Market Information

The Company's net asset value ('NAV') is published daily, via the London Stock Exchange. The Company's shares are listed on the London Stock Exchange. The market price is shown daily in the Financial Times, The Guardian, The Times, The Daily Telegraph, The Independent, The Herald, The Scotsman, BBC Ceefax and on the JPMorgan Internet site at [www.jpmeuropeanfledgeling.com](http://www.jpmeuropeanfledgeling.com), where the share price is updated every fifteen minutes during trading hours.

### Share Transactions

The Company's shares may be dealt in directly through a stockbroker or through a professional adviser acting on an investor's behalf. They may also be purchased and held through the JPMorgan Investment Trust Share Plan, Individual Savings Account (ISA), Personal Equity Plan (PEP) and the Pension Account.

### Manager and Secretary

JPMorgan Asset Management (UK) Limited

### Company's Registered Office

Finsbury Dials, 20 Finsbury Street,  
London EC2Y 9AQ  
Telephone number: 020 7742 6000

*Please contact Hilary Lowe for company secretarial and administrative matters at the above address or telephone 020 7742 6000.*

### Registrars

**Lloyds TSB Registrars**, Reference 1083,  
The Causeway, Worthing, West Sussex BN99 6DA  
Telephone number: 0870 600 3984

*Notifications of changes of address and enquiries regarding share certificates or dividend cheques should be made in writing to the Registrar quoting reference 1083.*

*Registered shareholders can obtain further details on their holdings on the internet by visiting [www.shareview.co.uk](http://www.shareview.co.uk)*

### Savings Plan Administrators

For queries on the JPMorgan ISA, PEP, Share Plan or Pension Account, see contact details on back cover.

### Independent Auditors

**PricewaterhouseCoopers LLP**, Southwark Towers,  
32 London Bridge Street, London SE1 9SY

### Broker

**UBS**, 1 Finsbury Avenue, London EC2M 2PP



The Company is a member of The Association of Investment Trust Companies.

## **JPMorgan Helpline**

**Freephone 0800 40 30 30** OR 020 7742 9999

**8.30 am to 6.00 pm Monday to Friday**

## **JPMorgan Pension Helpline**

**Freephone 0800 413 176** OR 01722 414 888

**9.00 am to 5.00 pm Monday to Friday**

Please use this service if you have any queries relating to the Pension Account.

Your telephone call may be recorded for your security.

**[www.jpmfeuropeanfledgeling.com](http://www.jpmfeuropeanfledgeling.com)**