Report and Accounts for the year ended 31st January 2001

Dresdner RCM Global Investors | Investment Trusts

The Merchants Trust PLC

www.merchantstrust.co.uk

its investment trusts
the easy way to invest in the stock market

Dresdner RCM Global Investors

Contents

Investment Objective

To provide an above average level of income and income growth together with long term growth of capital through a policy of investing mainly in higher yielding UK FTSE 100 companies.

Benchmark

The Trust's investment performance is assessed by comparison with other investment trusts within the UK Growth and Income sector. In addition it is benchmarked against the FTSE 100 Index, reflecting the emphasis within the portfolio, as well as the FTSE 350 Higher Yield Index, reflecting the Trust's high yield objective.

Financial Highlights

For the years ended 31st January

Revenue	**2001**	**2000**	**% change**
Revenue	£21,546,258	£22,590,052	–4.6
Available for Ordinary Dividend	£16,714,573	£18,344,607	–8.9
Earnings per Ordinary Share	16.35p	17.93p	–8.8
Dividend per Ordinary Share	16.40p	16.00p	+2.5
Key Data as at 31st January			
Total Net Assets	£474,906,733	£391,495,283	+21.3
Net Asset Value per Ordinary Share	463.5p	381.4p	+21.5
Ordinary Share Price	411.25p	337.0p	+22.0
Discount of net asset value to Ordinary Share Price	11.3%	11.6%	—

Investor Information

Results

Half-year announced mid-September.
Full-year announced mid-March.
Report and Accounts posted to Shareholders mid-April.
Annual General Meeting held mid-May.

Ordinary Dividends

First quarterly paid late August.
Second quarterly paid late November.
Third quarterly paid late February.
Final paid late May.

Preference Dividends

Payable half-yearly 1st August and 1st February.

Interest on 4% Perpetual Debenture Stock

Payable half-yearly 1st May and 1st November.

Dividend Payment Schedule

Year to:		**Dividend**	**Payment Date**
January 1997	First Interim	3.25p	23.08.96
	Second Interim	3.25p	18.11.96
	Third Interim	3.25p	21.02.97
	Final	3.90pø	23.05.97
January 1998	First Interim	2.35p	09.06.97
	Second Interim	4.65p	18.11.97
	Third Interim	3.50p	26.02.98
	Final	3.75p	20.05.98
January 1999	First Interim	3.75p	21.08.98
	Second Interim	3.75p	18.11.98
	Third Interim	4.34p‡	22.02.99
	Final	3.75p	19.05.99
January 2000	First Interim	3.95p	24.08.99
	Second Interim	3.95p	10.11.99
	Third Interim	4.05p	22.02.00
	Final	4.05p	18.05.00
January 2001	First Interim	4.10p	24.08.00
	Second Interim	4.10p	10.11.00
	Third Interim	4.10p	16.02.01
	Final (proposed)	4.10p	17.05.01

ø‡ See page 8 "Historical Record" for details of FID enhancements paid.

Investor Information

Market and Portfolio Information

The Company's Ordinary Shares are listed on the London Stock Exchange. The market price, price range, gross yield and net asset value are shown daily in the Financial Times and The Daily Telegraph. The net asset value of the Ordinary Shares is calculated weekly and published on the London Stock Exchange Primark Service. The geographical spread of investments and ten largest holdings are published monthly on the London Stock Exchange Primark Service. They are also available to any enquirer from the Investment Trust Helpline or the Dresdner RCM website: www.dresdnerrcm-its.co.uk.

Share Prices

The share prices quoted in London Stock Exchange Daily Official List for 31st January 2001 were 406¼p-416¼p.

For CGT indexation purposes at 31st March 1982 the share price, after adjustment for bonus issues, was 48.75p.

Savings Plan

The Dresdner RCM Global Investors Investment Trusts Savings Plan provides a convenient and economical way for shareholders to increase their existing holdings. Investments can be in the form of a regular payment or an individual lump sum and there is an arrangement for the reinvestment of dividends. There are also facilities for selling and switching.

Investment Trust Maxi ISA

Shareholders can invest in the shares of the Trust through the Dresdner RCM Investment Trust ISA. Full details are available from the Investment Trust Helpline on 020 7475 5832.

Website

Further information about the Trust is available on the Dresdner RCM website www.merchantstrust.co.uk.

Dresdner RCM Global Investors

Dresdner RCM Global Investors is the global asset management arm of the Dresdner Bank Group, providing management and advisory services with respect to over £57.7 billion of assets. It manages ten listed investment trusts, including the Merchants Trust PLC, with aggregated total assets of some £1.95 billion as at 31st January 2001.

Dresdner RCM Global Investors gives enhanced access to a full range of global, regional and country investment capabilities and asset allocation expertise, assisted by their Grassroots market research network throughout Europe and the rest of the world. It is backed by the financial strength and stability of the Dresdner Bank Group – one of the world's largest financial institutions with a presence in 70 countries around the globe.

According to a survey published by Merrill Lynch in April 2000 your Trust's total expenses of 0.58% as a proportion of total assets compared with a UK Growth and Income peer group average of 0.85%.

Payment of Dividends Direct to Bank Accounts

Cash dividends will be sent by cheque to first-named shareholders at their registered address together with a tax voucher. Dividends may be paid directly into Shareholders' bank accounts. Details of how this may be arranged can be obtained from Capita IRG. Dividends mandated in this way are paid via BACS (Bankers' Automated Clearing Services). Tax vouchers will then be sent directly to Shareholders at their registered address unless other instructions have been given.

Association of Investment Trust Companies (AITC)

The Company is a member of the AITC, which provides a range of literature including fact sheets and a monthly statistical service. Copies of these publications can be obtained from the AITC, Durrant House, 8-13 Chiswell Street, London EC1Y 4YY.

Category: UK Growth and Income

'its' Campaign

The Company is a supporter of the Association of Investment Trust Companies' **'its'** campaign.

Contact Details

Shareholder Enquiries

Capita IRG plc are the Company's registrars and maintain the share register. In the event of queries regarding their holdings of shares, lost certificates, dividend cheques, registered details, etc., shareholders should contact them on 020 8639 2000. Changes of name and address must be notified to the registrars in writing.

Any general enquiries about the Company should be directed to the Company Secretary, The Merchants Trust PLC, 10 Fenchurch Street, London EC3M 3LB.

Managers and Advisers

Fund Manager
Nigel Lanning AUKSIP ACIS
Director European Equities, Dresdner RCM Global Investors (UK) Ltd.

Secretary and Registered Office
Nicola Schrager von Altishofen ACIS
10 Fenchurch Street, London EC3M 3LB
Telephone: 020 7475 2700

Deputy Secretary
Kirsten Salt BA (Hons) ACIS

Registered Number 28276

Registrars and Transfer Office
Capita IRG plc
Bourne House, 34 Beckenham Road,
Beckenham, Kent BR3 4TU
Telephone: 020 8639 2000

Auditors
PricewaterhouseCoopers, Chartered Accountants
Southwark Towers
32 London Bridge Street, London SE1 9SY

Bankers
Barclays Bank PLC
Lloyds TSB Bank plc
Kleinwort Benson Private Bank Limited

Stockbroker
Cazenove & Co.

The Merchants Trust PLC website
www.merchantstrust.co.uk

Dresdner RCM Investment Trust Helpline
020 7475 5832

Dresdner RCM website
www.dresdnerrcm-its.co.uk

Chairman's Statement

In this my first report to shareholders as Chairman of the Trust, I should start by paying tribute to my predecessor, Colin Black, who retired in May of last year. Colin was Chairman for seven of his eight years as a Director. In his time on the Board total net assets increased from £220m to nearly £400m and earnings per share grew from 10.9p to 17.9p. His wise advice and deep knowledge of investment trusts will be missed by the Board and the Managers. We wish him a long and happy retirement.

Results

Shareholders will recall that the year ended 31st January 2000 was characterised by the rapid appreciation of the technology, media and telecoms sectors at the expense of the more established companies in which your Trust typically invests. These trends were reversed in the year under review. Investors have given much greater attention to basic investment issues, such as cashflow, dividends and stability of earnings – factors which have always been the cornerstone of the Merchants portfolio, given the Trust's long term dividend growth objective.

The year ended 31st January 2001 produced a total return to shareholders of 25.8%. At the year end the net asset value per share stood at 463.5p, representing an increase of 21.5% over the 381.4p recorded a year previously. This compares with capital growth of 0.5% recorded by the FTSE 100 Index and 24.6% recorded by the FTSE 350 Higher Yield Index. (The latter index should, however, be treated with caution, since it does not include any telecoms stocks and is thus not representative of the market as a whole). The Trust's capital returns for the year are some 6% above the average for the UK Growth and Income sub-sector as calculated by Datastream. The Trust's net dividend yield of 4.4% at 374p, is approximately 0.7% above the sub-sector average.

Net revenue earnings per ordinary share were 16.35p. Taking account of revenue special dividend receipts of 1.21p, the underlying earnings per share were 15.14p. These figures compare with 17.93p per share recorded in 1999/2000, or 16.62p per share after adjusting for revenue special dividend receipts in that year. In the last annual report, we stated that whilst the Trust would adhere rigorously to its income growth objectives, its investment policy would accommodate a broader spread of companies than previously. This new strategy is reflected in the 8.8% fall in underlying earnings in the latest year.

Dividends

The Board is recommending a final dividend of 4.1p per share, giving a total of 16.4p for the full year. On this basis dividends will have increased by 2.5% in 2000/01 without any material recourse to the Trust's Revenue Reserves which now stand at £10.2m. The underlying rate of inflation in the UK during the year was 1.8%, so that the recommended dividend sustains the Trust's record of real dividend growth.

Issue of Secured Bonds

The decision to increase the Trust's borrowings in December 1999 proved to be timely in two respects. The £30 million raised in this way entailed an interest cost of 6.1% per annum over the bonds' 30 year life. This capital raising preceded a sharp rise in corporate borrowing spreads, which increased significantly the cost of debt finance to all non-government borrowers. Moreover the investment of these funds last Spring in a number of undervalued high yielding equities has already enhanced returns to shareholders in a meaningful way.

Repurchase of Shares

As at the date of this report the Company has repurchased and cancelled a total of 175,000 shares pursuant to the authorisation granted by shareholders at last year's Annual General Meeting. The Board is proposing that this authority be renewed at the Annual General Meeting.

Prospects

For a number of reasons, the US economy stalled in the closing months of last year and this has been reflected in weaker stockmarkets throughout the world, including the UK. For the first time in nearly a decade, a number of forecasters are questioning the sustainability of economic growth in the US. It is unclear at present whether this represents a serious impediment to growth world-wide or whether the prompt action taken to cut interest rates, both in the US and the UK, will have been sufficient to offset these negative trends.

In the past when investors have had to contend with the conflicting influences of slower earnings growth and falling interest rates, it is the latter that have held sway. With interest rates forecast to be cut further over the course of 2001, there is every hope that established UK company shares should prove to be relatively attractive investments, not least because the UK market appears to be good value by global standards. The Trust is well placed to take advantage of this.

Dividend Forecast

In arriving at a dividend forecast the Board has taken due account of all these issues, as well as the strength of the Trust's Revenue Reserves. The Directors forecast that, in the absence of unforeseen circumstances, dividend payments for 2001/2 will total at least 16.8p per share, an increase of just under 2.5%.

Hugh Stevenson
Chairman
5th April 2001

Historical Record

Years ended 31st January

Revenue and Capital	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Revenue (£000's)	13,823◊	14,456◊	13,563†*◊	15,514◊	17,466◊	17,351◊	18,769◊	20,399◊	20,119◊	22,590	21,546
Earnings per share (net)	10.46p†	10.92p†	10.20p†*	11.04p	12.12p	12.41p	13.66p	14.88p	15.21p	17.93p	16.35p
Paid net per Share	9.00p	10.00p	10.60p	11.00p	11.50p	12.25p	13.65pø	14.25p	15.59p‡	16.00p	16.40p
Tax Credit per Share	3.00p	3.30p	3.31p	2.75p	2.88p	3.06p	3.41p#	3.56p	3.90p§	1.78p	1.82p
Gross Ordinary Dividend	12.00p	13.30p	13.91p	13.75p	14.38p	15.31p	17.06p	17.81p	19.49p	17.78p	18.22p
Total Net Assets (£000's)	197,514†	220,007†	242,331†*	311,127	253,604	303,934◊	335,212	421,504	426,037	391,495	474,907
Net Assets attributable to Ordinary Capital (£000's)	196,336†	218,829†	241,153†*	309,949	252,426	302,756◊	334,034	420,326	424,859	390,317	473,729
Net Asset Value per Ordinary Share	191.9p†	213.9p†	235.7p†*	302.9p	246.7p	295.9◊	326.4p	410.8p	415.2p	381.4p	463.5p
NAV Total Return (%)×	–10.7	+16.7	+15.1	+33.2	–14.8	+24.9	+14.9	+30.2	+4.9	–4.3	+25.8
Retail Price Index Increase (%)δ	+8.5	+5.6	+3.2	+2.8	+2.8	+2.8	+3.1	+2.5	+2.6	+2.1	+1.8

Notes

◊ Restated in accordance with Financial Reporting Standard 16 "Current Taxation".

† Restated to reflect the change in accounting policy during the year ended 31st January 1994 for finance costs of long-term borrowings.

* Restated to reflect the change in accounting policy during the year ended 31st January 1994 for dividends and interest receivable on investments.

× NAV total return reflects both the change in net asset value per ordinary share and the net ordinary dividends declared in respect of each year.

ø The total distribution for 1997 was 13.65p. This was made up of interim dividends of 9.75p, a final foreign income dividend (FID) of 2.00p and a final ordinary dividend of 1.90p. The final ordinary dividend was enhanced by 0.40p to ensure no shareholder would be adversely affected by the FID. Excluding this enhancement the "normal" distribution for 1997 was therefore 13.25p.

Inclusive of 0.50p tax credit on the FID which is notional and not repayable.

‡ The total distribution for 1999 was 15.59p. This was made up of interim ordinary dividends of 8.86p, an interim foreign income dividend (FID) of 2.98p and a final ordinary dividend of 3.75p. The FID was enhanced by 0.59p to ensure that no shareholder would be adversely affected by receiving this form of dividend. Excluding this enhancement the "normal' distribution for 1999 was therefore 15.00p.

§ Inclusive of 0.74p tax credit on the FID which is notional and not repayable.

δ RPIX – excludes the effect of mortgage rates.

Geographical Distribution

Percentage of Portfolio Investments

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
United Kingdom	95.7	98.8	99.1	99.5	99.5	99.6	99.6	99.8	99.8	99.9	100.0
North America	4.3	1.2	0.9	0.5	0.5	0.4	0.4	0.2	0.2	0.1	—
	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Thirty Largest Holdings

at 31st January 2001

	Valuation £'000s	%	Unrealised Gain (Loss) over Book Cost £'000s
BP Amoco	38,547	6.55	6,447
British Telecommunications	29,192	4.97	5,742
Shell	26,790	4.56	8,827
GlaxoSmithkline	23,261	3.96	5,489
Vodafone	18,634	3.17	(4,847)
Royal Bank of Scotland	16,270	2.77	9,177
*Standard Chartered	14,878	2.53	3,078
Lloyds TSB	13,300	2.27	378
Bank of Scotland	12,495	2.13	2,723
Imperial Tobacco	11,050	1.88	1,112
Royal & Sun Alliance	11,046	1.88	(622)
Wimpey	11,025	1.88	1,783
CGNU	10,571	1.81	3,229
Scottish & Southern Energy	10,566	1.81	(732)
Barclays	10,379	1.78	5,816
Halifax	10,265	1.76	(1,887)
Alliance & Leicester	9,796	1.67	2,351
Wolseley	9,555	1.63	2,263
Boots	8,456	1.44	(604)
Legal & General	8,388	1.43	375
Scottish & Newcastle	8,010	1.36	(4,479)
BOC	8,000	1.36	(37)
Marconi	7,946	1.35	(788)
Sainsbury (J)	7,942	1.35	280
Abbey National	7,731	1.32	897
Anglo American	7,475	1.27	1,343
Associated British Ports	7,380	1.26	1,428
United Utilities	7,296	1.24	(2,036)
Allied Domecq	7,020	1.20	2,916
Great Universal Stores	6,885	1.17	134
	£380,149	64.76	

*Includes £2,724,425 of Convertible Bonds

Investment Managers' Review

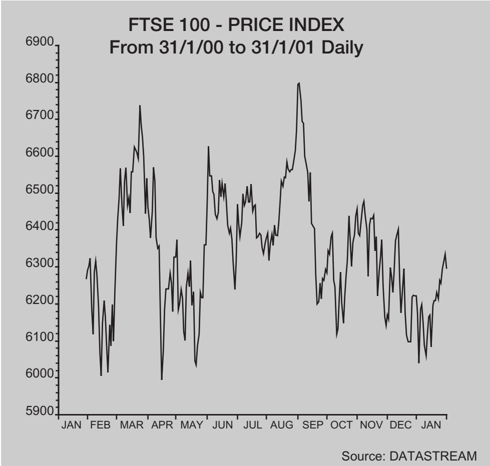
Economic Background

The year 2000 proved to be another year of progress for the UK economy with provisional figures showing growth of nearly 3%. This continued the sequence of unbroken expansion dating back to 1992. Perhaps even more remarkably inflation has remained well under control, especially in the light of the rapid increase in crude oil prices during the last year. In fact inflation has now stayed below the Monetary Policy Committee's 2.5% target for nearly two years. Thus, although base rates rose to 6% in February 2000, the MPC did not consider it necessary to raise them above that level. Furthermore, they were reduced to 5.75% in February of this year.

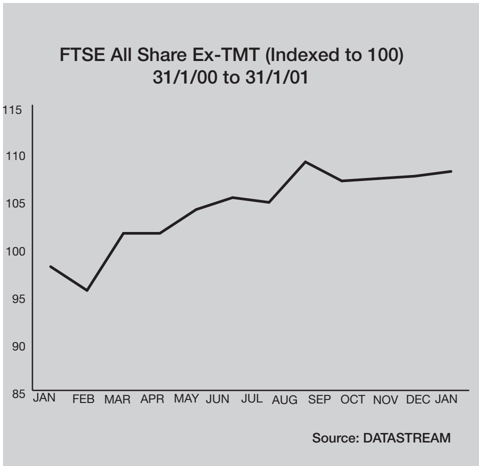
The reduction in interest rates in the UK followed a marked easing in US monetary policy involving two cuts of 0.5% in the Fed Funds rate in the early weeks of 2001. It appears that US growth slowed considerably in the closing months of 2000, giving rise to fears of recessionary conditions in the US and elsewhere in 2001. To date the evidence from UK Government statistics and from UK company news is that the slowdown is chiefly affecting the technology sector. Whilst there are signs of a slowdown elsewhere, progress is still being recorded as far as the main economic variables are concerned. In this light it seems feasible that economic growth in the UK will continue in 2001, albeit at a slower rate than that seen recently. This should help to sustain the level of corporate profits and dividends during 2001.

Market Trends

The UK equity market, as a whole, struggled to make meaningful progress over the course of 2000/01. Over the last financial year a trading range varying from 6000 to 6800 proved to be reasonably robust for the FTSE 100 Index. If one ignores the impact of the Technology, Media and Telecoms sectors (TMT), one can see from the second graph on this page that a different picture emerges. Further, the FTSE 350 Higher Yield Index recorded consistent progress throughout the year under review.



In terms of sector contribution to returns, it is notable that there has been an almost complete reversal of the trends seen in 1999/2000, as the Chairman has said. Specifically, the leading sectors were Tobacco (+83.4%), Insurance (+53.9%) and Banks (+49.9%). The characteristics of financial strength evidenced in these sectors show a marked contrast to those exhibited by the weakest performers over the latest year. The latter included IT Software (-41.8%), Telecoms (-33.4%) and IT Hardware



(-30.3%). All of the leading sectors are renowned for their dividend paying credentials and, as a consequence, have made major contributions to the Trust's performance in the last twelve months. Although there have been significant weaknesses in all security values since the year end, these broad sector trends have nevertheless been sustained in relative terms.

Portfolio Changes

Shareholders will recall that at the 1999/2000 year end the Trust held nearly £27m, or some 5% of total assets, in short dated gilt-edged securities. These investments represented a temporary home for the funds raised through the December 1999 bond issue. In early March of last year, two-thirds of these holdings were sold to facilitate purchases of a number of high yielding UK equities which had suffered a sharp fall in their ratings. In particular, these purchases included Associated British Foods, Anglo American, BP Amoco, Burmah, Imperial Tobacco, Royal Bank of Scotland and Scottish & Newcastle. The remaining gilt-edged holdings were subsequently sold in June.

Looking at other purchases made during the last year, they can broadly be divided into two categories. Firstly there were several shares which were forecast to produce a stable and growing income, including BAA, British Land and Shell. Secondly, there were some more cyclical companies where the prospective fall in interest rates was expected to have a positive impact on valuations. These included Alliance & Leicester, Bank of Scotland and Wolseley. In addition to these, the Trust purchased a holding in Man Group, the specialist fund management group. Amongst the "new" economy sectors, the Trust exploited profitable opportunities in Alliance Unichem, Dimension Data, Energis and Misys.

With growing uncertainties regarding the economic outlook, there were a number of sales of shares where it was considered profit forecasts had run ahead of reasonable expectations. These sales included BAE Systems (formerly British Aerospace) and Reuters. Further, towards the end of the financial year, profits were also taken in companies such as Johnson Matthey, Prudential and Smith and Nephew, where the share ratings appeared to be up with events. Additionally, the last year was a good one for take-overs amongst the Trust's holdings. As a result there were disposals of Burmah, NatWest Bank, Tarmac, Thames Water and United Assurance as well as the bids for Beazer and Abbey National, which were current at the year end.

Lastly, it is pleasing to report the sale of one of the remaining unquoted investments, O'Connor, which largely completes our long term objective to invest only in listed stocks in this category. The remaining unquoted investment, valued at £51,458, is not sufficiently material to warrant a separate listing in the latest accounts.

Future Policy

At present, the economic uncertainties for 2001 are overlaid by the probability of a general election in the UK. Whilst this climate demands great vigilance from a fund management viewpoint, the UK equity market still exhibits many attractive qualities. In general, companies are well run by historic standards and there is widespread acceptance of the need to target shareholders' best long term interests. Whilst the fall in new economy shares means that value is now to be found in some of these growth areas, in general best advantage seems most in evidence amongst the established blue chip companies in which the Trust typically invests. With interest rates appearing to be on a downward path, the managers will continue to seek good investment opportunities in the months ahead.

United Kingdom Listed Holdings

at 31st January 2001

	Value (£)	Principal Activities
BP Amoco	38,546,750	Oil exploration and production
British Telecommunications	29,192,000	Telecommunications
Shell	26,790,000	Oil and gas
GlaxoSmithkline	23,261,046	Pharmaceuticals
Vodafone	18,634,000	Telecommunications
Royal Bank of Scotland	16,270,000	Banking
*Standard Chartered	14,877,925	Banking
Lloyds TSB	13,300,000	Banking
Bank of Scotland	12,495,000	Banking
Imperial Tobacco	11,050,000	Tobacco
Royal & Sun Alliance	11,046,000	Insurance
Wimpey	11,025,000	Housebuilding
CGNU	10,571,100	Life & general insurance
Scottish & Southern Energy	10,566,000	Electricity
Barclays	10,378,750	Banking
Halifax	10,264,800	Banking
Alliance & Leicester	9,795,500	Banking
Wolseley	9,555,000	Building materials distribution
Boots	8,456,000	Retailing
Legal & General	8,387,500	Life & general insurance
Scottish & Newcastle	8,010,000	Brewing and leisure
BOC	8,000,000	Industrial gases
Marconi	7,946,422	Telecom equipment
Sainsbury (J)	7,942,000	Food retailing
Abbey National	7,731,340	Banking
Anglo American	7,475,400	Mining
Associated British Ports	7,380,000	Transportation & storage
United Utilities	7,296,000	Water
Allied Domecq	7,019,883	Spirits and food
Great Universal Stores	6,885,000	Retailing
Land Securities	6,870,000	Property
Hilton Group	6,797,250	Betting & hotels
FKI	6,697,500	Electrical equipment
Gallaher	6,587,500	Tobacco
Rio Tinto	6,556,000	Mining
Billiton	6,532,000	Mining
Dixons	6,456,000	Retailing
ICI	6,350,000	Chemicals
Beazer	6,318,866	Housebuilding
Wilson Connolly	6,247,500	Housebuilding
Bradford & Bingley	6,229,600	Banking
Morgan Crucible	5,980,000	Engineering
British Sky Broadcasting	5,900,000	Media
BAA	5,880,000	Airports and retailing
BBA	5,839,500	Engineering

United Kingdom Listed Holdings

at 31st January 2001

	Value (£)	Principal Activities
△BAE Systems	5,827,500	Aerospace & defence
United Business Media	5,824,000	Media
Kingfisher	5,755,750	Retailer
Cable & Wireless	5,583,860	Telecommunications
Prudential Corporation	5,515,850	Life and general insurance
Scottish Power UK	5,500,250	Electricity
Amvescap	5,446,800	Fund management
Great Portland Estates	5,310,300	Property
EMI	5,244,750	Media
Aggregate Industries	5,094,375	Building materials
Tate & Lyle	4,992,000	Sugar
Granada	4,844,000	TV and media
Lattice	4,593,750	Gas distribution
Reuters	4,420,000	Media
Associated British Foods	4,410,000	Food manufacturing
†Airtours	3,932,262	Travel
Man	3,905,000	Fund management
Tomkins	3,784,000	Holding company
P & O Princess Cruises	3,475,000	Leisure
British Airways	3,472,500	Airline
Corus	3,064,750	Steel
Johnson Matthey	3,013,637	Chemicals and metals
P&O	2,987,500	Ports and logistics
Safeway	2,965,000	Food retailing
Severn Trent	2,545,452	Water
WPP	2,205,000	Advertising
RMC	1,175,636	Building materials
Carlton Communications	880,169	TV and media
	£591,159,223	

†Consists of Convertible Bonds
*Includes £2,724,425 of Convertible Bonds
△Consists of Convertible Preference shares

Performance Attribution Analysis

For the year ended 31st January 2001

	%	%
Capital return on FTSE 100 Index		0.5
Relative return from Portfolio	17.4	
Less: Expenses charged to capital	(1.4)	
Net relative return from portfolio		16.0
Change in total assets		16.5
Impact of gearing		4.8
Increase due to repurchase of shares		0.2
Increase in Net Asset Value per Ordinary Share		21.5

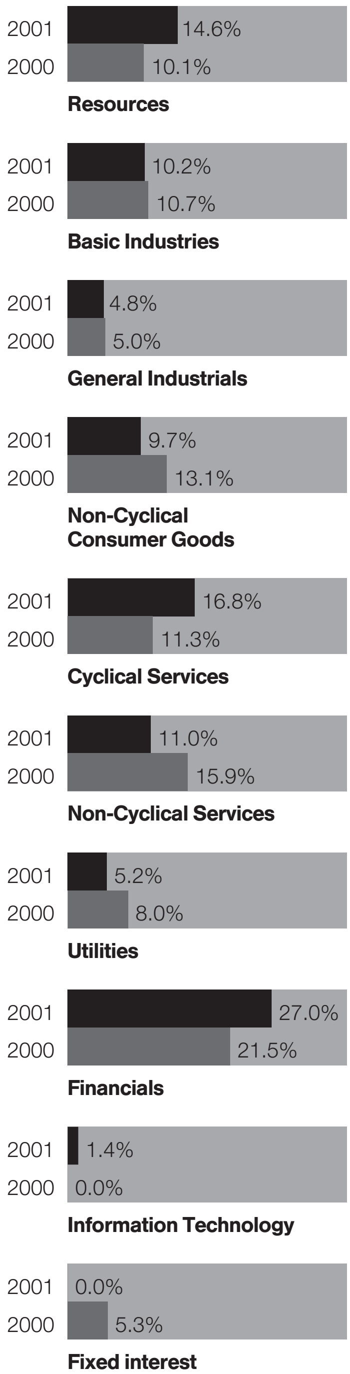
Computed relative to FTSE 100

Distribution of Total Assets

at 31st January 2001

Total Assets (less creditors falling due within one year) £586,989,188 (2000: £503,729,701)

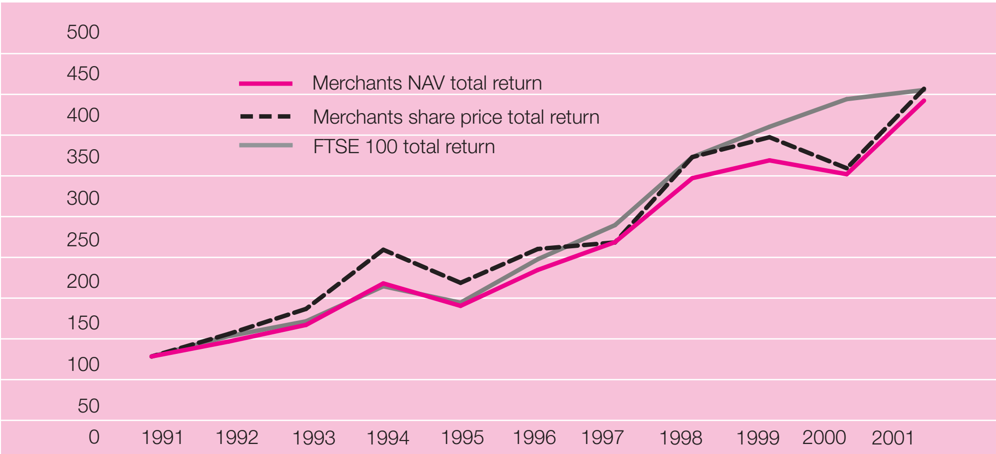
	Percentage of Total Assets 2001	2000
Equities (including convertibles)		
Resources		
Mining	3.5	1.2
Oil and gas	11.1	8.9
	14.6	10.1
Basic Industries		
Chemicals	3.0	3.9
Construction & building materials	6.7	5.8
Steel & other metals	0.5	1.0
	10.2	10.7
General Industrials		
Aerospace & defence	1.0	1.7
Engineering & machinery	3.8	3.3
	4.8	5.0
Non-Cyclical Consumer Goods		
Beverages	1.2	1.9
Food products & process	1.5	2.1
Health	—	1.2
Pharmaceuticals	4.0	4.7
Tobacco	3.0	3.2
	9.7	13.1
Cyclical Services		
General retailers	4.6	2.1
Leisure, entertainment & hotels	4.0	1.8
Media & photography	4.2	4.5
Restaurants, pubs & breweries	—	2.0
Transport	4.0	0.9
	16.8	11.3
Non-Cyclical Services		
Food & drug retail	1.9	2.9
Telecommunication services	9.1	13.0
	11.0	15.9
Utilities		
Electricity	2.7	4.3
Gas distribution	0.8	1.7
Water	1.7	2.0
	5.2	8.0
Financials		
Banks	17.2	12.1
Insurance	1.9	1.9
Life assurance	4.2	3.5
Real estate	2.1	2.8
Speciality & other financials	1.6	1.2
	27.0	21.5
Information Technology		
Information technology hardware	1.4	0.0
	1.4	0.0
Total Equities	100.7	95.6
Fixed Interest		
Government Securities	0.0	5.3
Total Fixed Interest	0.0	5.3
Net Current Liabilities	(0.7)	(0.9)
Total Assets	100.0	100.0



Performance Graphs

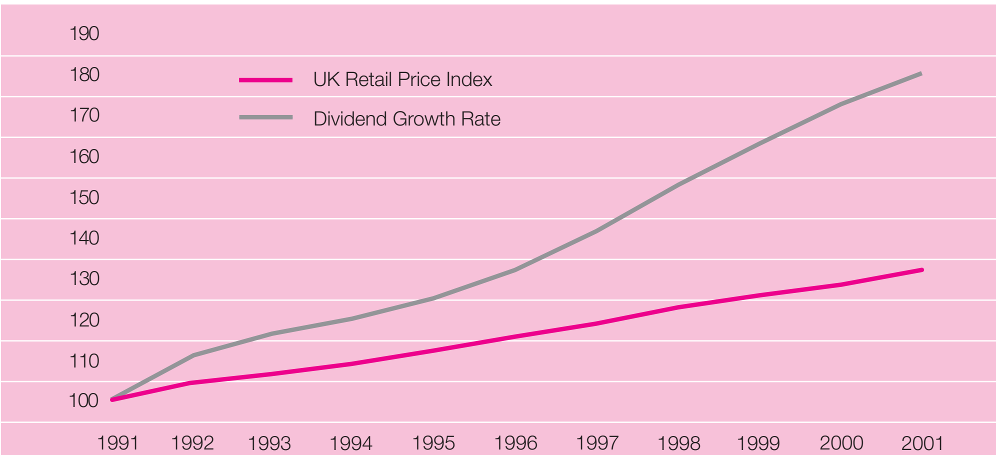
10 year record—as at 31st January

Merchants Total Return compared to FTSE 100 Total Return



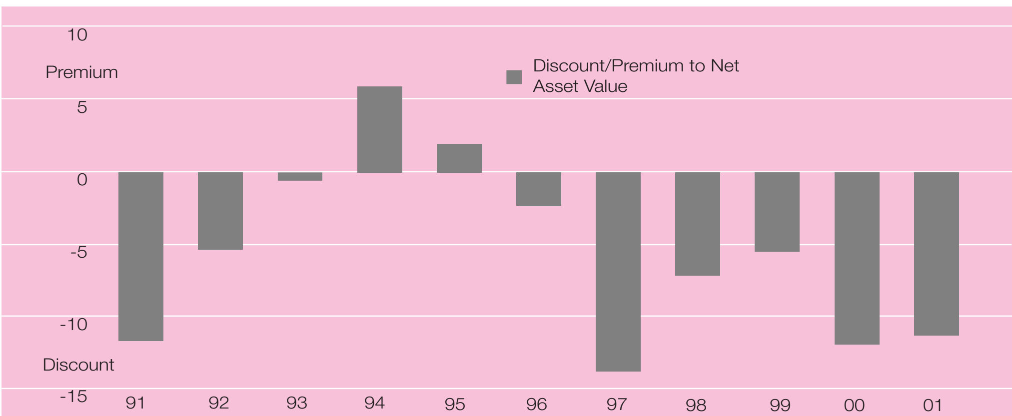
(Rebased to 100, net income reinvested) Source: Datastream

Merchants Net Dividend Growth compared to Inflation



***excluding FID enhancements (see page 9 for details)**
(Rebased to 100) Source: Dresdner RCM/Datastream

Merchants Share Price Discount/Premium to Net Asset Value



Risk Review

Financial Reporting Standard 13—Derivatives and Other Financial Instruments: Disclosure

FRS 13 requires entities to disclose narrative and numerical information about the financial instruments that they use.

The purpose of these disclosures is to ensure that enough information is provided to investors to enable them to make their own decisions about the risk profile of the entity in which they have invested and to assess for themselves the impact of the use of financial instruments (investments, cash/overdraft and borrowings) on the performance of the entity.

Numerical disclosures are listed in Note 20 to the Accounts. These disclosures are in line with the requirements of FRS 13.

As an investment trust, the Company invests in securities for the long term. Accordingly it is, and has been throughout the year under review, the Company's policy that no short term trading in investments or other financial instruments shall be undertaken.

The main risks arising from the Company's financial instruments are market price risk, liquidity risk and interest rate risk. The overall risk profile of the Company and the policies adopted to manage risk remain unchanged from the prior year.

Market price risk

Market price risk arises mainly from the 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 price movements. The Board meets regularly to consider the asset allocation of the portfolio in order to evaluate the risk associated with particular industry sectors. A dedicated fund manager has the responsibility for monitoring the existing portfolio selection in accordance with the Company's investment objectives and seeks to ensure that individual stocks meet an acceptable risk reward profile.

Liquidity risk

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

Interest rate risk

The Company invests predominantly in equities, the values of which are not directly affected by changes in prevailing market interest rates.

The Company finances its operations through a mixture of share capital, retained earnings and long term borrowings.

Foreign currency risk

The Company invests predominantly in UK listed securities. Accordingly, the income and capital value of the Company's investments are not materially affected by exchange rate movements.

Credit risk

As from February 2000 the Trust has commenced stock lending in order to generate additional income. The risk of default is managed by holding collateral, in the form of letters of credit, G7 bonds and G7 equities amounting to 105% of the mid value of the stock on loan. The level of collateral required is recalculated on a daily basis.

Statement of Total Return

for the year ended 31st January 2001

	Note	2001 £ Revenue	2001 £ Capital	2001 £ Total	2000 £ Revenue	2000 £ Capital	2000 £ Total
Net gains (losses) on investments	8	—	89,852,702	89,852,702	—	(30,408,125)	(30,408,125)
Exchange rate differences		—	1,158,076	1,158,076	—	(743)	(743)
Income	1	21,546,258	—	21,546,258	22,590,052	—	22,590,052
Investment management fee	2	(826,964)	(1,535,791)	(2,362,755)	(779,436)	(1,447,525)	(2,226,961)
Expenses of administration	3	(642,557)	—	(642,557)	(551,804)	—	(551,804)
Net return before finance costs and taxation		20,076,737	89,474,987	109,551,724	21,258,812	(31,856,393)	(10,597,581)
Finance costs of borrowings	4	(3,134,815)	(5,723,936)	(8,858,751)	(2,650,058)	(4,877,533)	(7,527,591)
Return on ordinary activities before taxation		16,941,922	83,751,051	100,692,973	18,608,754	(36,733,926)	(18,125,172)
Taxation	5	(184,352)	184,352	—	(221,150)	220,411	(739)
Return on ordinary activities after taxation for the financial year		16,757,570	83,935,403	100,692,973	18,387,604	(36,513,515)	(18,125,911)
Dividends on Preference Stock		(42,997)	—	(42,997)	(42,997)	—	(42,997)
Return attributable to Ordinary Shareholders		16,714,573	83,935,403	100,649,976	18,344,607	(36,513,515)	(18,168,908)
Dividends on Ordinary Shares	6	(16,769,646)	—	(16,769,646)	(16,372,630)	—	(16,372,630)
Transfer to (from) reserves		(55,073)	83,935,403	83,880,330	1,971,977	(36,513,515)	(34,541,538)
Return per Ordinary Share	7	16.35p	82.09p	98.44p	17.93p	(35.68)p	(17.75)p
Net Asset Value	15						
Per Ordinary Share				463.5p			381.4p
Per Preference Stock Unit				100.0p			100.0p

The revenue column of this statement is the profit and loss account of the Company.

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

The Notes on pages 21 to 32 form part of these Accounts.

Balance Sheet

at 31st January 2001

	Note	2001 £	2001 £	2000 £
Fixed Assets				
Investments	8		591,210,681	508,246,237
Current Assets				
Debtors	10	7,771,150		18,962,194
Cash at bank	10	1,044,517		1,586,682
		8,815,667		20,548,876
Creditors—Amounts falling due within one year	10	(13,037,160)		(25,065,412)
Net Current Liabilities			(4,221,493)	(4,516,536)
Total Assets less Current Liabilities			586,989,188	503,729,701
Creditors—Amounts falling due after more than one year	10		(112,082,455)	(112,234,418)
Total Net Assets			474,906,733	391,495,283
Capital and Reserves				
Called up Share Capital:				
Ordinary	11		25,550,984	25,582,234
Preference	11		1,178,000	1,178,000
			26,728,984	26,760,234
Capital Redemption Reserve	12		31,250	—
Share premium account			39,809	39,809
Capital Reserves: Realised	13	384,849,145		347,584,119
Capital Reserves: Unrealised	13	53,024,144		6,822,647
			437,873,289	354,406,766
Revenue Reserve	14		10,233,401	10,288,474
Shareholders' Funds	16		474,906,733	391,495,283
Analysis of Shareholders' Funds				
Equity interests	15		473,728,733	390,317,283
Non-equity interests	15		1,178,000	1,178,000
			474,906,733	391,495,283

Approved by the Board of Directors on 5th April 2001
and signed on its behalf by:

Hugh Stevenson
Joe Scott Plummer
Directors

The Notes on pages 21 to 32 form part of these Accounts

Cash Flow Statement

for the year ended 31st January 2001

	Note	2001 £	2001 £	2000 £
Net cash inflow from operating activities	18		17,748,009	20,942,289
Servicing of finance				
Interest paid		(8,850,396)		(7,340,354)
Preference dividends paid		(42,997)		(42,997)
Net cash outflow on servicing of finance			(8,893,393)	(7,383,351)
Taxation				
UK income tax repaid		865,492		47,545
Advance corporation tax recovered		—		142,667
Net tax repaid			865,492	190,212
Investing Activities				
Payments to acquire fixed asset investments		(334,875,548)		(444,356,135)
Proceeds on disposal of fixed asset investments		340,271,533		412,048,368
Net cash inflow (outflow) from financial investment			5,395,985	(32,307,767)
Equity dividends paid			(16,677,567)	(16,362,397)
Net cash outflow before financing			(1,561,474)	(34,921,014)
Financing				
Increase (decrease) in short term loan		1,488,189		(497,256)
Issue of Secured Bonds		—		28,942,800
Purchase of Ordinary Shares for cancellation		(468,880)		—
Cash inflow from financing			1,019,309	28,445,544
Decrease in cash	19		(542,165)	(6,475,470)

The Notes on pages 21 to 32 form part of these Accounts.

Statement of Accounting Policies

for the year ended 31st January 2001

(i) The financial statements have been prepared under the historical cost convention, modified to include the revaluation of investments, and in accordance with applicable accounting standards including the Statement of Recommended Practice – "Financial Statements of Investment Trust Companies" issued by the Association of Investment Trust Companies.

(ii) Revenue – Dividends on equity shares are accounted for on an ex-dividend basis. UK dividends are shown net of tax credits and foreign dividends are grossed up at the appropriate rate of withholding tax. Income from convertible securities having an element of equity is recognised on an accruals basis. Fixed returns on non-equity shares are recognised on an accruals basis.

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

Deposit interest receivable and stock lenders' fee income are accounted for on an accruals basis. Underwriting commission is recognised when the issue underwritten closes.

(iii) Investment management fee – The investment management fee is calculated on the basis set out in Note 2 to the financial statements and is charged to capital and revenue in the ratio 65:35 to reflect the prospective split of capital and income returns.

(iv) Valuation—Investments listed in the United Kingdom have been valued at middle market prices. Those listed abroad have been valued at closing or middle market prices as available. Unlisted investments are valued by the Directors based upon the latest dealing prices, stockbrokers' valuations, net asset values, earnings and other known accounting information in accordance with the principles set out by the British Venture Capital Association. An unrealised Capital Reserve has been established to reflect differences between value and book cost.

Net gains or losses arising on realisations of investments are taken directly to a realised Capital Reserve.

(v) Finance costs – In accordance with Financial Reporting Standard 4 "Capital Instruments", long term borrowings are stated at the amount of net proceeds immediately after issue plus the appropriate accrued finance costs at the balance sheet date. The finance costs of such borrowings, being the difference between the net proceeds of a borrowing and the total payments that may be required in respect of that borrowing, are allocated to periods over the term of the debt at a constant rate on the carrying amount. Finance costs on long term borrowings are charged to Capital Reserves and the Revenue Account in the ratio 65:35 to reflect the Company's prospective split of capital and income returns.

(vi) Taxation – Where expenses are allocated between capital and revenue, any tax relief obtained in respect of those expenses is allocated between capital and revenue, using the Company's effective rate of corporation tax for the accounting period.

Deferred taxation, where applicable, is provided for on the liability method on all timing differences which are expected to crystallise in the foreseeable future, calculated at the rate at which it is estimated that the tax liability or asset will accrue.

(vii) Foreign currency – Transactions in foreign currencies are translated into sterling at the rates of exchange ruling on the date of the transaction. Foreign currency assets and liabilities are translated into sterling at the rates of exchange ruling at the balance sheet date. Profits and losses thereon are recognised in Capital Reserves.

(viii) No Statement of Recognised Gains and Losses as required by Financial Reporting Standard 3 has been prepared. The Managers consider that the additional information provided would not add materially to the information disclosed in the Statement of Total Return from which recognised gains and losses can be derived.

Notes to the Accounts

for the year ended 31st January 2001

1. Income

	2001 £	2001 £	2000 £
Income from Investments			
Equity income from UK investments		18,956,896	19,408,241
Special dividends from UK investments		1,240,814	1,335,600
Unfranked income:			
Interest from UK fixed income securities	957,769		926,532
Dividends from overseas equity securities	—		70,969
Interest from overseas fixed income securities	63,139		202,100
Foreign income dividends from UK equity securities	—		412,540
		1,020,908	1,612,141
		21,218,618	22,355,982
Other income			
Deposit interest	310,266		222,707
Underwriting commission	6,527		11,363
Stocklending fees	10,847		—
		327,640	234,070
Total income		21,546,258	22,590,052
Income from Investments			
Listed		21,218,618	22,343,243
Unlisted		—	12,739
		21,218,618	22,355,982

2. Investment Management Fee

	2001 £ Revenue	2001 £ Capital	2001 £ Total	2000 £ Revenue	2000 £ Capital	2000 £ Total
Investment management fee	826,964	1,535,791	2,362,755	779,436	1,447,525	2,226,961

The management contract with Dresdner RCM Global Investors (UK) Ltd ("Dresdner RCM"), terminable at one year's notice, provides for a management fee based on 0.35% (2000 – 0.35%) per annum of the value of the Company's assets calculated quarterly after deduction of current liabilities, short-term loans under one year and any funds within the portfolio managed by Dresdner RCM. The amounts stated include irrecoverable VAT of £351,900 (2000 – £331,675). Under the contract Dresdner RCM provides the Company with investment management, accounting, secretarial, administration and custodial services.

Notes to the Accounts

for the year ended 31st January 2001

3. Expenses of Administration

	2001 £	2000 £
Directors' fees	70,637	76,915
Auditors' remuneration for audit services	13,548	11,860
Marketing costs	302,472	167,630
Contribution to "**its**" campaign costs	56,558	99,168
Other administrative expenses	199,342	196,231
	642,557	551,804

(i) The above expenses include value added tax where applicable.

(ii) There were no payments in respect of non-audit services included in other administrative expenses (2000 – £2,408).

(iii) Directors' fees are paid at the rate of £10,000 (2000 – £10,000) per annum with an additional sum of £3,000 (2000 – £3,000) per annum paid to the Chairman of the Audit Committee and an additional sum of £5,000 (2000 – £5,000) per annum paid to the Chairman.

4. Finance Costs of Borrowings

	2001 £ Revenue	2001 £ Capital	2001 £ Total	2000 £ Revenue	2000 £ Capital	2000 £ Total
On Stepped Rate Interest Loan repayable after more than five years	1,091,316	2,026,728	3,118,044	1,205,200	2,238,229	3,443,429
On Fixed Rate Interest Loan repayable after more than five years	1,326,416	2,463,344	3,789,760	1,328,899	2,467,957	3,796,856
On 4% Perpetual Debenture Stock repayable after more than five years	19,250	35,750	55,000	19,250	35,750	55,000
On 5.875% Secured Bonds repayable after more than five years	645,138	1,198,114	1,843,252	73,014	135,597	208,611
On sterling overdraft	52,695	—	52,695	23,695	—	23,695
	3,134,815	5,723,936	8,858,751	2,650,058	4,877,533	7,527,591

Included in the finance costs of the 5.875% Secured Bonds 2029 is £26,731 payable to the Auditors in respect of non-audit services.

5. Taxation

	2001 £ Revenue	2001 £ Capital	2001 £ Total	2000 £ Revenue	2000 £ Capital	2000 £ Total
Credit for expenses allocated to capital	184,352	(184,352)	—	220,411	(220,411)	—
Overseas taxation	—	—	—	739	—	739
	184,352	(184,352)	—	221,150	(220,411)	739

6. Dividends on Ordinary Shares

	2001 £	2000 £
Dividends on Ordinary Shares of 25p—		
First interim 4.10p paid 24th August 2000 (1999 – 3.95p)	4,195,486	4,041,993
Second interim 4.10p paid 10th November 2000 (1999 – 3.95p)	4,193,436	4,041,993
Third interim 4.10p paid 16th February 2001 (1999 – 4.05p)	4,190,362	4,144,322
Final proposed – ordinary dividend 4.10p paid 17th May 2001 (1999 – 4.05p)	4,190,362	4,144,322
	16,769,646	16,372,630

The proposed final dividend accrued is based on the number of shares in issue at the year end. However, the dividend payable will be based on the number of shares in issue on the record date and will reflect any purchases and cancellation of shares by the Company settled subsequent to the year end.

Ordinary dividends paid by the Company carry a tax credit of 10%. The credit discharges the tax liability of shareholders subject to income tax at less than the higher rate. Shareholders liable to pay tax at the higher rate will have further tax to pay. PEP and ISA holders may be able to reclaim this tax credit and charities are subject to transitional provisions.

7. Return per Ordinary Share

	2001 £ Revenue	2001 £ Capital	2001 £ Total	2000 £ Revenue	2000 £ Capital	2000 £ Total
Return after taxation	16,757,570	83,935,403	100,692,973	18,387,604	(36,513,515)	(18,125,911)
Attributable to Preference Stockholders	(42,997)	—	(42,997)	(42,997)	—	(42,997)
Attributable to Ordinary Shareholders	16,714,573	83,935,403	100,649,976	18,344,607	(36,513,515)	(18,168,908)
Return per Ordinary Share	16.35p	82.09p	98.44p	17.93p	(35.68)p	(17.75)p

The return per Ordinary Share is based on a weighted average of 102,250,726 Ordinary Shares of 25p in issue throughout the period (2000 – 102,328,936).

Notes to the Accounts

for the year ended 31st January 2001

8. Fixed Asset Investments

	Note	2001 £	2000 £
Listed at market valuation on recognised Stock Exchanges—			
United Kingdom		591,159,223	501,741,736
Abroad		—	6,261,257
		591,159,223	508,002,993
Unlisted at Directors' valuation—			
Abroad		51,458	35,359
Subsidiary at Directors' valuation	9	—	207,885
		51,458	243,244
Total fixed asset investments		591,210,681	508,246,237
Market value of investments brought forward		508,246,237	508,503,479
Unrealised gains brought forward		(6,822,647)	(76,884,400)
Cost of investments held brought forward		501,423,590	431,619,079
Additions at cost		320,738,103	447,509,026
Disposals at cost		(283,975,156)	(377,704,515)
Cost of investments held at 31st January		538,186,537	501,423,590
Unrealised gains at 31st January		53,024,144	6,822,647
Market value of investments held at 31st January		591,210,681	508,246,237
Gains on investments			
Net realised gains based on historical costs		43,651,205	39,653,628
Less: Net unrealised gains recognised on these investments at the previous balance sheet date		(44,810,715)	(31,339,013)
Net realised (losses) gains based on carrying value at previous balance sheet date		(1,159,510)	8,314,615
Net unrealised gains (losses) arising in the year		91,012,212	(38,722,740)
Net gains (losses) on investments		89,852,702	(30,408,125)

The Board considers that the Company's remaining unquoted investment is not material to the financial statements.

Stock Lending	£	£
Aggregate value of securities on loan at year-end	6.8m	—
Maximum aggregate value of securities on loan during the year	32.7m	—
Fee income from stock lending during the year	10,847	—

In respect of securities on loan at the year-end, the Company held £7.2m (2000 – £nil) letters of credit as collateral, the value of which exceeded the value of the loan securities by £0.4m (2000 – £nil).

In respect of the maximum aggregate value of securities on loan during the year, the Company held £34.4m (2000 – £nil) as collateral, the value of which exceeded the value of the securities on loan, by £1.7m (2000 – £nil).

9. Investments in Subsidiary and Other Companies

Surrey Investments Inc. is a wholly owned subsidiary registered in the State of Delaware, U.S.A. with an issued share capital of US$300,000. It was formed to act as a Limited Partner in JW O'Connor Associates LP and a shareholder in JW O'Connor & Co Inc., both of which are engaged in property development in the US. This company is now in the process of liquidation following the disposal of the interest in O'Connor.

The Company has not produced consolidated accounts in view of the immaterial amounts involved.

The Company held more than 10% of the share capital of the following companies, both of which are incorporated in Great Britain and registered in England and Wales:

Company	Class of Shares Held	% of Class held	% Equity
First Debenture Finance PLC ('FDF')	'B' Shares	41.0	20.4
Fintrust Debenture PLC ('Fintrust')	Ordinary	49.5	49.5

In the opinion of the Directors, the Company is not in a position to exert significant influence over these companies. The aggregate share capital, reserves and results are immaterial to the Trust's accounts. FDF and Fintrust are the lenders of the Company's Stepped Rate Loan and Fixed Rate Interest Loan, as detailed in notes 10(i) and (ii), respectively. The finance costs of these borrowings and outstanding balances at the year end are shown in notes 4 and 10 respectively. Apart from the finance costs and the provision of a short term loan by FDF, there were no other transactions between FDF, Fintrust and the Company during the year.

10. Current Assets and Creditors

	2001 £	2000 £
Debtors—		
Sales for future settlement	4,802,246	16,289,342
Accrued income	2,940,209	2,476,885
Other debtors	28,695	53,152
Taxation recoverable	—	142,815
	7,771,150	18,962,194
Cash at bank—		
Sterling bank balances—		
Current account	404,517	125,724
Deposit accounts		
Barclays Bank plc	640,000	342,044
Kleinwort Benson Private Bank Ltd	—	1,118,914
	1,044,517	1,586,682

Notes to the Accounts

for the year ended 31st January 2001

10. Current Assets and Creditors (continued)

	Note	2001 £	2000 £
Creditors: Amounts falling due within one year—			
Taxation payable		650,578	—
Purchases for future settlement		—	14,137,445
Short term loan		1,488,189	—
Other creditors		1,176,904	1,458,876
Interest on borrowings (see (vi) below)		1,319,266	1,158,948
Dividend on Cumulative Preference Stock Units		21,499	21,499
Dividend on Ordinary Shares (declared)	6	4,190,362	4,144,322
Dividend on Ordinary Shares (proposed)	6	4,190,362	4,144,322
		13,037,160	25,065,412
Creditors: Amounts falling due after more than one year—			
Stepped Rate Interest Loan (see (i) below)		34,900,297	34,812,495
Fixed Rate Interest Loan (see (ii) below)		46,849,398	46,949,468
5.875% Secured Bonds 2029 (see (iii) below)		28,957,760	29,097,455
4% Perpetual Debenture Stock (see (iv) below)		1,375,000	1,375,000
		112,082,455	112,234,418

(i) The Stepped Rate Interest Loan comprises adjustable Stepped Rate Interest Loan Notes of £5,133,520 and Stepped Rate Interest Bonds of £20,534,079 issued at 97.4%. £34,034,112 is repayable in 2018 inclusive of a premium of £8,366,513 but exclusive of any redemption expenses. Interest, payable on the Bonds in July and January, was an initial rate of 7.16% per annum increasing annually by 7.5% compound until January 1998. Thereafter it became payable at 14.75% per annum until maturity on 2nd January 2018. Interest on the Loan Notes is variable in accordance with the terms of the agreement with the lender, First Debenture Finance PLC ("FDF").

The effective interest rate of the Stepped Rate Interest loan over its term is 11.28% per annum.

The Company has guaranteed the repayment of £34,012,852, being its proportionate share (42.52%) of the required amount to enable FDF to meet all of its liabilities to repay principal and interest on its £80 million of 11.125% Severally Guaranteed Debenture Stock 2018. There is a floating charge on all the Company's present and future assets to secure this obligation. The Company has also agreed to meet its proportionate share of any expenses incurred by FDF, including any tax liability which may accrue to FDF as a result of the redemption or earlier transfer of the Stepped Rate Loan Notes and Bonds held by FDF. The accounting treatment adopted in respect of the stepped rate interest and redemption premiums is set out in the Statement of Accounting Policies.

(ii) The Fixed Rate Interest Loan of £42,000,000 is due to Fintrust Debenture PLC ('Fintrust'). This loan is repayable in 2023 and carries interest at the rate of 9.25125% per annum on the principal amount payable in arrears by equal half yearly instalments in May and November in each year. As security for this loan, the Company has granted a floating charge over all its undertakings, property and assets in favour of the lender. This charge ranks pari passu with the floating charge noted in (i) above.

Following the liquidation of Kleinwort Overseas Investment Trust plc ('KOIT') in March 1998, the Company assumed £12,000,000 of its obligations to Fintrust. Both the interest cost and repayment terms of this additional borrowing are identical to the Company's existing loan. In order that the finance costs on this new borrowing be comparable to existing market rates at that time, the Company also received a premium payment from KOIT of £5,286,564. This premium is being amortised over the remaining life of the loan in accordance with FRS 4, as set out in the Statement of Accounting Policies. At 31st January 2001, the unamortised premium included within the Fixed Rate Interest Loan balance of greater than one year amounted to £4,980,907 (2000 £5,082,626).

The original loan from Fintrust is stated at net proceeds (being the principal amount of £30,000,000 less issue costs of £141,053) plus accrued finance costs.

10. Current Assets and Creditors (continued)

(iii) The £30,000,000 5.875% Secured Bonds, repayable on 20th December 2029, carry interest at the rate of 5.875% per annum on the principal amount payable in arrears by equal half yearly instalments in June and December in each year. As security for this loan the Company has granted a floating charge ranking pari passu with the floating charges referred to in note (i) and (ii) above over the whole of the present and future undertakings, property, assets and rights of the Company.

The accounting treatment adopted in respect of the Bond is set out in the Statement of Accounting Policies.

(iv) The 4% Perpetual Debenture Stock is secured by a floating charge on the assets of the Company, which ranks prior to any other floating charge.

(v) The short term loan from FDF is interest free and repayable on demand.

(vi) Interest on borrowings consists of interest on the following:

	2001	**2000**
	£	**£**
Stepped Rate Interest Loan	313,728	312,003
Fixed Rate Interest Loan	783,545	779,240
5.875% Secured Bond 2029	208,243	53,955
4% Perpetual Debenture Stock	13,750	13,750
	1,319,266	1,158,948

11. Share Capital

		2001	**2000**
		£	**£**
Authorised			
1,178,000	3.65% Cumulative Preference Stock Units of £1	1,178,000	1,178,000
107,431,248	Ordinary Shares of 25p	26,857,812	26,857,812
Allotted and fully paid			
1,178,000	3.65% Cumulative Preference Stock Units of £1	1,178,000	1,178,000
102,203,936	Ordinary Shares of 25p (2000 – 102,328,936)	25,550,984	25,582,234
		26,728,984	26,760,234

(i) The Cumulative Preference Stock Units have been classified as non-equity interests in shareholders' funds under the provisions of FRS 4 on Capital Instruments. The rights of the Stock to receive payments are not calculated by reference to the Company's profits and, in the event of a return of capital are limited to a specific amount, being £1,178,000.
Dividends on the Preference Stock are payable half yearly on 1st August and 1st February.

(ii) The Directors are authorised by an ordinary resolution passed on 8th May 2000 to allot relevant securities, in accordance with Section 80 of the Companies Act 1985, up to a maximum aggregate nominal amount of £1,275,578. This authority, if not previously revoked or varied, expires five years from the date of the resolution.
The Directors are also authorised by a special resolution passed on 8th May 2000 to allot relevant securities for cash, in accordance with Section 95 of the Companies Act 1995, up to a maximum aggregate nominal amount of £1,275,578. This authority, if not previously revoked or renewed, expires at the next Annual General Meeting and a resolution will be proposed at the Annual General Meeting for its renewal.

Notes to the Accounts

for the year ended 31st January 2001

12. Capital Redemption Reserve

The balance on this account was created by the transfer of £31,250 in respect of 125,000 Ordinary Shares of 25p each which were purchased by the Company and subsequently cancelled.

13. Capital Reserves

	Realised £	Unrealised £	Total £
Balance at 1st February 2000	347,584,119	6,822,647	354,406,766
Net loss on realisation of investments	(1,159,510)	—	(1,159,510)
Increase in unrealised appreciation	—	91,012,212	91,012,212
Transfer on disposal of investments	44,810,715	(44,810,715)	—
Exchange rate differences	1,158,076	—	1,158,076
Investment management fee	(1,535,791)	—	(1,535,791)
Finance costs of borrowings	(5,723,936)	—	(5,723,936)
Attributable taxation in respect of management fee and finance costs	184,352	—	184,352
Purchase of ordinary shares for cancellation	(468,880)	—	(468,880)
Balance at 31st January 2001	384,849,145	53,024,144	437,873,289

14. Revenue Reserve

	£
Balance at 1st February 2000	10,288,474
Deficit for the year	(55,073)
Balance at 31st January 2001	10,233,401

15. Net Asset Value per Share

The Net Asset Value per share (which equals the net asset values attributable to each class of share at the year end calculated in accordance with the Articles of Association) were as follows:

	Net Asset Value per Share attributable 2001	2000
Ordinary Shares of 25p	463.5p	381.4p
3.65% Cumulative Preference Stock Units of £1	100.0p	100.0p

	Net Asset Values attributable 2001 £	2000 £
Ordinary Shares of 25p	473,728,733	390,317,283
3.65% Cumulative Preference Stock Units of £1	1,178,000	1,178,000

The movements during the year of the assets attributable to each class of share were as follows:

	Ordinary Shares £	Cumulative Preference Stock £	Total £
Total net assets attributable at 1st February 2000	390,317,283	1,178,000	391,495,283
Total return on ordinary activities after taxation for the year	100,649,976	42,997	100,692,973
Purchase of Ordinary Shares for cancellation	(468,880)	—	(468,880)
Dividends appropriated in the year	(16,769,646)	(42,997)	(16,812,643)
Total net assets attributable at 31st January 2001	473,728,733	1,178,000	474,906,733

The Net Asset Value per Ordinary Share is based on 102,203,936 Ordinary Shares in issue at the year end (2000 – 102,328,936).

16. Reconciliation of Movements in Shareholders' Funds

	2001 £	2000 £
Revenue reserves		
Revenue profit available for distribution	16,757,570	18,387,604
Dividends appropriated in the year	(16,812,643)	(16,415,627)
Transfer (from) to distributable reserves	(55,073)	1,971,977
Other reserves		
Recognised net capital profits (losses) transferred to capital reserves	83,935,403	(36,513,515)
Purchase of Ordinary Shares for cancellation	(468,880)	—
Net increase (decrease) in Shareholders' Funds	83,411,450	(34,541,538)
Opening Shareholders' Funds	391,495,283	426,036,821
Closing Shareholders' Funds	474,906,733	391,495,283

17. Contingent Liabilities and Guarantees

At 31st January 2001 there were no outstanding contingent liabilities (2000 – £nil) in respect of underwriting commitments and calls on partly paid investments.

Details of the guarantee provided by the Company as part of the terms of its Stepped Rate Loan are provided in Note 10(i) "Current Assets and Creditors" on page 26.

18. Reconciliation of Operating Revenue before Taxation to Net Cash Inflow from Operating Activities

	2001 £	2000 £
Revenue before taxation	16,941,922	18,608,754
Add: Finance costs of borrowings	3,134,815	2,650,058
Less: Management fee charged to capital	(1,535,791)	(1,447,525)
Less: Overseas tax suffered	—	(739)
Less: UK income tax deducted from unfranked income	(72,098)	(178,299)
	18,468,848	19,632,249
(Increase) decrease in debtors	(438,867)	697,210
(Decrease) increase in creditors	(281,972)	612,830
Net cash inflow from operating activities	17,748,009	20,942,289

Notes to the Accounts

for the year ended 31st January 2001

19. Reconciliation of net cash flow to movement in net debt

(i) Analysis of Net Debt

	Cash	Short term loan	Stepped and Fixed Rate loans	5.875% Secured Bond 2029	4% Perpetual Debenture Stock	Net Debt
	£	£	£	£	£	£
At 1st February 2000	1,586,682	—	(81,761,963)	(29,097,455)	(1,375,000)	(110,647,736)
Movement in year	(542,165)	(1,488,189)	12,268	139,695	—	(1,878,391)
At 31st January 2001	1,044,517	(1,488,189)	(81,749,695)	(28,957,760)	(1,375,000)	(112,526,127)

(ii) Reconciliation of net cash flow to movement in net debt

	2001	2000
	£	£
Net cash outflow	(542,165)	(6,475,470)
(Increase) decrease in short term loan	(1,488,189)	497,256
Decrease (increase) in long term loans	151,963	(29,082,111)
Movement in net funds	(1,878,391)	(35,060,325)
Net debt brought forward	(110,647,736)	(75,587,411)
Net debt carried forward	(112,526,127)	(110,647,736)

20. Financial Reporting Standard 13 – Derivatives and other Financial Instruments: Disclosures

The note below should be read in conjunction with the Risk Review of the Company detailed on page 16.

(a) Interest Rate Risk Profile

The tables below summarise in sterling terms the assets and liabilities whose values are affected by changes in interest rates, together with the weighted average rates and periods for which rates are fixed on the fixed interest bearing assets and liabilities.

	Currency	2001 Fixed rate interest paid £000s	2001 Floating rate interest paid £000s	2001 Nil interest paid £000s	2001 Total £000s	2000 Fixed rate interest paid £000s	2000 Floating rate interest paid £000s	2000 Nil interest paid £000s	2000 Total £000s
Financial Assets									
Values directly affected by changes in interest rates:									
Treasury Stocks	Sterling	—	—	—	—	26,708	—	—	26,708
		—	—	—	—	26,708	—	—	26,708
Values not directly affected by changes in interest rates:									
Equities	Sterling	—	—	578,675	578,675	—	—	446,311	446,311
Equities	US Dollar	—	—	51	51	—	—	243	243
Preference Shares and Bonds	Sterling	12,484	—	—	12,484	19,971	—	—	19,971
Bonds	US Dollar	—	—	—	—	15,013	—	—	15,013
Cash	Sterling	—	1,045	—	1,045	—	1,587	—	1,587
		12,484	1,045	578,726	592,255	34,984	1,587	446,554	483,125
Total Financial Assets		12,484	1,045	578,726	592,255	61,692	1,587	446,554	509,833
Financial Liabilities									
Values affected by changes in interest rates:									
First Debenture Finance loan	Sterling	(46,849)	—	—	(46,849)	(34,813)	—	—	(34,813)
Fintrust loan	Sterling	(34,900)	—	—	(34,900)	(46,950)	—	—	(46,950)
5.875% Secured Bonds 2029	Sterling	(28,958)	—	—	(28,958)	(29,097)	—	—	(29,097)
4% Perpetual Debenture Stock	Sterling	(1,375)	—	—	(1,375)	(1,375)	—	—	(1,375)
Total Financial Liabilities		(112,082)	—	—	(112,082)	(112,235)	—	—	(112,235)
Net Financial Assets		(99,598)	1,045	578,726	480,173	(50,543)	1,587	446,554	397,598
Short term debtors and creditors					(5,266)				(6,103)
Net Assets per Balance Sheet					**474,907**				**391,495**

Notes to the Accounts

for the year ended 31st January 2001

20. Financial Reporting Standard 13 – Derivatives and other Financial Instruments: Disclosures (continued)

The fixed rate interest liabilities bear the following coupon and effective rates:

	Maturity date	Amount borrowed £	Coupon rate	Effective rate since inception*
First Debenture Finance loan—bonds	2/1/2018	20,534,079	14.75%	11.28%
First Debenture Finance loan—notes	2/1/2018	5,133,520	14.75%	11.28%
Fintrust—original loan	20/11/2023	30,000,000	9.25125%	9.30%
Fintrust—new loan	20/11/2023	12,000,000	9.25125%	6.00%
5.875% Secured Bond	20/11/2029	30,000,000	5.875%	6.13%
4% Perpetual Debenture Stock	n/a	1,375,000	4.00%	n/a

*The effective rates are calculated in accordance with FRS 4 as detailed in the Accounting Policies.

The weighted average coupon rate of the Company's fixed interest bearing liabilities is 9.58% (2000 – 9.58%) and the weighted average period to maturity of these liabilities (excluding the 4% perpetual debenture stock) is 23.2 years (2000 – 24.2) years.

The weighted average coupon rate of the Company's fixed interest bearing assets is 6.41% (2000 – 6.01%) and the weighted average period to maturity of those assets is 3.2 years (2000 – 4.1) years.

(b) Currency Risk Profile

A portion of the assets and liabilities of the Company is denominated in currencies other than Sterling, with the effect that the total net assets and total return can be affected by currency movements.

	2001 Investments £000s	2001 Current Assets £000s	2001 Creditors £000s	2001 Net currency exposure £000s	2000 Investments £000s	2000 Current Assets £000s	2000 Creditors £000s	2000 Net currency exposure £000s
Sterling	591,160	8,816	(125,120)	474,856	492,990	20,549	(137,300)	376,239
US Dollar	51	—	—	51	15,256	—	—	15,256
	591,211	8,816	(125,120)	474,907	508,246	20,549	(137,300)	391,495

(c) Fair Values Disclosures

The assets and liabilities of the Company are held at fair value with the exception of the FDF and Fintrust loans shown below:

	2001 £ million Book value	2001 £ million Fair value	2000 £ million Book value	2000 £ million Fair value
First Debenture Finance Loan	34.8	50.9	34.8	50.6
Fintrust loan	46.9	57.8	46.9	58.4

(d) Liquidity profile

The maturity profile of the Company's financial liabilities at the 31st January 2001 (being the borrowings from Fintrust, First Debenture Finance, the 5.875% Secured Bond and the 4% Perpetual Debenture stock) is detailed in Note 10—"Current Assets and Creditors" on pages 25 to 27. The undrawn committed borrowing facilities available to the Company at 31st January 2001 were £10 million.

(e) Hedging instruments

At the year end the Company had no hedging arrangements in place. (2000 – Nil)

Report of the Auditors

Independent auditors' report to the members of The Merchant Trust PLC

We have audited the financial statements on pages 17 to 32 which have been prepared under the historical cost convention (as modified by the revaluation of investments) and the accounting policies set out on page 20.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements, United Kingdom Auditing Standards issued by the Auditing Practices Board and the Listing Rules of the Financial Services Authority.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, 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 or the Listing Rules regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the directors' report, the chairman's statement, the operating and financial review and the corporate governance statement.

We review whether the corporate governance statement reflects the company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules, 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 to form an opinion on the effectiveness of the company's corporate governance procedures or its risk and control procedures.

Basis of audit opinion

We conducted our audit in accordance with auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether 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 financial statements 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 financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of the company's affairs at 31st January 2001 and of its total return and cash flows for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers
Chartered Accountants
and Registered Auditors

5th April 2001

Southwark Towers
32 London Bridge Street
London SE1 9SY

Statement of Directors' Responsibilities

Company law requires the Directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and of the revenue of the Company for that period. In preparing those financial statements, the Directors are required to:

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

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements 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.

Corporate Governance

The Board has put in place a framework for corporate governance which it believes is appropriate for an investment trust company and which enables the Company to comply with the Combined Code on Corporate Governance ("the Combined Code") issued by the Financial Services Authority.

The Board considers that the Company has complied with the provisions contained within Section 1 of the Combined Code throughout the year ended 31st January 2001 except that full compliance with the Internal Control Guidance for Directors in the Combined Code published in September 1999 ("the Turnbull guidance") was not achieved until part way through the year. As detailed below, the Board has not identified a senior non-executive Director. This statement describes how the relevant principles of governance are applied to the Company.

The Board

The Board currently consists of six Directors, all of whom are non-executive and deemed by the Board to be independent of the Company's investment manager. Their biographies, on page 37, demonstrate a breadth of investment, industrial and commercial experience.

The Board meets at least six times a year and between these meetings there is regular contact with the Investment Manager. Matters specifically reserved for decision by the full Board have been defined and a procedure adopted for Directors, in the furtherance of their duties, to take independent professional advice at the expense of the Company. The Directors have access to the advice and services of the Company Secretary who is responsible to the Board for ensuring that Board procedures are followed and that applicable rules and regulations are complied with.

When a new Director is appointed there is an induction process carried out by the Investment Manager. Directors are provided, on a regular basis, with key information on the Company's policies, regulatory and statutory requirements and internal controls. Changes affecting Directors' responsibilities are advised to the Board as they arise.

A senior non-executive Director has not been identified as the Board considers that this is not necessary for a non-executive Board of this size where the positions of Chairman of the Board and Chairman of the Audit Committee are held by different Directors.

The Board has contractually delegated to the Investment Manager the management of the investment portfolio, the custodial services and the day to day accounting and company secretarial requirements. This contract was entered into after due consideration by the Board of the quality and cost of services offered including the internal control systems in operation in so far as they relate to the affairs of the Company. The Board receives and considers reports regularly from the Investment Manager and ad hoc reports and information are supplied to the Board as required.

All non-executive Directors are appointed for an initial term of three years, subject to re-election and Companies Act provisions. In accordance with the Articles of Association, new Directors stand for election at the first Annual General Meeting following their appointment and every Director stands for re-election at intervals of not more than three years.

Board Committees

The Board has established a nominations committee to make recommendations on the appointment and re-appointment of Directors. Due to its size, the Board as a whole considers nominations made in accordance with an agreed procedure. The Audit Committee carries out the functions of a management engagement committee, to review and discuss the terms of the management contract with the Investment Manager.

The Audit Committee consisting of the full Board has defined terms of reference and duties. This committee is also responsible for review of the annual accounts and interim report, terms of appointment of the auditors together with their remuneration as well as the non-audit services provided by the auditors. It also meets with representatives of the Investment Manager and receives reports on the effectiveness of the internal controls maintained on behalf of the Company and reviews the effectiveness of the Company's internal controls.

Environmental Policy

The Investment Managers have been directed by the Board to take account of companies' environmental performance when taking investment decisions.

Directors' Remuneration

Under the Financial Services Authority's Listing Rule 21.20(i), where an investment trust company has no executive Directors the Code principles relating to Directors' remuneration do not apply and accordingly the financial statements do not include a Directors' Remuneration Report.

Relations with Shareholders

The Board strongly believes that the Annual General Meeting should be an event which private shareholders are encouraged to attend and in which they are invited to participate. The Annual General Meeting is attended by the Chairman of the Board and the Chairman of the Audit Committee and the Investment Manager makes a presentation to the meeting.

The Notice of Meeting sets out the business of the meeting and resolutions proposed under special business are explained more fully in the Directors' Report on pages 38 to 42. Separate resolutions are proposed for each substantive issue.

Corporate Governance

Accountability and Audit

The Directors' statement of responsibilities in respect of the accounts is on page 34 and a statement of going concern is on page 38.

The report of the auditors can be found on page 33.

Internal Control

The Directors have overall responsibility for the Company's system of internal controls. Whilst acknowledging their responsibility for the system of internal control, the Directors are aware that such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can provide only reasonable but not absolute assurance against material misstatement or loss.

The Board has established an ongoing process for identifying, evaluating and managing the significant risks faced by the Company. This process is subject to review by the Board and accords with the Turnbull guidance. The process was fully in place from 8th May 2000 and up to the date of the signing of this Report and Accounts. During the earlier months of 2000, the Board's review of the measures necessary to implement the Turnbull guidance was being finalised.

The key elements of the procedures that the Directors have established and which are designed to provide effective internal control are as follows:

▶ The Board, assisted by the Managers, undertook a full review of the Company's business risks and these are analysed and recorded in a risk matrix. The Board receives every six months from the Managers a formal report which details any known internal controls failures, including those that are not directly the responsibility of the Managers. Steps will be taken to continue to ensure that the system of internal control and risk management becomes embedded into the operations and culture of the Company and its key suppliers.

▶ The appointment of Dresdner RCM Global Investors (UK) Limited ('Dresdner RCM') as the Managers and Custodian. Dresdner RCM provides all investment management, custodial, accounting and secretarial services to the Company. The Managers and Custodian maintain the internal controls associated with the day to day operation of the Company. These responsibilities are included in the Management Agreement between the Company and the Managers (see page 21). The Managers' system of internal control includes organisation arrangements with clearly defined lines of responsibility and delegated authority as well as control procedures and systems which are regularly evaluated by management and monitored by their internal audit department. Dresdner RCM is regulated by IMRO and its compliance department regularly monitors their compliance with IMRO rules. The effectiveness of the internal controls is assessed by the Managers' compliance and risk management department on an ongoing basis.

▶ The regular review and control by the Board of asset allocation and any risk implications. Regular and comprehensive review by the Board of management accounting information including revenue and expenditure projections, actual revenue against projections, and performance comparisons.

▶ Authorisation and exposure limits are set and maintained by the Board.

▶ An Audit Committee which reviews the terms of the agreement with the Managers and Custodians, assesses the Managers' and Custodians' systems of controls and approves the appointment of sub-custodians. The Audit Committee also receives reports from the Managers' and Custodians' internal auditors and compliance department.

The Board has undertaken a full review of the aspects covered by the Turnbull guidance and believes that there is an effective framework substantially in place to meet the requirements of the Combined Code.

Exercise of Voting Powers

The Company's investments are held in a nominee name. The Board has delegated discretion to the Managers to exercise voting powers on its behalf.

Directors and Management

Directors

Hugh Stevenson* (Chairman)

(Born September 1942) joined the board in September 1999. Formerly Chairman of Mercury Asset Management Group plc, he is Chairman of Equitas Limited, a Director of Standard Life Assurance Company and a member of the Investment Committee of the Wellcome Trust.

Sir John Banham*

(Born August 1940) joined the Board in August 1992. Formerly Director General of the Confederation of British Industry, he is Chairman of Kingfisher PLC, ECI Ventures Ltd and Whitbread PLC. He is also a Director of Amvescap Plc.

Dick Barfield*

(Born April 1947) joined the board in May 1999. Formerly Chief Investment Manager of Standard Life Assurance Company, he is a Director of Equitas Limited, Baillie Gifford Japan Trust PLC, Marshalls PLC, New Look Group PLC and other companies.

Anthony Forbes*

(Born January 1938) joined the Board in July 1994. Formerly joint senior partner of Cazenove & Co, he is a Director of Royal and Sun Alliance Insurance Group plc and Carlton Communications plc.

Sir Bob Reid*

(Born May 1934) joined the Board in January 1995. Formerly Chairman of Shell (UK), British Rail, London Electricity plc, and Sears PLC he is a Deputy Governor of the Bank of Scotland.

Joe Scott Plummer*

(Born August 1943) joined the Board in May 1997. He is Chairman of Martin Currie Limited and is a Director of Candover Investments PLC and Martin Currie Portfolio Investment Trust PLC.

*All of the above Directors are non-executive and independent of the Manager, and each serves on the Company's Audit and Nomination Committees.

Directors' Report

Status

The Company operates as an approved investment trust within the meaning of Section 842 of the Income and Corporation Taxes Act 1988. Such approval is expected to be granted for the previous accounting year and the accounting year now under review. The Company is not a close company. The Company is an Investment Company within the meaning of Part VIII of the Companies Act 1985.

Going Concern

After making enquiries, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

Share Capital

During the year under review a total of 125,000 ordinary shares were repurchased and cancelled as part of the share buyback programme that was approved last year. The consideration paid, excluding buyback expenses, amounted to £462,000. After the year end the purchase of a further 50,000 shares was completed at a cost of £205,750.

Payment Policy

It is the Company's payment policy for the forthcoming financial year to obtain the best terms for all business and therefore there is no consistent policy as to the terms used. In general the Company agrees with its suppliers the terms on which business will take place and it is our policy to abide by these terms. The Company had no trade creditors at the year end.

Invested Funds

Sales of investments during the year resulted in net gains based on historical costs of £43,651,205 (2000 – £39,653,628). Provisions contained in the Finance Act 1980 exempt approved Investment Trusts from corporation tax on their chargeable gains. Invested funds at 31st January 2001 had a value of £591,210,681 before deducting net liabilities of £116,303,948 (2000 – £508,246,237 and £116,750,954).

Net Asset Value

The Net Asset Value of the Ordinary Shares of 25p at the year end, after deducting the provision for final dividend, was 463.5p as compared with a value of 381.4p at 31st January 2000.

Donations and Subscriptions

Aggregate charitable donations and subscriptions in respect of the year amounted to £Nil (2000 – £1,599). No political donations were made during the year.

Historical Record

There is included on page 9 a schedule of the Company's thirty largest holdings. The distribution of total assets is shown on page 14, and the historical record of the Company's revenue, capital and invested funds over the past ten years is shown on page 8. Graphs are included on page 15 showing the performance on a total return basis over the past ten years of the net asset value of the Company's Ordinary Shares against the Company's benchmark indices, the growth in net ordinary distributions made by the Company against the Retail Price Index, and the Company's discount to net asset value over the same period.

Directors' Report

Business Review

A review of the Company's activities is given in the Chairman's Statement on pages 6 and 7 and in the Investment Managers' Review on pages 10 and 11.

Revenue	**£**
Revenue for the year after deducting management and general expenses and finance costs of borrowings amounted to	16,941,922
Taxation	(184,352)
and there remained a balance of	16,757,570
from which has been deducted the dividend on £1,178,000 of Preference Stock	(42,997)
leaving available for distribution to the Ordinary Shareholders	16,714,573

Dividends

Provision has been made in the Accounts for dividends announced on the Ordinary Shares of 25p as follows:

	£	
1st Interim 4.10p per Share paid 24th August 2000	(4,195,486)	
2nd Interim 4.10p per Share paid 10th November 2000	(4,193,436)	
3rd Interim 4.10p per Share paid 16th February 2001	(4,190,362)	
Final 4.10p per Share proposed payable on 17th May 2001	(4,190,362)	
		(16,769,646)
leaving a deficit to be transferred to Revenue Reserve of		(55,073)

Subject to the final dividend being approved payment will be made on 17th May 2001 to shareholders on the Register of Members at the close of business on 20th April 2001 at the rate of 4.10p per Ordinary Share. Further details are provided in Note 6 on page 23.

Substantial Shareholdings

In accordance with Section 198 of the Companies Act 1985 and the Disclosure of Interests in Shares (Amendment) Regulations 1993, as at the date of this report, the Company has been advised of the following substantial share interests in its relevant share capital:

3.65% Cumulative Preference Stock:
The Prudential Corporation PLC—176,000 (14.9%); Ecclesiastical Insurance Office PLC—134,690 (11.4%); Zurich Financial Services Group—90,000 (7.6%); Royal Insurance PLC—60,000 (5.1%).

Ordinary Shares of 25p:
Barclays PLC and its subsidiaries—4,209,758 (4.1%).

Directors and Management

All Directors listed below served throughout the financial year under review except Mr C. H. Black who retired from the Board and as Chairman on 8th May 2000. Mr H. A. Stevenson was appointed Chairman on 8th May 2000.

Directors' Report

Mr A. D. A. W. Forbes, Mr P. J. Scott Plummer and Sir Bob Reid retire by rotation in accordance with the Articles of Association and, being eligible, offer themselves for re-election.

The present Board and their interests in the share capital of the Company as at 31st January 2001 and 2000 (or date of appointment if later) are listed below:

	Ordinary Shares of 25p			
	2001		2000	
	Beneficial	Non-Beneficial	Beneficial	Non-Beneficial
R. A. Barfield	1,872	—	400	—
Sir John Banham	800	—	800	—
A. D. A. W. Forbes	1,000	—	1,000	—
Sir Bob Reid	500	—	500	—
P. J. Scott Plummer	1,000	—	1,000	—
H. A. Stevenson	25,000	—	25,000	—

Between the end of the period under review and the date of this report Mr R. A. Barfield has acquired a further 14 ordinary shares of 25p each through the Dresdner RCM Investment Trust ISA bringing his total holding in the Trust to 1,886 shares.

No contracts of significance in which Directors are deemed to have been interested have subsisted during the year under review.

Management Agreement

The management agreement with Dresdner RCM Global Investors (UK) Limited provides for a fee of 0.35% per annum (2000—0.35%) of the value of the assets, calculated quarterly, after deduction of current liabilities, short term loans under one year and any funds within the portfolio managed by Dresdner RCM. The management agreement is terminable at one years' notice (2000—one year).

The Managers have discretion to exercise voting rights at the meetings of companies in which the Trust is invested, and will usually do so. However, in cases of takeover, merger or other offer involving a corporate client of the Managers or any of its associated companies the voting rights may only be exercised with the approval of at least one independent Director of the Trust. Similar approval must be sought in the case of any investment transactions in such companies or underwriting participations involving the securities of corporate clients of the Managers or any of its associated companies. The Managers do not have any discretion over any securities of Dresdner Bank Group or its subsidiaries that may be held by the Trust.

The Company has entered into an annual agreement with Dresdner RCM to operate the Savings Plan. The cost to the Company for the year ended 1st February 2002 will be £265,806 (excluding VAT) (2001—£257,423 excluding VAT). The fee relates to generic costs and is partially calculated on a usage and market capitalisation basis.

Individual Savings Accounts/PEPs

The affairs of the Company are conducted in such a way as to meet the requirement of a qualifying investment trust for Personal Equity Plans and the requirements for an Individual Savings Account and it is the intention to continue to do so.

Analysis of Share Register

	Shareholder Accounts				Ordinary Shareholding			
	Number		%		000's		%	
Shareholder Type	**2001**	**2000**	**2001**	**2000**	**2001**	**2000**	**2001**	**2000**
Private holders*	10,084	10,802	65.1	68.1	27,145	37,472	26.6	36.6
Nominees	4,476	3,993	28.9	25.2	64,387	53,654	63.0	52.4
Insurance Companies	57	67	0.4	0.4	2,266	2,265	2.2	2.2
Other holders	546	617	3.5	3.8	4,076	3,816	4.0	3.7
Pension Funds	8	7	0.1	0.1	74	59	0.1	0.1
Investment Trusts and Funds	312	378	2.0	2.4	4,208	5,063	4.1	5.0
	15,483	15,864	100.0	100.0	102,156	102,329	100.0	100.0

*Including PEP, ISA and Saving Plan Nominees.

Based on an analysis of the Ordinary Share register at 29th March 2001 (28th February 2000).

Directors' and Officers' Liability Insurance

The Company maintained Directors' and Officers' liability insurance during the year.

Purchase of own shares

As referred to in the Chairman's statement, the Board is proposing that the Company should be given renewed authority to purchase Ordinary Shares in the market for cancellation. The Board believes that such purchases in the market at appropriate times and prices would be a suitable method of enhancing shareholder value. The Company would make either a single purchase or a series of purchases, when market conditions are suitable, with the aim of maximising the benefits to shareholders and within guidelines set from time to time by the Board.

Where purchases are made at prices below the prevailing net asset value of the Ordinary Shares, this will enhance net asset value for the remaining shareholders. It is therefore intended that purchases would only be made at prices below net asset value, with the purchases to be funded from the realised capital profits of the Company (which are currently in excess of £395 million). The rules of the London Stock Exchange limit the price which may be paid by the Company to 105% of the average middle-market quotation for an Ordinary Share on the 5 business days immediately preceding the date of the relevant purchase. The minimum price to be paid will be 25p per Ordinary Share (being the nominal value). Additionally, the Board believes that the Company's continued ability to purchase its own shares should create additional demand for the Ordinary Shares in the market and that this increase in liquidity should assist shareholders wishing to sell their Ordinary Shares.

The Board considers that it will be most advantageous to shareholders for the Company to be able to make such purchases as and when it considers the timing to be most favourable and therefore does not propose to set a timetable for making any such purchases.

Directors' Report

Under the rules of the London Stock Exchange, the maximum number of shares which a listed company may purchase through the market pursuant to a general authority such as this is equivalent to 14.99% of its issued share capital. For this reason, the Company is limiting its renewed authority to make such purchases to 15,312,875 Ordinary Shares, representing 14.99% of the issued share capital at the date of this document. The authority will last until the Annual General Meeting of the Company to be held in 2001 or the expiry of 18 months from the date of the passing of this resolution, whichever is the earlier. The authority will be subject to renewal by shareholders at subsequent Annual General Meetings.

Allotment of new shares

Approval is sought for the renewal of the Directors authority to allot relevant securities, in accordance with Section 80 of the Companies Act 1985, up to a maximum aggregate nominal amount of £1,319,328. This authority would expire 5 years from the date of renewal, if not previously revoked or varied.

A Resolution was passed at the Annual General Meeting held on 8th May 2000 to authorise the Directors to allot the unissued share capital for cash. The power to allot new shares for cash other than pro rata to existing shareholders, limited to the aggregate nominal amount of £1,274,703 Ordinary capital, being approximately 4.99 per cent of the issued Ordinary Share capital of the Company as at the date of this report, is renewable annually and expires at the conclusion of the Annual General Meeting in 2001. A Special Resolution is therefore proposed under special business at the forthcoming Annual General Meeting to renew this authority for a further year.

Whilst it is anticipated that allotments under this authority will normally be to the Dresdner RCM Investment Trusts Savings Plan the resolution allows for allotments of new shares at the discretion of the Directors and is not limited only to this Plan. The Directors confirm that no allotment of new shares will be made unless the lowest market offer price of the Ordinary Shares is at least at a premium to net asset value.

Auditors

PricewaterhouseCoopers have indicated their willingness to continue in office and resolutions concerning their re-appointment and authorising the Directors to determine their remuneration will be proposed at the forthcoming Annual General Meeting.

By Order of the Board
Kirsten Salt
Deputy Secretary

5th April 2001

Notice of Meeting

Notice is hereby given that the Annual General Meeting of **The Merchants Trust PLC** will be held at **20 Fenchurch Street, London EC3P 3DB**, on Monday, 14th May 2001 at 12.30 p.m. to transact the following business:

Routine Business

1 To receive and adopt the Report of the Directors and the Accounts for the year ended 31st January 2001 together with the Auditors' Report thereon.

2 To declare a final ordinary dividend of 4.10p per Ordinary Share.

3 To re-elect Mr. A. D. A. W. Forbes as a Director.

4 To re-elect Mr. P. J. Scott Plummer as a Director.

5 To re-elect Sir Bob Reid as a Director.

6 To re-appoint PricewaterhouseCoopers as Auditors of the Company.

7 To authorise the Directors to determine the remuneration of the Auditors.

Special Business

Resolution 9 will be proposed as an Ordinary Resolution and resolutions 8 and 10 as Special Resolutions:

8 THAT the Company be and is hereby generally and 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 Ordinary Shares of 25p each in the capital of the Company ("Ordinary Shares"), provided that:

(i) the maximum number of Ordinary Shares hereby authorised to be purchased shall be 15,312,875;

(ii) the minimum price which may be paid for an Ordinary Share is 25p;

(iii) the maximum price which may be paid for an Ordinary Share is an amount equal to 105 per cent of the average of the middle market quotations for an Ordinary Share taken from the London Stock Exchange Official List for the 5 business days immediately preceding the day on which the Ordinary Share is purchased or such other amount as may be specified by the London Stock Exchange from time to time;

(iv) the authority hereby conferred shall expire at the conclusion of the annual general meeting of the Company in 2002 or, if earlier, on the expiry of 18 months from the passing of this resolution, unless such authority is renewed prior to such time; and

(v) the Company may make a contract to purchase Ordinary Shares under the authority hereby conferred prior to the expiry of such authority which will or may be executed wholly or partly after the expiration of such authority and may make a purchase of Ordinary Shares pursuant to any such contract.

Notice of Meeting

9 THAT for the purposes of Section 80 of the Companies Act 1985 the Directors be generally and unconditionally authorised to exercise all the powers of the Company to allot relevant securities (within the meaning of the said section) up to an aggregate nominal amount of £1,319,328 provided that:

(i) the authority granted shall expire five years from the date upon which this Resolution is passed but may be revoked or varied by the Company in General Meeting and may be renewed by the Company in General Meeting for a further period not exceeding five years; and

(ii) the said authority shall allow and enable the Directors to make an offer or agreement before the expiry of that authority which would or might require relevant securities to be allotted after such expiry and the Directors may allot relevant securities in pursuance of any such offer or agreement as if that authority had not expired.

10 THAT the Directors be empowered in accordance with Section 95 of the Companies Act 1985 to allot equity securities (within the meaning of Section 94 of that Act) for cash as if sub-section (1) of Section 89 of the Act did not apply to any such allotment provided that:

(i) the power granted shall be limited to the allotment of equity securities wholly for cash up to an aggregate nominal amount of £1,274,703 (being within 5 per cent of the issued Ordinary Share capital at the date of this Notice).

(ii) the power granted shall (unless previously revoked or renewed) expire at the conclusion of the next Annual General Meeting of the Company after the passing of this resolution; and

(iii) the said power shall allow and enable the Directors to make an offer or agreement before the expiry of that power which would or might require equity securities to be allotted after such expiry and the Directors may allot equity securities in pursuant of such offer or agreement as if that power had not expired.

10 Fenchurch Street,
London EC3M 3LB
5th April 2001

By Order of the Board
Kirsten Salt
Deputy Secretary

Notes: Members entitled to attend and vote at this Meeting may appoint one or more proxies to attend and, on a poll, vote in their stead. The proxy need not be a Member of the Company. Duly completed forms of proxy must reach the office of the Registrars at least 48 hours before the Meeting. A form of proxy is provided with the Annual Report. Completion of the enclosed form of proxy does not preclude a Member from attending the Meeting and voting in person.

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 at 12.30 pm on 12th May 2001 ("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 at the time which is 48 hours before the time fixed for the adjourned Meeting or, if the Company gives notice of the adjourned Meeting, at the time specified in that notice.

Contracts of service are not entered into with the Directors, who hold office in accordance with the Articles of Association.

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Form of Proxy

THE MERCHANTS TRUST PLC
FORM OF PROXY
FOR ANNUAL GENERAL MEETING

Notes on how to complete the proxy form

If you are a registered Shareholder and you are unable to attend the Meeting you may appoint a proxy to attend and, on a poll, to vote on your behalf.

A Appointing a proxy

If you wish to appoint someone other than the Chairman as your proxy please cross out the words "the Chairman of the Meeting", initial the deletion, and insert the name and address of your proxy. A proxy need not be a member of the Company, but must attend the Meeting in order to represent you.

B Telling your proxy how to vote

Tick the appropriate box indicating how your proxy should vote on the Resolutions. If you do not give instructions, your proxy will vote or abstain at his discretion.

C How to sign the form

(i) Please print your name and address in the space provided and sign and date the form.

(ii) If someone else signs the form on your behalf, the authority entitling them to do so, or a certified copy of it, must accompany the form.

(iii) In the case of a corporation, this form must be executed either under its common seal or be signed on its behalf by an attorney or duly authorised officer of the corporation.

(iv) In the case of joint holders, the signature of the first-named on the Register of Members, in respect of the joint holding, shall be accepted to the exclusion of the other joint holders.

Returning the form

The form must reach the office of the Registrars of the Company no later than 48 hours before the time of the Meeting. If you are a registered Shareholder and you subsequently decide to attend the Meeting you may do so.

Appointment of Proxy

A I/We, the undersigned, being (a) member(s) of the above-named Company hereby appoint the Chairman of the Meeting or

SURNAME MR/MRS/MISS/TITLE

FORENAMES

ADDRESS

POSTCODE

as my/our proxy to attend and vote for me/us and on my/our behalf as directed below at the Annual General Meeting of the Company to be held on Monday 14th May 2001 at 12.30 pm and at any adjournment thereof.

	B Routine Business	For	Against
1	To receive the Report and Accounts	☐	☐
2	To declare a final dividend of 4.10p	☐	☐
3	To re-elect Mr. A. D. A. W. Forbes as a Director	☐	☐
4	To re-elect Mr. P. J. Scott Plummer as a Director	☐	☐
5	To re-elect Sir Bob Reid as a Director	☐	☐
6	To re-appoint PricewaterhouseCoopers as Auditors	☐	☐
7	To authorise the Directors to determine the remuneration of the Auditors	☐	☐
	Special Business		
8	To authorise the Company to make market purchases of its own shares	☐	☐
9	To renew the Directors' authority to allot shares	☐	☐
10	To renew the Directors' authority to allot shares for cash	☐	☐

C Shareholders Details

SURNAME MR/MRS/MISS/TITLE

FORENAMES

ADDRESS

POSTCODE

SIGNATURE DATE

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BUSINESS REPLY SERVICE
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Capita IRG plc
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Second Fold