Allianz Dresdner Asset Management

THE MERCHANTS TRUST PLC

Report and Accounts for the year ended 31st January 2003

Report

Contents

Key Facts

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 Company'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 Company's higher yield objective.

Financial Highlights for the years ended 31st January

Revenue	2003	2002	% change
Revenue	£22,100,765	£21,595,671	+2.3
Available for Ordinary Dividend	£17,626,161	£17,051,644	+3.4
Earnings per Ordinary Share	17.26p	16.70p	+3.4
Dividends per Ordinary Share	17.20p	16.80p	+2.4

Key Data as at 31st January	2003	2002	% change
Total Net Assets	£274,585,271	£422,160,624	−35.0
Net Asset Value per Ordinary Share	267.8p	412.3p	−35.0
Ordinary Share Price	256.0p	392.0p	−34.7
Discount of Net Asset Value to Ordinary Share Price	4.4%	4.9%	n/a

Investor Information

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

Ordinary Dividends
First quarterly paid August
Second quarterly paid November
Third quarterly paid February
Final paid May

Preference Dividends
Payable half-yearly 1st August and 1st February

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 by the London Stock Exchange. The geographical spread of investments and ten largest holdings are also published monthly by the London Stock Exchange. They are also available to any enquirer from Allianz Dresdner Asset Management Investor Services on 020 7475 6151 or the Allianz Dresdner Asset Management website: www.allianzdresdneram.co.uk.

Share Prices

The share prices quoted in The London Stock Exchange Daily Official List for 31st January 2003 were 251p-261p.
For CGT indexation purposes at 31st March 1982 the share price, after adjustment for bonus issues, was 48.75p.

Savings Scheme

The Allianz Dresdner Asset Management Investment Trust Savings Scheme 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 & PEP Transfer

Shareholders can invest in the shares of the Company through the Allianz Dresdner Investment Trust ISA. Full details are available from Allianz Dresdner Asset Management Investor Services on 020 7475 6151.

Website

Further information about the Company is available on the Allianz Dresdner Asset Management website www.allianzdresdneram.co.uk.

Allianz Dresdner Asset Management

In January 2003 the Managers changed their name from Dresdner RCM Global Investors (UK) Ltd. to Allianz Dresdner Asset Management (UK) Limited.

Allianz Dresdner Asset Management Group is one of the largest fund managers in Europe. As at 31st December 2002, the Allianz Dresdner Asset Management Group had combined assets of £647 billion under management.

Allianz Dresdner Asset Management, through its predecessors, has a heritage of investment trust management expertise in the UK stretching back to the nineteenth century and had £1.07 billion assets under management in a range of investment trusts as at 31st December 2002.

Investor Information

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 Registrars. Dividends mandated in this way are paid via BACS (Bankers' Automated Clearing Service). 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

Contact Details

Shareholders' Enquiries

Capita Registrars 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 0870 1623100 or, if telephoning from overseas, 0044 20 8639 2157. 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 ASIP ACIS
Director UK Equities, Allianz Dresdner Asset Management (UK) Ltd.

Secretary and Registered Office
Kirsten Salt BA (Hons) ACIS
10 Fenchurch Street, London EC3M 3LB
Telephone: 020 7475 5808
E mail: kirsten.salt@allianzdresdneram.co.uk.

Registered Number 28276

Registrars and Transfer Office
Capita Registrars
The Registry
34 Beckenham Road
Beckenham, Kent BR3 4TU
Telephone: 0870 1623100 or, if telephoning from overseas, 0044 20 8639 2157
E mail: ssd@capitaregistrars.com

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

Bankers
HSBC Bank PLC
Barclays Bank plc

Stockbroker
Cazenove & Co. Ltd

Allianz Dresdner Asset Management Investor Services
020 7475 6151

Allianz Dresdner website
www.allianzdresdneram.co.uk

Chairman's Statement

Results

The year ended 31st January 2003 was marked by extraordinarily heavy falls in world stock markets. During the year the FTSE 100 Index - the principal benchmark for the Trust - fell by 30.9% and the Trust's other benchmark - the FTSE Higher Yield Index - fell by 28.7%. By comparison the Trust's portfolio - before the impact of gearing and costs - fell in value by 26.2%.

The investment objective of the Trust has been, and remains, to provide an above average level of income and income growth together with long term growth of capital through a policy of investing money in higher yielding UK FTSE 100 companies.

At 8th April 2003, the net yield on the Trust's shares was 6.5%, compared with the net yield of 3.6% on the FTSE 100 Index at that date. This policy has shielded the Trust from the worst effects of the almost unprecedented decline in markets during the past three years. Over the last three financial years ending 31st January, the Trust's portfolio of Total Assets Less Current Liabilities (i.e., before the impact of long-term gearing) fell by 23.2%. The Trust's net asset value fell by 29.8%. By comparison the FTSE 100 Index fell by 43.1%. Secondly, notwithstanding the decline in capital values in the past year, the portfolio produced a further small increase in earnings per share, sufficient to cover the increased dividend recommended by the Board.

Return on Shareholders' Funds

The net asset value per share fell by 35.0% over the year from 412.3p to 267.8p. After taking credit for the Trust's revenues, there was a negative total return on shareholders' funds of 30.9% The share price fell by 34.7% from 392p to 256p.

Earnings per share

Net earnings per share rose by 3.4% from 16.70p to 17.26p. The total for 2002/3 includes special dividend receipts equivalent to 0.59p per share, which compares with 0.21p per share from this source in 2001/2. On an underlying basis, earnings per share rose by 1.1%. This represents a resilient performance at a time when a number of company dividend payments have been cut.

Dividends

The Board is recommending a final dividend of 4.3p per share giving a total of 17.2p for the full year, an increase of 2.4%. This continues the policy of increasing payments broadly in line with the retail prices index. The proposed total, costing £17.6m, allows for a small transfer to the Trust's revenue reserve. This reserve, which can be used to support future distributions, now stands at approximately £10.2m, or 59% of last year's total dividends. The Trust has recorded 21 years of consecutive dividend increases.

Gearing

As shareholders will know, it has been the Trust's policy for many years to seek to augment the investment returns accruing to investors through the use of long term borrowings. Given the historic returns achieved by equity markets, this approach has been a key distinguishing feature and attraction of investment trusts in general. In falling markets, however, the Trust's gearing has the opposite effect.

Following the sharp deterioration in stock markets the Company's borrowings have risen as a proportion of shareholders' funds and the net asset value per share has consequently become more volatile, when compared with movements in the stock market. In considering the capital structure of the Company, the Board has had regard both to the cost of redeeming the Trust's outstanding borrowings and to the principal investment objective of the Trust - income growth. With dividend yields from many blue chip companies now exceeding the return from bank deposits and from gilts, the Board does not at present believe that it would be in shareholders' best interests to reduce income by selling equities in order to offset debt with holdings of cash or gilts. If, however, the Board was concerned that the general level of dividends from the UK equity market was about to suffer a significant setback or if gearing was to rise to a level which the Board regarded as no longer prudent, the investment strategy of the Trust would be reviewed.

Repurchase of Shares

During the last financial year the shares of the Trust have traded at a relatively small discount, and at times at a small premium, to net asset value. During the year the Trust did not add to the total number of shares previously re-purchased and cancelled. Thus the total number of shares re-purchased remains at 225,000. As in previous years the Board is proposing to renew this authority at the forthcoming AGM on 12th May 2003.

Prospects

In assessing the outlook for the current financial year it is striking that there are still a large number of issues, both political and economic, which could continue to depress market sentiment. Moreover US equities continue to be relatively

Chairman's Statement

highly rated and this fact may well constrain progress for equities elsewhere in the developed world. However, after three years of falling markets, UK equities are once again attractive by reference to a number of historic yardsticks. There is now a much broader investor interest in dividend income, and as a consequence, in the higher yielding companies in which the Trust is invested.

Hugh Stevenson
Chairman
9th April 2003

Historical Record

Years ended 31st January

Revenue and Capital

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Revenue (£000s)	15,514◊	17,466◊	17,351◊	18,769◊	20,399◊	20,119◊	22,590	21,546	21,596	22,101
Earnings per share (net)	11.04p	12.12p	12.41p	13.66p	14.88p	15.21p	17.93p	16.35p	16.70p	17.26p
Paid net per Share	11.00p	11.50p	12.25p	13.65pØ	14.25p	15.59p‡	16.00p	16.40p	16.80p	17.20p
Tax Credit per Share	2.75p	2.88p	3.06p	3.41p#	3.56p	3.90p§	1.78p	1.82p	1.87p	1.91p
Gross Ordinary Dividend	13.75p	14.38p	15.31p	17.06p	17.81p	19.49p	17.78p	18.22p	18.67p	19.11p
Total Net Assets (£000s)	311,127	253,604	303,934	335,212	421,504	426,037	391,495	474,907	422,161	274,585
Net Assets attributable to										
Ordinary Capital (£000s)	309,909	252,426	302,756	334,034◊	420.326	424,859	390,317	473,729	420,983	273,407
Net Asset Value per Ordinary Share	302.9p	246.7p	295,9p◊	326.4p	410.8p	415.2p	381.4p	463.5p	412.3p	267.8p
NAV Total Return (%)*	+33.2	-14.8	+24.9	+14.9p	+30.2	+4.9	-4.3	+25.8	-7.4	-30.9
Retail Price Index Increases (%)6	+2.8	+2.8	+2.8	+3.1	+2.5	+2.6	+2.1	+1.8	+2.6	+2.7

Notes

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

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 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.

6 RPIX - excludes the effect of mortgage rates.

* 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.

Thirty Largest Holdings
at 31st January 2003

	Valuation		Unrealised Gain (Loss) Over Book Cost
	£'000s	%	£'000s
BP	34,571	8.83	(9,072)
HSBC	30,919	7.89	(9,594)
GlaxoSmithKline	22,079	5.64	(5,566)
Shell Transport & Trading	20,590	5.26	(2,782)
Barclays	10,508	2.68	(5,903)
Gallaher	10,248	2.62	3,042
Imperial Tobacco	10,219	2.61	4,817
BT	10,150	2.59	(12,176)
Lloyds TSB	9,665	2.47	(6,004)
Severn Trent	9,460	2.42	(279)
Royal Bank of Scotland	9,373	2.39	2,471
Alliance & Leicester	8,370	2.14	1,849
HBOS	7,080	1.81	(1,398)
Boots	6,786	1.73	(1,631)
Rank	6,334	1.62	436
Land Securities	6,303	1.61	(687)
Abbey National	6,030	1.54	(9,072)
Bradford & Bingley	5,988	1.53	(652)
BPB	5,963	1.52	210
Next	5,928	1.51	(1,461)
Scottish Power	5,876	1.50	(2,563)
Vodafone	5,668	1.45	(10,189)
Wilson Connolly	5,547	1.42	(1,081)
United Utilities	5,343	1.36	(1,438)
Scottish & Southern Energy	5,342	1.36	(237)
Prudential	5,197	1.33	(1,678)
Sainsbury (J)	5,176	1.32	(2,487)
Pennon	4,928	1.26	(575)
Safeway	4,865	1.24	22
Legal & General	4,741	1.21	(4,052)
	289,247	73.86	% of Total Invested Funds

Investment Managers' Review

Economic Background

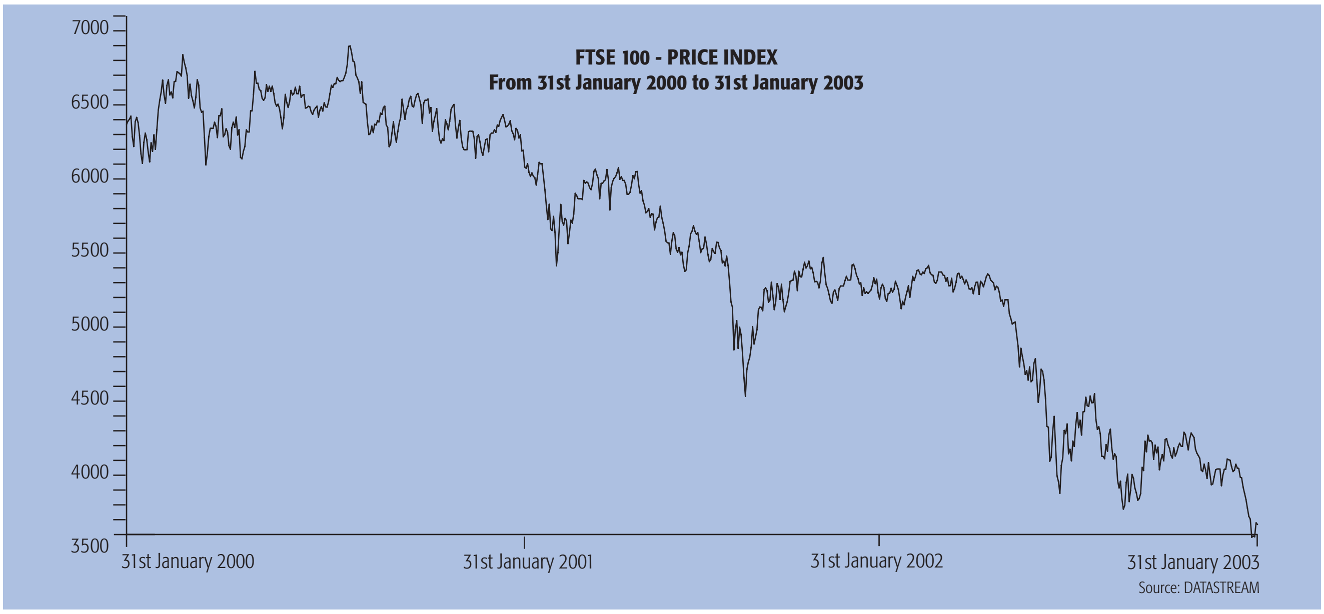
In the last twelve months the UK economy has produced steady growth in the order of 2%, which was broadly in line with the rate recorded in 2001. In the event the consumer element has been rather more buoyant than expected, rising by about 3.5%, whilst the manufacturing component has been weak, falling by a similar proportion. Overseas economies were, in the main, unhelpful. The US recorded a useful recovery with 2.5% growth, prompted by the aggressive easing of monetary policy by the "Fed", but Europe's and Japan's economies remained becalmed. The Monetary Policy Committee kept UK base rates unchanged at 4%, despite buoyant consumer demand and large increases in Government spending. Consequently consumer confidence was sustained by continued low unemployment over the course of 2002.

These trends have been reflected in the quoted sector's profits, where progress has been hampered by a lack of pricing power in a wide range of business sectors. To combat this, it has been noticeable that many western manufacturing companies have been out-sourcing their production to low cost countries in Eastern Europe and the Far East. For companies in general, proximity to the consumer has led to more stable profitability and also to more resilient share price performances. Currency trends have had a somewhat surprising impact on markets, with the dollar falling by over 12% against sterling, whilst in contrast the euro rose by about 8%.

Market Trends

As the graph of the FTSE 100 Index for the last three years shows, the market experienced two significant periods of weakness in the last financial year. After a steady performance up to the end of April 2002, the index fell sharply through to the middle of July. The fall was led by Wall Street where fears over slower growth rates were compounded by corporate governance and accounting concerns. Having formed a base at about 3800 for the FTSE 100 Index in July and September, the market hovered around the 4000 level until the end of 2002. In the last month of the financial year the market fell sharply again as fears over conflict in the Middle East eroded sentiment once again.

On a sector basis, Tobacco (+9.5%), Food Producers (-9.5%) and Utilities (-13.4%) were amongst the leading sectors over the year to January 2003, whilst Information Technology (-67.1%), Life Assurance (-46.8%) and Pharmaceuticals (-33.9%) were some of the weaker performers. For the leaders, it is notable that all the above three sectors have predictable sales and cash flow characteristics and, as a consequence, they have been key features of the portfolio in the recent past. In contrast the portfolio has had low weightings in the latter group of companies, with the exception of life assurance.



Investment Managers' Review

Portfolio Changes

As we reported in the 2002 Annual Report, the investment policy was essentially a cautious one at the start of the last financial year. Nevertheless it was essential, in adverse circumstances, to try to identify any holdings where investors' expectations might not be fulfilled. Simultaneously we reduced the number of holdings in the portfolio, reflecting greater concentration on those companies where the business prospects were the most secure. In this light we sold Airtours (now MyTravel), EMI, Morgan Crucible and Schroders. Amongst blue chips, we disposed of the holdings in AstraZeneca and GUS where the valuation appeared to have moved ahead of the companies' prospects. In the leisure sector, we made partial disposals of Hilton and Allied Domecq, with the latter change representing a switch into a new holding, Diageo. On a positive note, the bid for Lattice led to its shares being exchanged for those in National Grid, whilst the multiple bids for Safeway precipitated a partial sale of a large holding towards the end of the year.

Reflecting the earlier comments on the reduction in the number of investments, several of the share purchases in the last year involved existing holdings. In this category we added to the Trust's holdings in BP, GlaxoSmithKline and HSBC, all of which suffered relative share price weakness during the year. In particular BP, currently the largest quoted UK company, had been a major underweight position in the portfolio and share price weakness, following its failure to achieve its stated production growth objective, afforded a good buying opportunity against the background of a rising crude oil price. Elsewhere we added to the holdings in Pennon, Scottish & Southern Energy, Scottish Power and Severn Trent in the utilities sector. Furthermore we made purchases of Provident Financial, the consumer lending group, as well as investing in William Hill, the gaming group, following its flotation. Lastly we subscribed to the rights issues from Kingfisher and Legal & General.

Future Policy

Following the fall in the value of UK quoted companies, there now appear to be a large number of established UK companies on undemanding share ratings. At present a high quality portfolio can be assembled giving a significantly higher yield than gilt-edged securities. Such low valuations have been reflected in a number of "public to private" take-over bids for companies, such as Safeway and Six Continents, where a large proportion of the funding would have been arranged through the debt markets. It is to be hoped that this recognition of value will help to provide a base for the market as a whole.

The recent trends in share price volatility are expected to continue for the foreseeable future, prompted by the many uncertainties still besetting the economic and political scene on a global basis. From a longer-term viewpoint this is expected to provide many good opportunities to invest in high quality companies with stable and growing dividends.

Performance Attribution Analysis

for the year ended 31st January 2003

	%
Capital return of FTSE 100 Index	(30.9)
Relative return from Portfolio	4.7
Change in total assets	(26.2)
Impact of gearing on Portfolio	(7.1)
Expenses charged to capital	(1.7)
Change in Net Asset Value per Ordinary Share	(35.0)

United Kingdom Listed Holdings
at 31st January 2003

	Value (£)	Principal Activities
BP	34,571,000	Oil production and refining
HSBC	30,919,000	Banking
GlaxoSmithKline	22,079,200	Pharmaceuticals
Shell Transport & Trading	20,590,200	Oil production and refining
Barclays	10,507,500	Banking
Gallaher	10,248,000	Tobacco
Imperial Tobacco	10,219,000	Tobacco
BT	10,149,750	Telecommunications
Lloyds TSB	9,664,500	Banking
Severn Trent	9,460,000	Water
Royal Bank of Scotland	9,373,000	Banking
Alliance & Leicester	8,370,000	Banking
HBOS	7,080,350	Banking
Boots	6,786,000	Retailing
Rank	6,333,500	Leisure and gaming
Land Securities	6,303,150	Real estate
Abbey National	6,030,000	Banking
Bradford & Bingley	5,987,769	Banking
BPB	5,962,880	Building materials
Next	5,928,000	Retailing
Scottish Power	5,875,625	Electricity
Vodafone	5,668,000	Telecommunications
Wilson Connolly	5,546,642	Housebuilding
United Utilities	5,342,850	Water
Scottish & Southern Energy	5,341,600	Electricity
Prudential	5,197,238	Life and general insurance
Sainsbury (J)	5,175,500	Food retailing
Pennon	4,927,563	Water
Safeway	4,865,400	Food retailing
Legal & General	4,740,750	Life and general insurance
Tomkins	4,723,875	Engineering
Scottish & Newcastle	4,521,000	Beverages
Standard Chartered	4,449,120	Banking
Northern Foods	4,250,000	Food production

United Kingdom Listed Holdings

at 31st January 2003

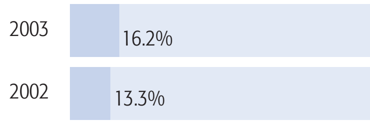
	Value (£)	Principal Activities
Aviva	4,143,513	Life assurance
Diageo	4,098,600	Beverages
Provident Financial	3,993,300	Speciality finance
Tate & Lyle	3,962,000	Food production
Slough Estates	3,955,682	Real estate
BAA	3,951,200	Transport
BOC	3,937,500	Chemicals
Allied Domecq	3,796,800	Beverages
Lonmin	3,724,000	Mining
Persimmon	3,651,014	Housebuilding
Rio Tinto	3,558,400	Mining
Woolworths	3,554,375	Retailing
Rexam	3,514,875	Packaging
Hanson	2,620,000	Building materials
BBA	2,592,500	Engineering
Wimpey (George)	2,470,000	Housebuilding
Close Bros	2,386,125	Speciality finance
Six Continents	2,375,900	Leisure and hotels
Johnson Matthey	2,263,257	Chemicals
FKI	2,182,500	Engineering
Associated British Ports	2,179,250	Transport
William Hill	2,060,000	Gaming
Smith (DS)	2,032,000	Paper
Royal & Sun Alliance	2,026,500	General Insurance
P & O	2,025,000	Transport
Dixons	2,023,700	Retailing
Hilton	1,860,000	Gaming and hotels
Exel	1,768,500	Transport
Pearson	1,766,375	Publishing
	391,660,828	

Distribution of Total Assets
at 31st January 2003

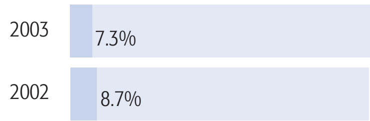
Total Assets (less creditors falling due within one year) £386,683,879 (2002 - £534,248,098)

	Percentage of Total Assets 2003	Percentage of Total Assets 2002
Equities (including convertibles)		
Resources		
Mining	1.9	3.2
Oil and gas	14.3	10.1
	16.2	13.3
Basic Industries		
Chemicals	1.6	1.8
Construction & building materials	5.2	6.9
Steel and & other metals	0.5	0.0
	7.3	8.7
General Industrials		
Engineering & machinery	1.8	3.3
	1.8	3.3
Non-Cyclical Consumer Goods		
Beverages	2.0	1.3
Food products & process	2.1	2.2
Pharmaceuticals	5.7	6.4
Tobacco	5.3	3.5
	15.1	13.4
Cyclical Services		
General retailers	4.7	4.4
Leisure, entertainment & hotels	4.4	6.7
Media & photography	0.5	1.4
Support services	0.9	0.8
Transport	3.2	2.7
	13.7	16.0
Non-Cyclical Services		
Food & drug retail	2.6	2.6
Telecommunication services	4.1	3.9
	6.7	6.5
Utilities		
Electricity	2.9	2.3
Gas distribution	0.0	1.3
Water	5.1	2.7
	8.0	6.3

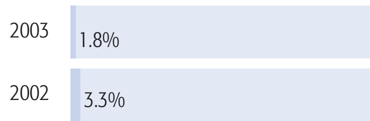
Resources



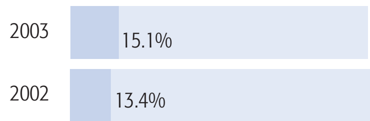
Basic Industries



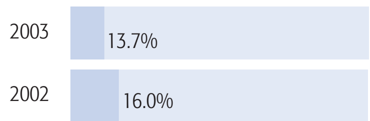
General Industrials



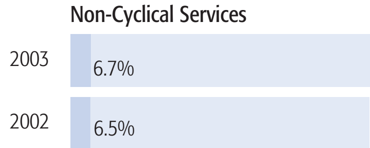
Non-Cyclical Consumer Goods



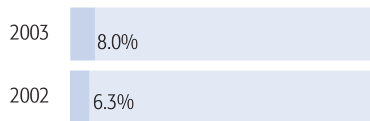
Cyclical Services



Non-Cyclical Services



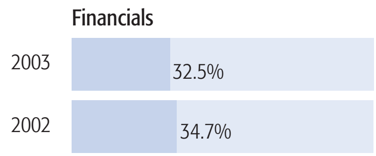
Utilities

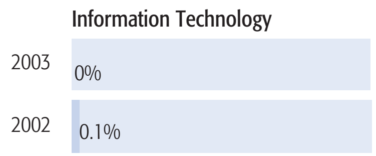


Distribution of Total Assets

at 31st January 2003

	Percentage of Total Assets 2003	2002
Financials		
Banks	24.0	23.1
Insurance	0.5	1.3
Life assurance	3.6	5.6
Investment companies	0.0	0.9
Real estate	2.7	1.9
Speciality & other financials	1.7	1.9
	32.5	34.7
Information Technology		
Information technology hardware	0.0	0.1
	0.0	0.1
Total Equities	101.3	102.3
Net Current Liabilities	(1.3)	(2.3)
Total Assets	100.0	100.0

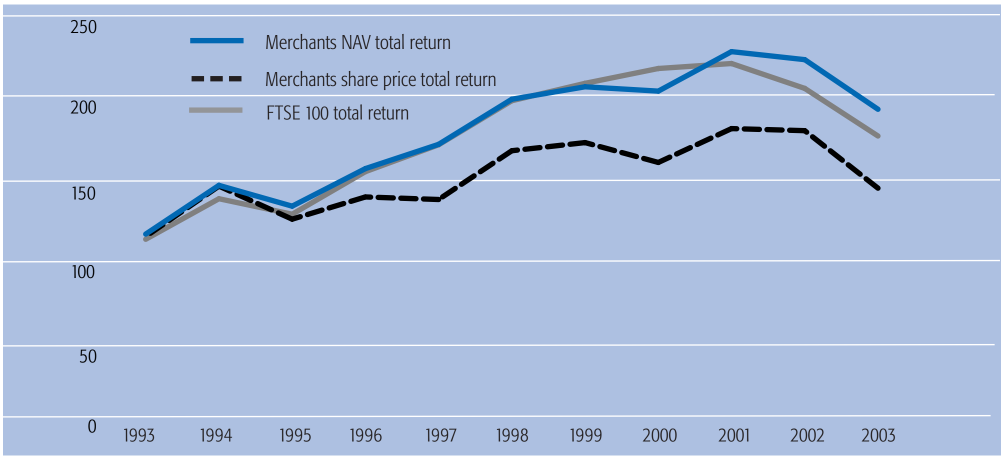




Performance Graphs

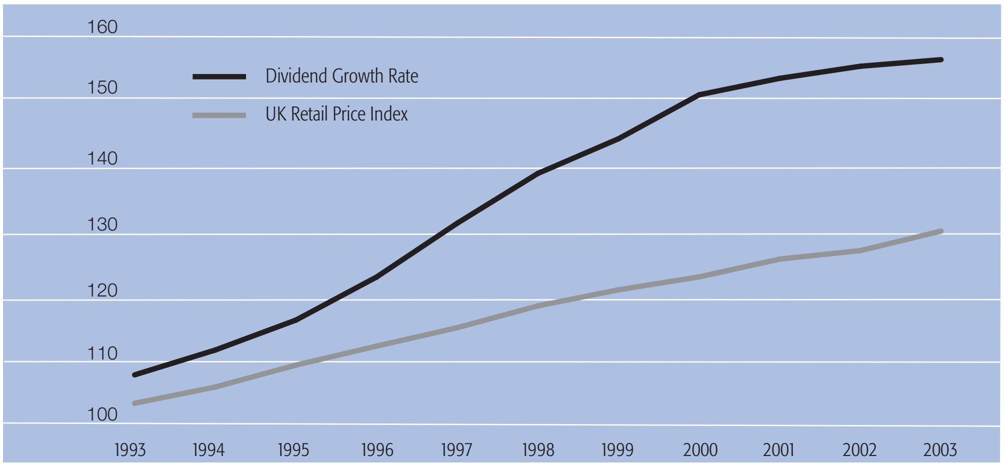
10 year record-as at 31st January

Merchants Total Return compared to FTSE 100 Total Return



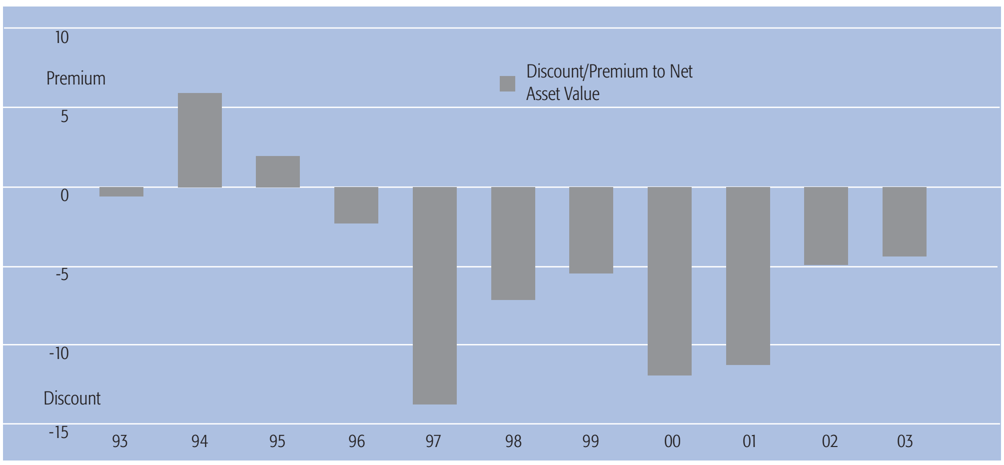
(Rebased to 100, net income reinvested) Source: Datastream

Merchants Net Dividend Growth compared to inflation*



*excluding FID enhancement (see page 8 for details)
(Rebased to 100) Source: Allianz Dresdner Asset Management/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.

This information is given so that investors in the Company can decide for themselves whether their investment is high or low risk. It allows them to assess what kind of impact the use of financial instruments (investments, cash/overdraft and borrowings) will have on the performance of the entity. Short term debtors and creditors are not considered to be financial instruments. They have been included at the bottom of the numerical disclosure in Note 20(a) merely to enable users of the accounts to reconcile the summary provided to total net assets per the balance sheet.

The narrative below explains the different types of risks the Company may face. 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 risk profile and the policies adopted to manage risk did not change materially during either the current or previous period.

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 can be achieved through the use of overdraft facilities, where necessary.

Interest rate risk

The Company invests predominantly in equities, the values of which are not directly affected by changes in prevailing market interest rates. Therefore there is minimal exposure to interest rate risk.

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

In February 2000 the Company 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 and FTSE 100 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 2003

	Note	2003 £ Revenue	2003 £ Capital	2003 £ Total	2002 £ Revenue	2002 £ Capital	2002 £ Total
Net losses on investments	8	–	(140,362,992)	(140,362,992)	–	(45,049,190)	(45,049,190)
Exchange rate differences		–	–	–	–	(47,836)	(47,836)
Income	1	22,100,765	–	22,100,765	21,595,671	–	21,595,671
Investment management fee	2	(684,279)	(1,270,805)	(1,955,084)	(805,463)	(1,495,860)	(2,301,323)
Expenses of administration	3	(507,788)	–	(507,788)	(588,430)	–	(588,430)
Net return before finance costs and taxation		20,908,698	(141,633,797)	(120,725,099)	20,201,778	(46,592,886)	(26,391,108)
Finance costs of borrowings	4	(3,239,540)	(6,005,840)	(9,245,380)	(3,068,058)	(5,682,815)	(8,750,873)
Return on ordinary activities before taxation		17,669,158	(147,639,637)	(129,970,479)	17,133,720	(52,275,701)	(35,141,981)
Taxation	5	–	–	–	(39,079)	39,079	–
Return on ordinary activities after taxation for the financial year		17,669,158	(147,639,637)	(129,970,479)	17,094,641	(52,236,622)	(35,141,981)
Dividends on Preference Stock		(42,997)	–	(42,997)	(42,997)	–	(42,997)
Return attributable to Ordinary Shareholders		17,626,161	(147,639,637)	(130,013,476)	17,051,644	(52,236,622)	(35,184,978)
Dividends on Ordinary Shares	6	(17,561,877)	–	(17,561,877)	(17,155,611)	–	(17,155,611)
Transfer to (from) reserves		64,284	(147,639,637)	(147,575,353)	(103,967)	(52,236,622)	(52,340,589)
Return per Ordinary Share	7	17.26p	(144.60)p	(127.34)p	16.70p	(51.15)p	(34.45)p
Net Asset Value	15						
Per Ordinary Share				267.8p			412.3p
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 33 form part of these Accounts.

Balance Sheet
at 31st January 2003

	Note	2003 £	2003 £	2002 £
Fixed Assets				
Investments	8		391,703,740	546,771,665
Current Assets				
Debtors	10	2,351,290		2,628,868
Cash at bank	10	3,866,703		–
		6,217,993		2,628,868
Creditors: Amounts falling due within one year	10	(11,237,854)		(15,152,435)
Net Current Liabilities			(5,019,861)	(12,523,567)
Total Assets less Current Liabilities			386,683,879	534,248,098
Creditors: Amounts falling due after more than one year	10		(112,098,608)	(112,087,474)
Total Net Assets			274,585,271	422,160,624
Capital and Reserves				
Called up Share Capital: Ordinary	11	25,525,984		25,525,984
Preference	11	1,178,000		1,178,000
			26,703,984	26,703,984
Capital Redemption Reserve	12		56,250	56,250
Share Premium Account			39,809	39,809
Capital Reserves: Realised	13	353,215,764		385,653,373
Unrealised	13	(115,624,254)		(422,226)
			237,591,510	385,231,147
Revenue Reserve	14		10,193,718	10,129,434
Shareholders' Funds	16		274,585,271	422,160,624
Analysis of Shareholders' Funds				
Equity interests	15		273,407,271	420,982,624
Non-equity interests	15		1,178,000	1,178,000
			274,585,271	422,160,624

Approved by the Board of Directors on 9th April 2003 and signed on its behalf by:

Hugh Stevenson

Joe Scott Plummer

The Notes on pages 21 to 33 form part of these Accounts.

Cash Flow Statement
for the year ended 31st January 2003

	Note	2003 £	2003 £	2002 £
Net cash inflow from operating activities	18		19,294,289	19,433,017
Servicing of finance				
Interest paid		(9,265,619)		(8,745,854)
Preference dividends paid		(64,496)		(42,997)
Net cash outflow on servicing of finance			(9,330,115)	(8,788,851)
Taxation				
UK income tax repaid (paid)			9,669	(660,987)
Investing Activities				
Payments to acquire fixed asset investments		(138,920,574)		(221,291,887)
Proceeds on disposal of fixed asset investments		151,375,089		227,689,157
Net cash inflow from investing activities			12,454,515	6,397,270
Equity dividends paid			(17,357,668)	(16,959,605)
Net cash inflow (outflow) before financing			5,070,690	(579,156)
Financing				
Decrease in short term loan		(461,460)		(802,368)
Purchase of Ordinary Shares for cancellation		–		(405,520)
Cash outflow from financing			(461,460)	(1,207,888)
Increase (decrease) in cash	19		4,609,230	(1,787,044)

The Notes on pages 21 to 33 form part of these Accounts.

Statement of Accounting Policies

for the year ended 31st January 2003

1. 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.

2. Revenue - Dividends on equity shares are accounted for on an ex-dividend basis. UK dividends are shown net of tax credits. 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 lending fees are accounted for on an accruals basis. Underwriting commission is recognised when the issue underwritten closes.

3. 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 Company's prospective split of capital and income returns.

4. 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 the realised Capital Reserve.

5. Finance costs – In accordance with Financial Reporting Standard 4 "Capital Instruments", long term borrowings are stated as 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 and revenue in the ratio 65:35 to reflect the Company's prospective split of capital and income returns.

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

   Full provision is made for deferred taxation except to the extent that deferred tax assets are likely to be considered irrecoverable.

7. 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.

8. 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 2003

1. Income

	2003 £	2003 £	2002 £
Income from Investments			
Franked income:			
Equity income from UK investments		21,233,313	20,905,128
Special dividends from UK investments		602,000	212,750
Unfranked income:			
Interest from UK fixed income securities		3,849	199,287
		21,839,162	21,317,165
Other income:			
Deposit interest	143,730		256,202
Underwriting commission	108,132		11,321
Stocklending fees	9,341		10,983
Other	400		–
		261,603	278,506
Total income		22,100,765	21,595,671

	2003 £	2002 £
Income from Investments		
Listed	21,839,162	21,317,165
Unlisted	–	–
	21,839,162	21,317,165

2. Investment Management Fee

	2003 £ Revenue	2003 £ Capital	2003 £ Total	2002 £ Revenue	2002 £ Capital	2002 £ Total
Investment management fee	684,279	1,270,805	1,955,084	805,463	1,495,860	2,301,323

The management contract with Allianz Dresdner Asset Management (UK) Ltd ("Allianz"), terminable at one year's notice, provides for a management fee based on 0.35% (2002 – 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 Allianz. The amounts stated include irrecoverable VAT of £291,183 (2002 – £342,750). Under the contract Allianz provides the Company with investment management, accounting, secretarial and administration services.

Notes to the Accounts

for the year ended 31st January 2003

3. Expenses of Administration

	2003 £	2002 £
Directors' fees	63,729	68,053
Auditors' remuneration for audit services	14,814	15,891
Marketing costs of Savings Scheme	201,596	281,994
Other promotional activity	32,686	34,561
Other administrative expenses	194,963	187,931
	507,788	588,430

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

(ii) Payments of £1,763 to the Auditors in respect of non-audit services are included in other administrative expenses (2002 – £nil).

(iii) Directors' fees are paid at the rate of £11,000 per annum (2002 – £10,000). The Chairman of the Audit Committee receives an additional £2,000 (2002 – £2,000) and the Chairman receives fees of £15,000 (2002 – £15,000).

4. Finance Costs of Borrowings

	2003 £ Revenue	2003 £ Capital	2003 £ Total	2002 £ Revenue	2002 £ Capital	2002 £ Total
On Stepped Rate Interest Loan repayable after more than five years	1,265,608	2,350,415	3,616,023	1,094,179	2,032,046	3,126,225
On Fixed Rate Interest Loan repayable after more than five years	1,326,966	2,464,366	3,791,332	1,324,943	2,460,609	3,785,552
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	622,089	1,155,309	1,777,398	621,605	1,154,410	1,776,015
On sterling overdraft	5,627	–	5,627	8,081	–	8,081
	3,239,540	6,005,840	9,245,380	3,068,058	5,682,815	8,750,873

Notes to the Accounts

for the year ended 31st January 2003

5. Taxation

	2003 £ Revenue	2003 £ Capital	2003 £ Total	2002 £ Revenue	2002 £ Capital	2002 £ Total
Corporation tax at 30%	–	–	–	39,079	(39,079)	–
Reconciliation of current charge						
Return on ordinary activities before taxation	17,669,158	(147,639,637)	(129,970,479)	17,133,720	(52,275,701)	(35,141,981)
Tax on return on ordinary activities at 30% (2002 – 30%)	5,300,747	(44,291,891)	(38,991,144)	5,140,116	(15,682,710)	(10,542,594)
Reconciling factors:						
Non taxable income	(6,550,594)	–	(6,550,594)	(6,335,363)	–	(6,335,363)
Non taxable capital gains	–	42,108,898	42,108,898	–	13,529,108	13,529,108
Disallowable expenses	135,440	121,002	256,442	106,184	19,405	125,589
Excess of allowable expenses over taxable income	1,114,407	2,061,991	3,176,398	1,128,142	2,095,118	3,223,260
Current year tax charge	–	–	–	39,079	(39,079)	–

The Company's taxable income is exceeded by its tax allowable expenses, which include both the capital and revenue elements of the management fee and finance costs of borrowings. The Company has surplus expenses carried forward of £56m (2002 – £45m). Given the Company's current investment strategy, it is unlikely to generate sufficient UK taxable profits to relieve these expenses.

As at 31st January 2003 there is an unrecognised deferred tax asset, measured at the standard rate of 30%, of £16.7m (2002 – £13.5m), This deferred tax asset relates to the current and prior year unutilised expenses. It is considered uncertain that there will be a liability in the future against which the deferred asset can be offset. Therefore, the asset has not been recognised.

6. Dividends on Ordinary Shares

	2003 £	2002 £
Dividends on Ordinary Shares of 25p–		
First interim 4.3p paid 9th August 2002 (2002 – 4.2p)	4,390,469	4,290,465
Second interim 4.3p paid 7th November 2002 (2001 – 4.2p)	4,390,469	4,290,465
Third interim 4.3p paid 14th February 2003 (2002 – 4.2p)	4,390,469	4,288,365
Final proposed 4.3p payable 13th May 2003 (2002 – 4.2p)	4,390,470	4,288,365
Prior year over accrual	–	(2,049)
	17,561,877	17,155,611

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 all or part of this tax credit and charities are subject to transitional provisions.

7. Return per Ordinary Share

	2003 £ Revenue	2003 £ Capital	2003 £ Total	2002 £ Revenue	2002 £ Capital	2002 £ Total
Return after taxation	17,669,158	(147,639,637)	(129,970,479)	17,094,641	(52,236,622)	(35,141,981)
Attributable to Preference Stockholders	(42,997)	–	(42,997)	(42,997)	–	(42,997)
Attributable to Ordinary Shareholders	17,626,161	(147,639,637)	(130,013,476)	17,051,644	(52,236,622)	(35,184,978)
Return per Ordinary Share	17.26p	(144.60)p	(127.34)p	16.70p	(51.15)p	(34.45)p

Notes to the Accounts

for the year ended 31st January 2003

8. Fixed Asset Investments

	Note	2003 £	2002 £
Listed at market valuation on recognised Stock Exchanges –			
United Kingdom		391,660,828	546,754,450
Unlisted at Directors' valuation –		42,912	17,215
Total fixed asset investments		391,703,740	546,771,665
Market value of investments brought forward		546,771,665	591,210,681
Unrealised losses (gains) brought forward		422,226	(53,024,144)
Cost of investments held brought forward		547,193,891	538,186,537
Additions at cost		136,643,652	224,015,391
Disposals at cost		(176,509,549)	(215,008,037)
Costs of investments held at 31st January		507,327,994	547,193,891
Unrealised losses at 31st January		(115,624,254)	(422,226)
Market value of investments held at 31st January		391,703,740	546,771,665
Losses on investments			
Net realised (losses) gains based on historical costs		(25,160,964)	8,397,180
Less: Net unrealised losses (gains) recognised on these investments at the previous balance sheet date		8,180,986	(1,889,072)
Net realised (losses) gains based on carrying value at previous balance sheet date		(16,979,978)	6,508,108
Net unrealised losses arising in the year		(123,383,014)	(51,557,298)
Net losses on investments		(140,362,992)	(45,049,190)

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

		2003	2002
Stock Lending			
Aggregate value of securities on loan at year-end		6.8m	15.2m
Maximum aggregate value of securities on loan during the year		90.2m	41.6m
Fee income from stock lending during the year		9,341	10,983

In respect of securities on loan at the year-end, the Company held £7.5m (2002 – £16.0m) as collateral, the value of which exceeded the value of the loan securities by £0.7m (2002 – £0.8m).

In respect of the maximum aggregate value of securities on loan during the year, the Company held £99.2m (2002 – £43.7m) as collateral, the value of which exceeded the value of securities on loan by £9.0m (2002 – £2.1m).

Notes to the Accounts

for the year ended 31st January 2003

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 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. This subsidiary is deemed not material for the purposes of giving a true and fair view.

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	Total Net Assets* £	Class of Shares Held	% of Class held	% Equity
First Debenture Finance PLC ('FDF')	(841,134)	'A' Shares	39.2	50.0
		'B' Shares	59.2	n/a
		'C' Shares	45.6	n/a
		'D' Shares	60.1	n/a
Fintrust Debenture PLC ('Fintrust')	21,613	Ordinary	50.0	50.0

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 Company'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. 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.

*At the date of the latest published financial statements.

10. Current Assets and Creditors

	2003 £	2002 £
Debtors –		
Sales for future settlement	443,966	470,470
Accrued income	1,878,978	2,129,245
Other debtors	28,346	19,484
Taxation recoverable	–	9,669
	2,351,290	2,628,868
Cash at bank –		
Current account	3,866,703	–

Notes to the Accounts

for the year ended 31st January 2003

10. Current Assets and Creditors (continued)

	Note	2003 £	2002 £
Creditors: Amounts falling due within one year–			
Bank overdraft		–	742,527
Purchases for future settlement		446,582	2,723,504
Short term loan (see (v) below)		224,361	685,821
Other creditors		498,079	1,083,088
Interest on borrowings (see (vi) below)		1,287,893	1,319,266
Dividend on Cumulative Preference Stock Units		–	21,499
Dividend on Ordinary Shares (declared)	6	4,390,469	4,288,365
Dividend on Ordinary Shares (proposed)	6	4,390,470	4,288,365
		11,237,854	15,152,435
Creditors: Amounts falling due after more than one year–			
Stepped Rate Interest Loan (see (i) below)		35,106,731	34,998,003
Fixed Rate Interest Loan (see (ii) below)		46,631,304	46,743,496
5.875% Secured Bonds 2029 (see (iii) below)		28,985,573	28,970,975
4% Perpetual Debenture Stock (see (iv) below)		1,375,000	1,375,000
		112,098,608	112,087,474

(i) The effective interest rate of the Stepped Rate Interest Loan over its terms is 11.28% per annum.

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%. These amounts are repayable on 2nd January 2018 exclusive of any redemption expenses, together with a premium of £8,366,513.

The initial interest rate in 1987 on the Loan Notes and Bonds was 7.16% per annum. This increased annually by 7.5% compound until January 1998 when it reached its current rate of 14.75%. However, the combined effect of this interest charge and the accrual of the premium referred to above results in an effective interest rate of 11.28% per annum. Interest is payable in January and July each year.

Interest on the Loan Notes is variable in accordance with the terms of the agreement with the lender, First Debenture Finance PLC ("FDF").

The Company has guaranteed the repayment of £34,012,852, being its proportionate share (60.10%) of the required amount to enable FDF to meet all of its liabilities to repay principal and interest on its £56.6 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 KOIT's 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 2003, the unamortised premium included within the Fixed Rate Interest Loan balance of greater than one year amounted to £4,759,035 (2002 – £4,873,202).

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.

Notes to the Accounts

for the year ended 31st January 2003

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 Bonds 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. Interest is repayable in arrears by equal half yearly instalments in May and November.

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

(vi) Interest on borrowings consists of:

	2003 £	2002
Stepped Rate Interest Loan	282,355	313,728
Fixed Rate Interest Loan	783,545	783,545
5.875% Secured Bonds 2029	208,243	208,243
4% Perpetual Debenture Stock	13,750	13,750
	1,287,893	1,319,266

11. Share Capital

		2003 £	2002 £
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
102,103,936	Ordinary Shares of 25p	25,525,984	25,525,984
		26,703,984	26,703,984

(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 13th May 2002 to allot relevant securities, in accordance with Section 80 of the Companies Act 1985, up to a maximum aggregate nominal amount of £1,331,828. This authority, if not previously revoked or varied, expires five years from the date of the resoluton.

The Directors are also authorised by a special resolution passed on 13th May 2002 to allot relevent securities for cash, in accordance with Section 95 of the Companies Act 1995, up to a maximum aggregate nominal amount of £1,273,746. This authority, if not previously revoked or renewed, expires at the forthcoming Annual General Meeting and a resolution will be proposed at that Annual General Meeting for its renewal.

Notes to the Accounts

for the year ended 31st January 2003

12. Capital Redemption Reserve

	£
Balance at 1st February 2002	56,250
Movement in the year	–
Balance at 31st January 2003	56,250

13. Capital Reserves

	Realised £	Unrealised £	Total £
Balance at 1st February 2002	385,653,373	(422,226)	385,231,147
Net loss on realisation of investments	(16,979,978)	–	(16,979,978)
Decrease in unrealised appreciation	–	(123,383,014)	(123,383,014)
Transfer on disposal of investments	(8,180,986)	8,180,986	–
Investment management fee	(1,270,805)	–	(1,270,805)
Finance costs of borrowings	(6,005,840)	–	(6,005,840)
Balance at 31st January 2003	353,215,764	(115,624,254)	237,591,510

14. Revenue Reserve

	£
Balance at 1st February 2002	10,129,434
Profit for the year	64,284
Balance at 31st January 2003	10,193,718

Notes to the Accounts
for the year ended 31st January 2003

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 2003	2002
Ordinary Shares of 25p	267.8p	412.3p
3.65% Cumulative Preference Stock Units of £1	100.0p	100.0p

The Net Asset Value per Ordinary Share is based on 102,103,936 Ordinary Shares in issue at the year end (2002 – 102,103,936).

	Net Asset Values attributable 2003 £	2002 £
Ordinary Shares of 25p	273,407,271	420,982,624
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 2002	420,982,624	1,178,000	422,160,624
Total return on ordinary activities after taxation for the year	(130,013,476)	42,997	(129,970,479)
Dividends appropriated in the year	(17,561,877)	(42,997)	(17,604,874)
Total net assets attributable at 31st January 2003	273,407,271	1,178,000	274,585,271

16. Reconciliation of Movements in Shareholders' Funds

	2003 £	2002 £
Revenue reserves		
Revenue profit available for distribution	17,669,158	17,094,641
Dividends appropriated in the year	(17,604,874)	(17,198,608)
Transfer to (from) distributable reserves	64,284	(103,967)
Other reserves		
Recognised net capital losses transferred to capital reserves	(147,639,637)	(52,236,622)
Purchase of Ordinary Shares for cancellation	–	(405,520)
Net decrease in Shareholders' Funds	(147,575,353)	(52,746,109)
Opening Shareholders' Funds	422,160,624	474,906,733
Closing Shareholders' Funds	274,585,271	422,160,624

Notes to the Accounts

for the year ended 31st January 2003

17. Contingent Liabilities and Guarantees

At 31st January 2003 there were no outstanding contingent liabilities (2002 – £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 the Stepped Rate Loan are provided in Note 10(i) "Current Assets and Creditors" on page 27.

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

	2003 £	2002 £
Revenue before taxation	17,669,158	17,133,720
Add: Finance costs of borrowings	3,239,540	3,068,058
Less: Management fee charged to capital	(1,270,805)	(1,495,860)
UK income tax deducted from unfranked income	–	740
	19,637,893	18,706,658
Decrease in debtors	241,405	820,175
Decrease in creditors	(585,009)	(93,816)
Net cash inflow from operating activities	19,294,289	19,433,017

19. Reconciliation of Net Cash Flow to Movement in Net Debt

(i) Analysis of Net Debt

	Overdraft £	Cash £	Short term loan £	Stepped and Fixed Rate loans £	5.875% Secured Bonds 2029 £	4% Perpetual Debenture Stock £	Net Debt £
At 1st February 2002	(742,527)	–	(685,821)	(81,741,499)	(28,970,975)	(1,375,000)	(113,515,822)
Movement in year	742,527	3,866,703	461,460	3,464	(14,598)	–	5,059,556
At 31st January 2003	–	3,866,703	(224,361)	(81,738,035)	(28,985,573)	(1,375,000)	(108,456,266)

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

	2003 £	2002 £
Net cash inflow (outflow)	4,609,230	(1,787,044)
Decrease in short term loan	461,460	802,368
Increase in long term loans	(11,134)	(5,019)
Movement in net funds	5,059,556	(989,695)
Net debt brought forward	(113,515,822)	(112,526,127)
Net debt carried forward	(108,456,266)	(113,515,822)

Notes to the Accounts

for the year ended 31st January 2003

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 17.

(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	2003 Fixed rate interest paid £000s	2003 Floating rate interest paid £000s	2003 Nil interest paid £000s	2003 Total £000s	2002 Fixed rate interest paid £000s	2002 Floating rate interest paid £000s	2002 Nil interest paid £000s	2002 Total £000s
Financial Assets									
Values not directly affected by changes in interest rates:									
Equities	Sterling	–	–	391,689	391,689	–	–	542,558	542,558
Equities	US Dollar	–	–	15	15	–	–	17	17
Preference Shares and Bonds	Sterling	–	–	–	–	4,197	–	–	4,197
Cash	Sterling	–	3,867	–	3,867	–	–	–	–
Total Financial Assets		–	3,867	391,704	395,571	4,197	–	542,575	546,772
Financial Liabilities									
Values directly affected by changes in interest rates:									
First Debenture Finance loan	Sterling	(46,631)	–	–	(46,631)	(46,743)	–	–	(46,743)
Fintrust loan	Sterling	(35,107)	–	–	(35,107)	(34,998)	–	–	(34,998)
5.875% Secured Bonds 2029	Sterling	(28,986)	–	–	(28,986)	(28,971)	–	–	(28,971)
4% Perpetual Debenture Stock	Sterling	(1,375)	–	–	(1,375)	(1,375)	–	–	(1,375)
		(112,099)	–	–	(112,099)	(112,087)	–	–	(112,087)
Values not directly affected by changes in interest rates:									
Bank overdraft	Sterling	–	–	–	–	–	(743)	–	(743)
Total Financial Liabilities		(112,099)	–	–	(112,099)	(112,087)	(743)	–	(112,830)
Net Financial (Liabilities) Assets		(112,099)	3,867	391,704	283,472	(107,890)	(743)	542,575	433,942
Short term debtors and creditors					(8,887)				(11,781)
Net Assets per Balance Sheet					274,585				422,161

Notes to the Accounts

for the year ended 31st January 2003

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

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

	Maturity date	Amount borrowed £	Coupon rate	Effective rate since inceptions*
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 Bonds	20/12/2029	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% (2002 – 9.58%) and the weighted average period to maturity of these liabilities (excluding the 4% Perpetual Debenture Stock) is 21.2 years (2002 – 22.2) years.

(b) Currency Risk Profile

As at 31st January 2003 £15,367 (2002 – £17,215) of the assets of the Company were denominated in US Dollars with the effect that the total net assets and total return are not materially affected by currency movements.

(c) Fair Value Disclosures

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

	2003 £ million Book value	2003 £ million Fair value	2002 £ million Book value	2002 £ million Fair value
First Debenture Finance Loan	35.1	51.2	35.0	51.9
Fintrust Loan	46.7	56.9	46.7	55.8
5.875% Secured Bonds	29.0	28.1	29.0	26.2
4% Perpetual Debenture Stock	1.4	1.2	1.4	1.0

(d) Liquidity Profile

The maturity profile of the Company's financial liabilities at 31st January 2003, (being the borrowings from Fintrust, First Debenture Finance, the 5.875% Secured Bonds and the 4% Perpetual Debenture Stock) is detailed in Note 10 – "Current Assets and Creditors" on pages 27 and 28. The undrawn committed borrowings facilities available to the Company at 31st January 2003 were £10,000,000.

(e) Hedging Instruments

At the year end the Company had no hedging arrangements in place (2002 – Nil).

Independent Auditors' Report

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

We have audited the financial statements which comprise the statement of total return, the balance sheet, the cash flow statement and notes 1 to 20, which have been prepared under the historical cost convention (as modified by the revaluation of certain fixed assets) and the accounting policies set out in the statement of accounting policies. We have also audited the disclosures required by Part 3 of Schedule 7A to the Companies Act 1985 contained in the Directors' Remuneration Report ("the auditable part").

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report, the directors' remuneration 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 and the auditable part of the Directors' Remuneration Report in accordance with relevant legal and regulatory requirements, United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the auditable part of the Directors' Remuneration Report have been 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 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 unaudited part of the Directors' Remuneration Report, the investment manager's report 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 of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or 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 and the auditable part of the Directors' Remuneration Report. 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 and the auditable part of the Directors' Remuneration Report 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 stat e of the Company's affairs at 31st January 2003 and of its total return and cash flows for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- those parts of the Directors' Remuneration Report required by Part 3 of Schedule 7A to the Companies Act 1985 have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Southwark Towers
32 London Bridge Street
London SE1 9SY

9th April 2003

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 confirm that they have complied with the above requirements in preparing the financial statements. 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. The financial statements are published on the www.allianzdresdneram.co.uk website, which is a website maintained by the Company's Investment Manager, Allianz Dresdner Asset Management (UK) Limited ("Allianz"). The maintenance and integrity of the website maintained by Allianz or any of its subsidiaries is, so far as it relates to the Company, the responsibility of Allianz. The work carried out by the auditors does not involve consideration of the maintenance and integrity of these websites and, accordingly, the auditors accept no responsibility for any changes that have occurred to the financial statements since they were initially presented on the website. Visitors to the website need to be aware that legislation in the United Kingdom governing the preparation and dissemination of the financial statements may differ from legislation in their juridiction.

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 2003 and with the Internal Control Guidance for Directors in the Combined Code published in September 1999 ("the Turnbull guidance") except that, 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 five 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 39, 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.

The Chairman of the Company is a non-executive Director. 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 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, which due to the size of the Board consists of all the Directors and considers nominations made in accordance with an agreed procedure.

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 and terms of appointment of the auditors together with their remuneration as well as the non-audit services provided by the auditors. The committee also reviews from time to time the terms of the management contract with the Managers. It also meets with representatives of the Managers 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.

Environment Policy

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

Directors' Remuneration

The Directors' Remuneration Report is set out on page 38.

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 40 to 43. 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 on page 35 and a statement of going concern is on page 40.

The report of the auditors can be found on page 34.

Internal Control

The Directors have overall responsibility for the Company's system of internal control and are also responsible for reviewing its effectiveness. 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 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. The Board continues to check that good systems of internal control and risk management are embedded in the operations and culture of the Company and its key suppliers.

- The appointment of Allianz Dresdner Asset Management (UK) Limited ("Allianz") as the Managers. Allianz provides all investment management, accounting and secretarial services to the Company. The Managers 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 Note 2 on page 22). 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. Allianz is regulated by the Financial Services Authority and its compliance department regularly monitors its compliance with The Financial Services Authority's rules. The effectiveness of the internal controls is assessed by the Managers' compliance and risk management departments on an ongoing basis.

- The regular review and control by the Board of asset allocation and any risk implications. The regular and comprehensive review by the Board of management of 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 agreements with the Managers and assesses the Managers' systems of controls. The Audit Committee also receives reports from the Managers' internal auditors and compliance department.

By means of the process above, the Board has reviewed the effectiveness of internal controls for the period under review and up to the date of the signing of this Report and Accounts

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. The Managers use a proxy voting service which casts votes in accordance with the guidelines of the National Association of Pension Funds (NAPF) research material, unless its clients request a very specific policy to be voted by its fund managers.

Where Directors hold directorships on the boards of companies in which the Company is invested, they do not participate in decisions made concerning those investments.

Directors' Remuneration Report

This report is submitted in accordance with the Directors' Remuneration Report Regulations 2002 for the year ended 31st January 2003.

The Board

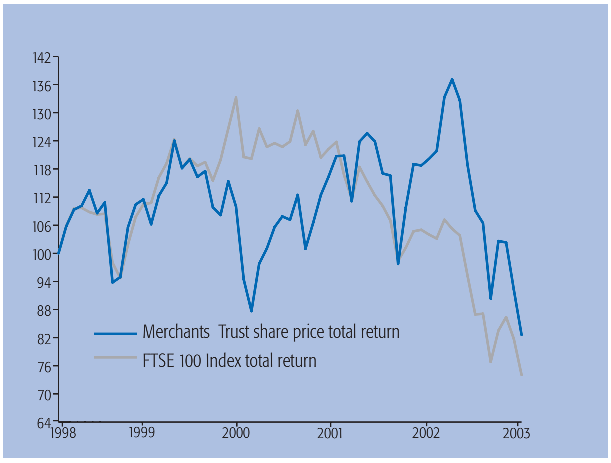
The Board of Directors is composed solely of non-executive Directors and the determination of the Directors' fees is a matter dealt with by the whole Board. The Board has not been provided with advice or services by any person to assist it to make its remuneration decisions, although the Directors carry out reviews from time to time of the fees paid to the directors of other investment trusts.

Policy on Directors' Remuneration

Directors meet at least six times a year and the audit committee meets twice a year. Directors offer themselves for retirement at least once every three years. No Director has a service contract with the Company. The Company's policy is for the Directors to be remunerated in the form of fees, payable quarterly in arrears. There are no long term incentive schemes and fees are not related to the individual directors' performance, nor to the performance of the Board as a whole.

The Company's Articles of Association limit the aggregate fees payable to the Board of Directors to a total of £100,000 per annum. Subject to this overall limit, it is the Company's policy to determine the level of Directors' fees having regard to the level of fees payable to non-executive directors in the investment trust industry generally, the role that individual Directors fulfil, and the time committed to the Company's affairs.

Performance Graph



Directors' and Officers' Liability insurance cover is held by the Company.

The Company's performance is measured against the FTSE 100 Index as this is the most appropriate in respect of its asset allocation and is the Company's benchmark.

The following disclosures on directors' remuneration have been audited as required by Part 3 of Schedule 7A of the Companies Act 1985.

Remuneration

In the year to 31st January 2003 Directors were paid at the rate of £10,000 per annum until 13th May 2002 and £11,000 thereafter with the Chairman of the Audit Committee receiving an extra £2,000 per annum and the Chairman of the Board receiving £15,000 per annum. The policy is to review these rates from time to time, but reviews will not necessarily result in a change to the rates.

Directors' emoluments

The payments receivable during the year and in the previous year are as follows:

	Director's fees Year 2003 £	Director's fees Year 2002 £
H. A. Stevenson	15,000	15,000
P. J. Scott Plummer	13,721	13,000
Sir John Banham	10,721	10,000
R. A. Barfield	10,721	10,000
Sir Bob Reid	10,721	10,000
A. D. A. W. Forbes*	2,846	10,000
Totals	63,730	68,000

*Ceased to be a Director and to be paid Directors' fees from 13th May 2002.

By Order of the Board
K. J. Salt
Secretary

9th April 2003

Directors and Management

Directors

Mr H. A. 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 other companies and a member of the Investment Committee of the Wellcome Trust.

Sir John Banham*
(Born August 1940) joined the Board in August 1992. Formerly Controller of the Audit Commission and Director General of the Confederation of British Industry, he is Chairman of Whitbread PLC, Geest plc, ECI Ventures LLP and Cyclacel Limited. He is also the Senior Non-Executive Director of Amvescap Plc.

Mr R. A. 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, The Baillie Gifford Japan Trust PLC, JP Morgan Fleming Overseas Investment Trust PLC, The Edinburgh Investment Trust PLC, Marshalls PLC, New Look Group PLC and other companies.

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.

Mr P. J. Scott Plummer* (Chairman of Audit Committee)
(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 was approved by the Inland Revenue as an investment trust for the year ended 31st January 2002 and approval is expected to be given for the year ended 31st January 2003. In the opinion of the Directors the Company has conducted its affairs so as to enable it to continue to obtain S.842 approval.

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

The share capital of the Company is set out in note 11 on page 28.

Payment Policy

It is the Company's payment policy for the financial year to 31st January 2004 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 losses based on historical costs of £25,160,964 (2002 –£8,397,180 gains). Provisions contained in the Finance Act 1980 exempt approved Investment Trusts from corporation tax on their chargeable gains. Invested funds at 31st January 2003 had a value of £391,703,740 before deducting net liabilities of £117,118,469 (2002 –£546,771,665 and £124,611,041).

Net Asset Value

The Net Asset Value of the Ordinary Shares of 25p at the year end, after deducting the provision for the final dividend, was 267.8p as compared with a value of 412.3p at 31st January 2002.

Donations and Subscriptions

Aggregate charitable donations and subscriptions is respect of the year amounted to £nil (2002 –£2,564). 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 16 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.

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.

Corporate Governance

The Corporate Governance Statement is set out on pages 36 and 37.

Directors' Fees

A report on the Directors' remuneration is set out on page 38.

Directors' Report

Revenue

	£	£
Revenue for the year after deducting management and general expenses and finance costs of borrowing amounted to		17,669,158
Taxation		–
and there remained a balance of		17,669,158
from which has been deducted the dividend on £1,178,000 of Preference Stock		(42,997)
leaving available for distribution to the Ordinary Shareholders		17,626,161
Dividends		
Provisions have been made in the Accounts for dividends announced on the Ordinary Shares of 25p as follows:		
First Interim 4.3p per Share paid 9th August 2002	4,390,469	
Second Interim 4.3p per Share paid 7th November 2002	4,390,469	
Third Interim 4.3p per Share paid 14th February 2003	4,390,469	
Final proposed 4.3p payable 13th May 2003	4,390,470	
		(17,561,877)
leaving a profit to be transferred to Revenue Reserve		64,284

Subject to the final dividend being approved payment will be made on 13th May 2003 to shareholders on the Register of Members at the close of business on 22nd April 2003 at the rate of 4.3p per Ordinary Share. Further details are provided in Note 6 on page 24.

Substantial Shareholdings

In accordance with Section 198 of the Companies Act 1985 and the Disclosure of Interests in Shares (Amendment) (No. 2) 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%);
Collins Stewart Limited –86,717 (7.36%)
P. S. & J. M. Allen –83,865 (7.1%)
Royal Insurance PLC –60,000 (5.1%)
D. J. Edwards –50,000 (4.2%)
J. Y. Miller –36,000 (3.0%)

Ordinary Shares:
Barclays PLC and its subsidiaries –3,719,287 (3.6%)
Legal & General Group PLC –3,155,760 (3.1%)

Directors and Management

All Directors listed below served throughout the financial year under review.

Mr A. D. A. W. Forbes also served as a Director until his retirement on 13th May 2002.

Mr R. A. Barfield and Mr H. A. Stevenson retire by rotation in accordance with the Articles of Association and being eligible, offer themselves for re-election.

The Directors and their interests in the share capital of the Company as at 31st January 2003 and 2002 are listed below:

	Ordinary Shares of 25p			
	2003 Beneficial	2003 Non-Beneficial	2002 Beneficial	2002 Non-Beneficial
R. A. Barfield	2,001	–	1,930	–
Sir John Banham	2,000	–	800	–
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 27 Ordinary Shares of 25p each through the Allianz Dresdner Asset Management Investment Trust ISA bringing his total holding in the Company to 2,028 shares.

Directors' Report

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 Allianz Dresdner Asset Management (UK) Limited ("Allianz") provides for a fee of 0.35% per annum (2002 –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 Allianz. The management agreement is terminable at one year's notice (2002 –one year).

The Managers have discretion to exercise voting rights at the meeting of companies in which the Company 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 Company. 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 Company.

The Company has entered into an annual agreement with Allianz to operate the Savings Plan. The cost to the Company for the year ending 31st January 2004 will be £169,404 excluding VAT (2003 –£272,140 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 to 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		%	
	2003	2002	2003	2002	2003	2002	2003	2002
Private holders*	9,988	10,212	62.0	64.2	25,920	26,829	25.4	26.3
Nominees	5,250	4,844	32.6	30.4	66,764	66,015	65.4	64.7
Insurance Companies	39	43	0.2	0.3	1,966	1,784	1.9	1.7
Other holders	607	559	3.8	3.5	4,389	3,796	4.3	3.7
Pension Funds	9	9	0.1	0.1	97	91	0.1	0.1
Investment Trusts and Funds	215	240	1.3	1.5	2,967	3,588	2.9	3.5
	16,108	15,907	100.0	100.0	102,103	102,103	100.0	100.0

*Including PEP, ISA and Saving Plan Nominees.

Based on an analysis of the Ordinary Share register at 28th March 2003 (25th March 2002).

Directors' Report

Directors' and Officers' Liability Insurance

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

Purchase of Own Shares

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 £353 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 own 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.

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 15,305,380 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 2004 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 £1,331,828. 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 13th May 2002 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 £1,273,746 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 2003. 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 Allianz Dresdner Asset Management 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

Following the conversion of PricewaterhouseCoopers to a Limited Liability Partnership (LLP) from 1st January 2003, PricewaterhouseCoopers resigned as auditors, and the Directors appointed PricewaterhouseCoopers LLP to fill the casual vacancy created by the resignation. The Directors will place a resolution before the Annual General Meeting to appoint PricewaterhouseCoopers LLP as auditors for the ensuing year. A resolution to authorise the Directors to determine their remuneration will also be proposed at the Annual General Meeting.

By Order of the Board
K. J. Salt
Secretary

9th April 2003

Notice of Meeting

Notice is hereby given that the Annual General Meeting of **The Merchants Trust PLC** will be held at **Riverbank House, 2 Swan Lane, London EC4R 3UX**, on Monday 12th May 2003 at 12.00 noon 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 2003 together with the Auditors' Report thereon.

2 To declare a final dividend of 4.3p per Ordinary Share

3 To re-elect Mr R. A. Barfield as a Director.

4 To re-elect Mr H. A. Stevenson as a Director.

5 To approve the Directors' Remuneration Report

6 To re-appoint PricewaterhouseCoopers LLP as Auditors of the Company (having previously been appointed by the Board to fill a casual vacancy arising by reason of the resignation of PricewaterhouseCoopers), to hold office until the conclusion of the next general meeting at which accounts are laid before 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 15,305,380;

(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 2004 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.

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 £1,331,828 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 authority shall allow and enable the Directors to make an offer or agreement before the expiry of that authority which would 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 the Act) for cash as if sub-section (1) of Section 89 of the Act did not apply to any such allotment provided that:

Notice of Meeting

(i) the power granted shall be limited to the allotment of equity securities wholly for cash up to an aggegate nominal amount of £1,273,746 (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.

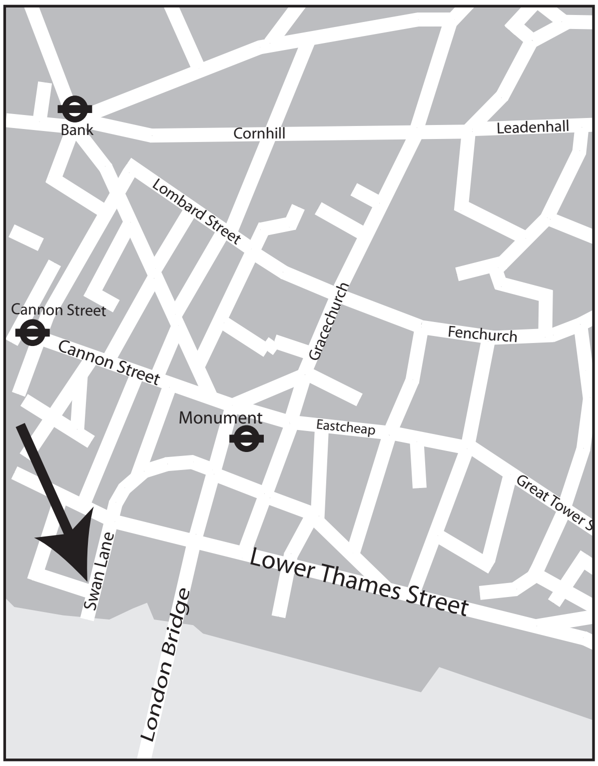
10 Fenchurch Street,	By Order of the Board
London EC3M 3LB	K. J. Salt
9th April 2003	Secretary

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 noon on 10th May 2003 ("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.

Annual General Meeting Venue



Location of Riverbank House

Riverbank House is located in Swan Lane, facing the River Thames. It is a few minutes' walk from Monument, Cannon Street and Bank Underground Stations.

Form of Proxy

Notes on how to complete the proxy form

If you are a registered Ordinary 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. Your proxy will also vote at their discretion on any other business that may be properly put before the Meeting.

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 Ordinary Shareholder and you subsequently decide to attend the Meeting you may do so.

THE MERCHANTS TRUST PLC
FORM OF PROXY
FOR ANNUAL GENERAL MEETING

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

Title and Surname

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 12th May 2003 at 12.00 noon and at any adjournment.

B Ordinary Business

		For	Against	Abstain
1	To receive the report and accounts	☐	☐	☐
2	To declare a final dividend of 4.3p per Ordinary Share	☐	☐	☐
3	To re-elect Mr R. A. Barfield as a Director	☐	☐	☐
4	To re-elect Mr H. A. Stevenson as a Director	☐	☐	☐
5	To approve the Directors' Remuneration Report	☐	☐	☐
6	To re-appoint PricewaterhouseCoopers LLP 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 Ordinary Shares	☐	☐	☐
9	To renew the Directors' authority to allot shares	☐	☐	☐
10	To renew the Directors' authority to allot shares for cash	☐	☐	☐

C

Title and Surname

Forenames

Address

Postcode

Signature

Date

Third Fold and Tuck in

BUSINESS REPLY SERVICE
Licence No. MB 122

2

Capita Registrars (proxies)
PO Box 25
BECKENHAM,
Kent
BR3 4BR

FIRST FOLD

Second Fold