Allianz
Global Investors

The Merchants Trust PLC

Annual Financial Report for the year ended 31 January 2008

www.merchantstrust.co.uk.

Contents

The Merchants Trust

The Merchants Trust was incorporated on 16 February 1889. It was launched by Robert Benson & Co., predecessors of the current Manager, RCM (UK) Ltd, and originally invested mainly in American railroads. The initial capital was £2 million, of which half was subscribed.

Key Facts

Investment Policy

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.

Gearing

The Company's policy is to remain substantially fully invested.

The Company has the facility to gear – borrow money – with the objective of enhancing future returns. Historically, gearing has been in the form of long-term, fixed-rate debentures. The Board monitors the level of gearing and makes decisions on appropriate action based on the advice of the Manager and the future prospects of the Trust's portfolio.

The Trust's authorised borrowing powers set out in the Articles of Association state that the Company's borrowings may not exceed its called up share capital and reserves. In normal market conditions, it is unlikely that gearing (borrowings as a percentage of net assets) will exceed 35%.

Risk Diversification

The Company will aim to achieve a spread of investments, with no single investment representing more than 15% of assets. The Trust will seek to diversify its portfolio into at least five industrial sectors, with no one sector comprising more than 35% of the portfolio.

Financial Summary

for the years ended 31 January

Revenue	2008	2007	% change
Revenue	£28,495,032	£27,750,450	+2.7
Revenue excluding special dividends	£27,992,582	£26,448,226	+5.8
Available for Ordinary Dividend	£23,649,820	£22,854,005	+3.5
Earnings per Ordinary Share	22.86p	22.17p	+3.1
Dividends per Ordinary Share	21.60p	20.00p	+8.0

Assets	2008	2007	% change
Total Net Assets	£506,187,213	£588,834,675	–14.0
Net Asset Value per Ordinary Share	492.3p	567.5p	–13.3
Ordinary Share Price	425.0p	513.0p	–17.2
Discount of Ordinary Share Price to Net Asset Value	13.7%	9.6%	n/a
Discount (Debt at market value)	9.6%	5.9%	n/a
FTSE 100 Index (Capital Return)			–5.2
FTSE 350 Higher Yield Index (Capital Return)			–12.1

Chairman's Statement

Results

After four successive years in which the net asset value has risen, in this financial year the net asset value per share fell by 13.3% to 492.3p and the total return per share, including dividends paid, was -9.6%. This compares with the total returns of -1.9% and -8.3% recorded by the FTSE 100 Index and the FTSE 350 Higher Yield Index, respectively.

Although the capital performance of the underlying portfolio exceeded that of the Higher Yield Index by 1.5%, gearing had a negative effect on the net asset value, reducing the returns to shareholders by approximately 2.2%. The full performance breakdown is shown on page 4.

In the twelve months to 31 January 2008, the Trust's share price fell by 17.2% from 513.0p to 425.0p. At 11 April 2008, the Trust's ordinary shares yielded 5.1% compared with the yield on the FTSE 100 Index of 3.8%.

Market and Portfolio Background

During the year the stock market became increasingly volatile as the disruption in credit markets spread to other asset classes. Volatility of individual sectors was even higher than at the level of the market as a whole. Higher yielding shares, which generally comprise Merchants' portfolio, performed particularly poorly as higher dividend yields provided little support. This area of the market is also heavily biased towards financials (which were very weak) and has no mining shares (which rose significantly). Another notable feature was the underperformance of medium sized companies often more exposed to the domestic economy.

Earnings per share

In 2007/8 earnings per share rose by 3.1% to 22.86p. This year's earnings include special dividends received by the Trust totalling £0.5m (2007 – £1.3m). Excluding special dividends, revenues increased by 5.8%.

Dividends

The Board is recommending a final dividend of 5.4p per share giving a total of 21.6p for the year, an increase of 8.0% over the total for the previous year.

VAT

During the course of the year, JP Morgan Fleming Claverhouse and the Association of Investment Companies were successful in their case against HM Revenue and Customs and I am pleased to report that VAT is no longer payable on management fees charged to the Trust. An amount of VAT payable in respect of prior years may also be recoverable but it is not yet possible to quantify the exact amount pending the conclusion of discussions with the Manager and no credit for this has been taken in these accounts.

Investment Policy

New Listing Rules for closed end investment funds have been published by the UK Listing Authority. These require the publication of an investment policy for all closed end investment companies which are listed under Chapter 15 of the Listing Rules. Our investment policy is set out on page 2.

Repurchase of Shares

During the financial year and following an increase in the discount of the net asset value to the ordinary share price, 946,413 shares were bought back for cancellation, representing 0.91% of the ordinary shares at the beginning of the year. As in previous years, the Board is proposing to renew the authority to repurchase shares at the forthcoming AGM on 13 May 2008.

Prospects

Over the coming months the disruption in the banking and credit markets is likely to shape developments in the wider economy. US growth is slowing rapidly and the risks of a significant economic slowdown in the UK have increased. Share prices are likely to remain volatile until a measure of confidence returns to the financial markets.

The Trust's Board

Sir Bob Reid, who joined the Board in January 1995, will be retiring from the Board after the AGM in May. During his career Sir Bob has been Deputy Governor of the Bank of Scotland and the Chairman of a number of FTSE 100 and other major companies, including Shell (UK), British Rail, London Electricity and Sears. He has made a notable contribution to the Trust over many years and I am sure that all shareholders will join me in thanking him and in wishing him well.

We will be appointing Michael McKeon and Henry Staunton to the Board with effect from 1 May 2008. Both of them will bring long and broad experience of a number of industries in which the Trust's funds are invested. Details of their respective careers are set out on page 14. In accordance with the Trust's Articles of Association, both of them will stand for election at the forthcoming Annual General Meeting.

Annual General Meeting

The Annual General Meeting of the Company will be held on Tuesday 13 May 2008 at 12.00 noon and we look forward to seeing as many shareholders then as are able to attend.

Hugh Stevenson
Chairman
14 April 2008

Historical Record

Revenue and Capital

Years ended 31 January

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Revenue (£'000s)	20,119*	22,590	21,546	21,596	22,101	22,247	22,675	24,714	27,750	28,495
Earnings per Ordinary Share	15.21p	17.93p	16.35p	16.70p	17.26p	17.34p	17.58p	19.44p	22.17p	22.86p
Dividends per Share	15.59p†	16.00p	16.40p	16.80p	17.20p	17.60p	18.00p	18.90p	20.00p	21.60p
Tax Credit per Share	3.90p§	1.78p	1.82p	1.87p	1.91p	1.96p	2.00p	2.10p	2.22p	2.40p
Gross Ordinary Dividend	19.49p	17.78p	18.22p	18.67p	19.11p	19.56p	20.00p	21.00p	22.22p	24.00p
Total Net Assets attributable to Ordinary Capital (£'000s)	424,859	390,317	473,729	420,983	273,407	357,442	424,511▲	514,713	588,835	506,187
Net Asset Value per Ordinary Share	415.2p	381.4p	463.5p	412.3p	267.8p	350.1p	415.8p▲	504.1p	567.5p	492.3p
NAV Total Return (%)*	+4.9	-4.3	+25.8	-7.4	-30.9	+37.3	+20.8▲	+25.6	+16.4	-9.6
Retail Price Index Increases (%)**	+2.6	+2.1	+1.8	+2.6	+2.7	+2.4	+2.1	+2.3	+4.2	+4.1

Notes

* Restated in accordance with Financial Reporting Standard 16 'Current Taxation'.

† The total distribution for 1999 was 15.59p. This was made up of interim ordinary dividends of 8.86p, an interim FID of 2.98p and a final ordinary dividend of 3.75p. The interim 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.

* NAV total return reflects both the change in net asset value per ordinary share and the net ordinary dividends paid.

** RPIX – excludes the effect of mortgage rates.

▲ Restated in accordance with Financial Reporting Standards 25 'Financial Instruments: Disclosure and Presentation' and 26 'Financial Instruments: Recognition and Measurement'. Years prior to 2005 have not been restated.

Performance Attribution Analysis

for the year ended 31 January 2008

	FTSE 100 Index %	FTSE 350 Higher Yield Index %
Capital return of Index	(5.2)	(12.1)
Relative return from Portfolio	(5.4)	1.5
Capital return of Portfolio	(10.6)	(10.6)
Impact of gearing on Portfolio	(2.2)	(2.2)
Retained Revenue	0.3	0.3
Expenses charged to Capital	(1.3)	(1.3)
Impact of Repurchasing Ordinary Shares	0.1	0.1
Other	0.4	0.4
Change in Net Asset Value per Ordinary Share	(13.3)	(13.3)

Investment Managers' Review

Economic Background

The UK economy grew at a respectable rate during the year with the latest estimate for GDP growth at around 3%. Inflation rose early in the year and temporarily exceeded the Bank of England's upper limit of 3% on the CPI measure before falling back towards the central rate of 2% again. This inflationary pressure led the Monetary Policy Committee of the Bank to raise rates in May and June by a total of 0.5% to 5.75% to restrain growth in consumption.

Conditions in the credit markets changed materially in the summer as the knock-on effects of problems in US sub-prime mortgages spread rapidly, leading to a drying up of liquidity in the wholesale money markets. One notable casualty in the UK was Northern Rock, the predominantly wholesale funded mortgage bank, which saw the first run on a UK bank for over a century.

By December, events in credit markets had significantly changed the economic outlook. Consumer confidence, already suffering from rising energy and food costs, was further dented by higher borrowing costs and lower availability of credit as banks tightened lending policies. This led to a sharp fall in housing transactions. Corporate borrowing costs had also risen as banks' funding costs rose. The MPC cut interest rates in December by 0.25% and by the same amount again in February, just after the financial year end. Flexibility to respond to the deterioration in financial market conditions was limited however by the persistence of inflation in commodity prices, particularly energy and food.

Although house prices and retail sales began to reflect a tougher consumer environment by the year end, overall consumption was solid during the year. The corporate sector in general also showed resilience with most industries seeing healthy profits growth and unemployment claims hitting the lowest levels since the 1970s.

Around the world, the authorities paid close attention to the growing banking crisis. Western central banks responded with a huge injection of liquidity into the banking system over the new year which brought down the wholesale cost of funding. In the USA interest rates were cut rapidly, notably by 1.25% in two moves in January to close the period under review at 3%, down from 5.25% in the summer. This was accompanied by the announcement of a fiscal stimulus package.

Market Trends

The stock market became increasingly volatile as the disruption in credit markets spread to other asset classes. The FTSE 100 index traded for much of the year between 6000 and 6700 but fell heavily in January to close the financial year at 5878 for a total return of -1.9%. Volatility of individual sectors was even higher than at the level of the market as a whole. In this more uncertain environment investors preferred companies offering stability and growth and paid less attention to valuation. Sectors under pressure reflected investor concerns about the growing credit crunch, a peak in the property cycle and the possibility of a consumer driven slowdown. For example, including dividends, the banks sector fell 25%, general retailers 32%, life insurers 15%, travel & leisure stocks 27% and real estate companies 25%. On the other hand natural resources companies were strong, benefiting from booming demand for commodities. The mining sector rose 50% and oil & gas producers were up 12%. Other strong performing sectors included those seen as relatively safe havens and those with exposure to emerging markets where demand remained buoyant. The tobacco sector gave a total return of 20%, mobile telecoms 23% and food producers 10%. Looking at the other large sectors, utilities were broadly unchanged over the year, pharmaceuticals fell 15% on specific concerns and fixed line telecoms were down over 9%.

Higher yielding shares performed particularly poorly as higher dividend yields provided little support. The FTSE 350 High Yield Index returned -8.3%. Another notable feature was the underperformance of medium sized companies, often more exposed to the domestic economy. We commented a year ago that the mid-cap FTSE 250 Index had consistently outperformed the FTSE 100 Index but we expected the trend to reverse. This year, the midcap index underperformed by 7.1%.

Investment Performance

The portfolio return was behind the FTSE 100 index return during the year, reversing the strong gains made in the previous year. The bias of the Trust towards higher yielding shares impacted performance as these companies lagged the broader index. However the portfolio return was ahead of the FTSE 350 Higher Yield Index.

The table below shows the biggest contributions to relative performance from individual companies within the equity portfolio. Looking at the positive stocks, there are three themes evident. First, two of the "growth" companies in the portfolio received takeover bids; **Reuters** and **Xansa**. Second, the "megacap" stocks, **Vodafone** and **Royal Dutch Shell** performed well. Third, we avoided several stocks which underperformed sharply for the reasons described above, including Astrazeneca, Northern Rock, Wolseley and Marks & Spencer.

On the negative side, there were also three major themes. The portfolio has had a relatively low exposure to the mining and oil sectors, mainly because of the low yields on offer. Not owning BG, BHP Billiton and Xstrata and having an underweight position in **Rio Tinto** held back relative performance. Secondly positions in the banks **Bradford & Bingley** and **Royal Bank of Scotland** were impacted by the growing credit crunch. Thirdly a number of industrial and consumer cyclical companies performed poorly, including **FKI** (where takeover talks were called off) **Pendragon**, **Persimmon** and **Rexam**.

Investment Managers' Review

Contribution to Investment Performance Relative to FTSE 100 Index

Positive Contribution	%	Negative Contribution	%
Astrazeneca (not owned)	0.7	BG (not owned)	-1.0
Reuters Group	0.4	Bradford & Bingley	-1.0
Xansa	0.4	BHP Billiton (not owned)	-0.9
Northern Rock (not owned)	0.3	Xstrata (not owned)	-0.7
Vodafone	0.3	Royal Bank of Scotland	-0.7
Wolseley (not owned)	0.3	FKI	-0.7
Lloyds TSB	0.3	Pendragon	-0.6
Marks & Spencer (not owned)	0.3	Persimmon	-0.4
British Land (not owned)	0.2	Rio Tinto (underweight)	-0.4
Royal Dutch Shell	0.2	Rexam	-0.4

Portfolio Changes

The volatility in individual share price movements was extremely high, especially in the last six months of the year. Companies that disappointed expectations were marked down aggressively. This made it a challenging environment for making investment decisions. Despite this, our focus remained on the long term value of businesses and their underlying cashflows.

Whilst we took advantage of volatility in the markets to make selective changes to the portfolio we also maintained basic portfolio management disciplines. These include diversification in order to avoid the Trust being too exposed to any one theme, and a phased approach to buying or selling shares, in the recognition that we will not always be able to time investments perfectly.

Largest Net Investment	£m	Largest Net Sales	£m
BAE Systems	14.6	Lloyds TSB	16.1
Aviva	12.7	Reuters	12.8
HBOS	12.3	Tesco	11.1
Bradford & Bingley	9.9	Royal Dutch Shell	10.7
Compass	9.1	Gallaher	10.3
HSBC	8.4	Premier Foods	9.9
Royal Bank of Scotland	7.8	National Express	8.4
GlaxoSmithKline	7.2	Barclays	7.3
Meggitt	7.0	EMAP	7.2
BT	6.7	Xansa	7.2

We can break down new additions to the portfolio into two categories; firstly companies with limited exposure to the economic environment and secondly those in more cyclical industries like retailing or finance.

In the first category we added several companies to the portfolio offering solid growth prospects where valuations were also attractive. We purchased **BAE Systems**, the UK's largest defence company with significant operations in the USA and Saudi Arabia. This company is delivering strong growth and we were able to buy the shares when they were depressed by concerns over historic corruption allegations. We also purchased **Meggitt**, a diversified defence and aerospace group when it made an acquisition cementing a leading position in aircraft wheels and brakes. The defence activities of both companies are relatively protected from the economic cycle and we are optimistic for the outlook for civil aerospace.

We added **Compass**, the contract catering company which is being turned around under new management with potential to become more efficient and increase profit margins. We also bought **Sage**, a leading small business software company which generates the majority of its profits from repeat service and

Investment Managers' Review

support revenues from their broad customer base. Sage raised their dividend payout ratio reflecting their strong cash generation, taking the yield to a more attractive level.

Another new addition to the portfolio with low economic sensitivity was dairy company **Dairy Crest**. The low valuation does not adequately reflect the gradual transformation of the business from commodity into branded products which include the UK's leading cheese brand Cathedral City.

In the second category, there were also opportunities in the year to buy more cyclical businesses where valuations fell to levels that looked attractive on a long term basis. Early in the year we bought **Pendragon**, the UK's leading car dealership which should benefit from rising profit margins in the medium term as it leads the consolidation of the industry. In the short term this investment proved disappointing as trading deteriorated sharply in a worsening consumer environment.

The other retailer we introduced was **Halfords** which has a more resilient record than many of its peers due to its emphasis on "must buy" products like car maintenance and child safety equipment as well as the growing categories of bicycles and electronic equipment such as satellite navigation systems. The shares were depressed with the sector and looked too cheap.

Elsewhere, we bought **Interserve**, a company involved in Private Finance Initiative investments in schools, prisons and hospitals, and facilities management and construction services with a fast growing Middle-Eastern business. **Close Brothers**, a diversified financial services company was also purchased. Close has a high quality specialist lending business and strong niche positions in securities, asset management and corporate finance. The value of the business was recognised later in the period when they were approached by potential acquirers and we sold part of the holding at a higher price. Subsequent to the year end the takeover interest subsided.

The banks sector was under pressure in the period. The industry has witnessed problems including losses on US mortgages and exotic credit instruments, a liquidity crunch and concerns over rising bad debts amongst US and UK consumers. As an investor it has been difficult to evaluate the long term value of banking franchises with such significant short term headwinds, especially given the banks' highly leveraged balance sheets. However we saw some significant positive factors too. Valuations of banks were pushed down to extremely low levels, arguably already pricing in a UK recession, whilst unemployment - a key driver of bad debts - remained very low. Competition lessened, pushing up lending margins materially and the authorities responded with unprecedented actions (especially in the key US market) including injections of liquidity and interest rate cuts. A well functioning banking system is so important to modern economies that further concerted action is likely to take place, if necessary, but the impact of such action is almost impossible for an investor to model accurately.

In our judgement the long term value of many of the UK banking franchises has not been damaged to the extent implied by share price declines and we maintained a large exposure through the year. However we have made several changes to the portfolio particularly in the second half as credit conditions tightened.

Relatively high valuations led us to reduce **Alliance & Leicester** and **Lloyds TSB**. The latter's low dividend cover was also a concern. We also reduced **Barclays** which has a significant exposure to troubled fixed income capital markets. Conversely we switched into **HBOS**, **Bradford & Bingley** and **Royal Bank of Scotland** as we thought valuations had fallen too far. We also added to **HSBC** where the strength of their balance sheet and their attractive emerging markets operations should compensate for problematic US operations. We did not hold Northern Rock.

Elsewhere we added to several existing holdings, particularly larger companies that offer solid prospects and attractive yields such as **GlaxoSmithKline**, **BT**, **Reed Elsevier** and **Aviva** (including a partial switch from **Legal & General**).

Turning to disposals: several of the companies in the Trust received bid approaches, mostly from foreign companies. **Gallaher**, **Xansa**, **RHM** and **Scottish Power** were taken over whilst we sold **Reuters** and most of the **Resolution** holding after they received bids. Paper and packaging company **Mondi**, demerged from **Anglo American**, was also sold.

As reported in the interim statement, we sold **Tesco**, **EMAP**, **Drax**, **Premier Foods**, **Rentokil Initial** and **National Express**. In the second half of the year we also sold **Pearson**, the education and publishing company on concerns that US state education budgets could come under pressure in the medium term from slowing tax revenues. The position in DIY company **Kingfisher** was reduced (and subsequently exited) on fears over trading. The only other significant activity was to take some profits on the oil companies **Royal Dutch Shell** and **BP** after they rose on the back of higher oil prices.

Future Policy

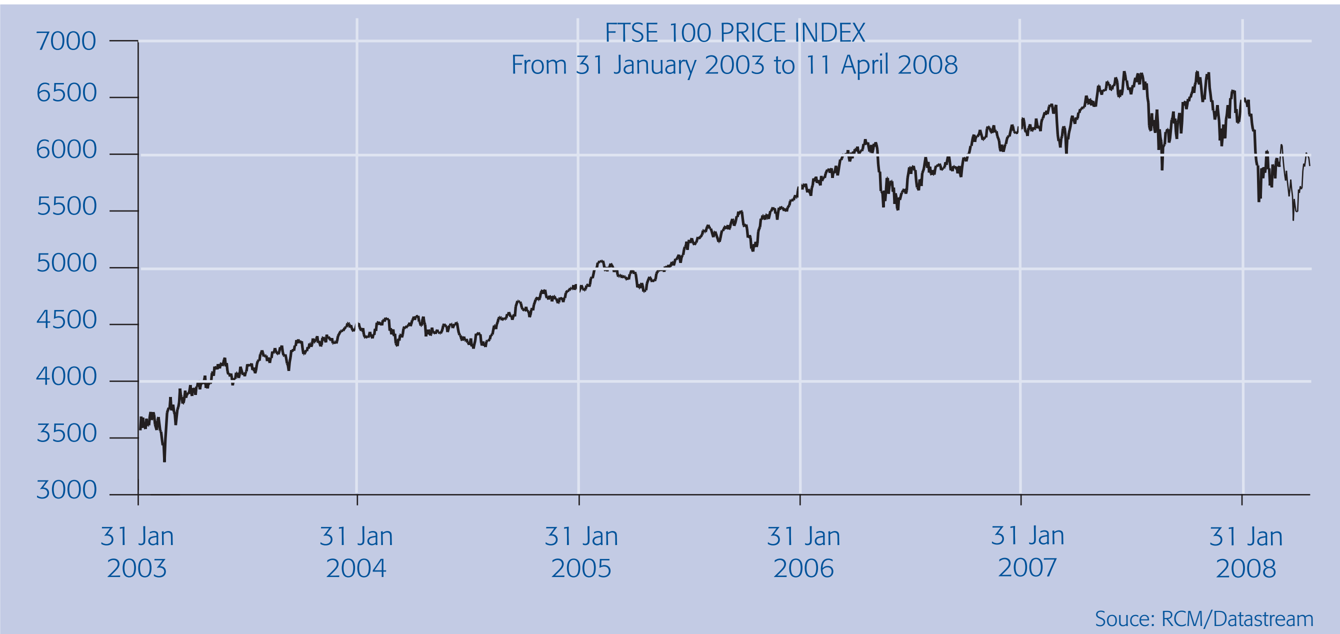
The economic outlook is more uncertain than for many years. The problems in the banking sector have restricted liquidity and credit conditions have tightened materially. Consumers and companies face lower availability and higher costs of finance which could have progressively more serious effects unless conditions ease. The US is seeing a major housing downturn and seems to be entering a recession, although many industrial sectors outside of construction are still robust and exports are strong. The outlook for the UK is not clear. Housing transactions and consumer sectors are likely to remain subdued, as credit is withdrawn and discretionary expenditure remains under

Investment Managers' Review

pressure. However unemployment is very low and the corporate sector is generally in strong health. Interest rate reductions in the USA and the UK will start to have an impact as the year progresses but will be partly offset by higher bank lending spreads. Elsewhere emerging markets are likely to continue to grow strongly, if not at the same rate as last year, but Europe and Japan may see tougher conditions.

Outside the financial and certain consumer sectors most UK companies have been reporting strong results, whilst dividend growth has generally been strong across the board. Looking forward though, the economic and credit picture provides reason to be more cautious. Developed world stock markets have not had to deal with a credit induced slowdown for many years. High volatility in markets reflects increased risks with investors unsure how to react to developments. There is a wide divergence in market prices between companies with high perceived risks, such as high debt levels or cyclical exposure, and companies seen to have more stable growth prospects. Aggregate market valuations are attractive but they give a slightly misleading picture given this divergence.

In this environment, we are maintaining the principles of portfolio diversification and we retain our focus on fundamental research. The portfolio has a large exposure to the very biggest companies, many of which have strong balance sheets and modest valuations. We have also invested in a number of companies with strong market positions offering longer term growth at sensible prices. However we will look to take advantage of market volatility on a selective basis. In particular we are looking for soundly financed companies that are significantly undervalued on a long term basis but out of favour for short term reasons.



Listed Holdings
at 31 January 2008

Name	Value (£)	Principal Activities
GlaxoSmithKline	49,531,140	Pharmaceuticals & Biotechnology
Vodafone	48,718,061	Mobile Telecommunications
BP	47,496,252	Oil & Gas Producers
Royal Dutch Shell 'B' Shares	46,075,900	Oil & Gas Producers
HSBC	43,211,250	Banking
HBOS	24,008,865	Banking
Royal Bank of Scotland	20,322,400	Banking
Aviva	19,780,800	Life Insurance
Anglo American	18,518,500	Mining
Scottish & Southern Energy	18,106,800	Electricity
Rio Tinto	17,590,250	Mining
BT	16,407,650	Fixed Line Telecommunications
BAE Systems	16,042,212	Aerospace & Defence
Reed Elsevier	15,842,869	Media
British American Tobacco	14,339,262	Tobacco
Bradford & Bingley	13,151,775	Banking
Rexam	12,395,683	General Industrials
Barclays	12,166,525	Banking
Centrica	11,635,650	Gas, Water & Multiutilities
National Grid	10,332,900	Gas, Water & Multiutilities
Lonmin	10,263,050	Mining
Compass	8,848,000	Travel & Leisure
Severn Trent	7,204,791	Gas, Water & Multiutilities
Diageo	7,185,200	Beverages
GKN	7,021,875	Automobiles & Parts
Meggitt	6,560,747	Aerospace & Defence
Smiths	6,217,747	General Industrials
Britvic	5,887,575	Beverages
Halfords	5,868,546	General Retailers
Close Bros	5,610,000	General Financial
British Insurance	5,511,219	Non - Life Insurance
Marshalls	5,223,750	Construction & Materials
Friends Provident	5,149,480	Life Insurance
Lloyds TSB	4,962,788	Banking
Sage	4,867,525	Software & Computer Services
Legal & General	4,742,390	Life Insurance
Persimmon	4,548,900	Household Goods

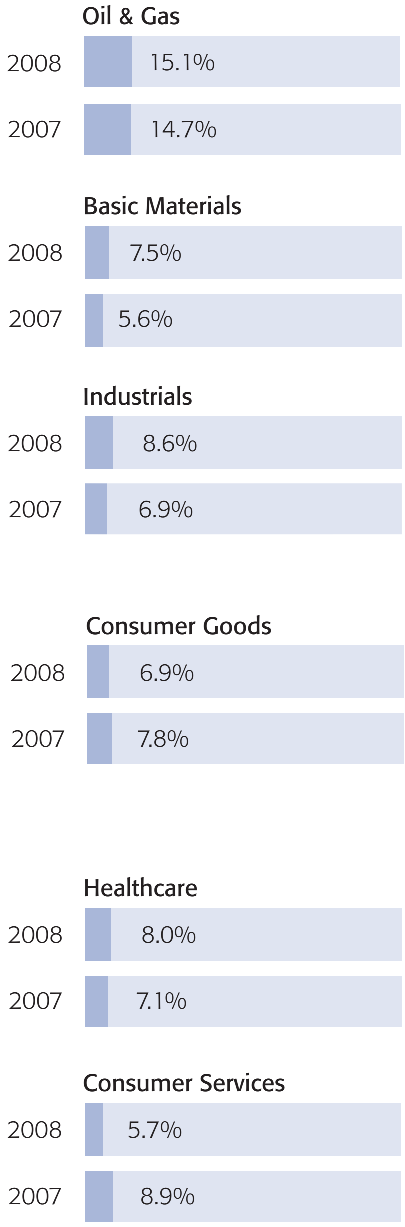
Listed Holdings
at 31 January 2008

Name	Value (£)	Principal Activities
Dairy Crest	4,031,250	Food Producers
FKI	3,899,477	Industrial Engineering
Segro	3,489,615	Real Estate
Resolution	3,328,718	Life Insurance
Interserve	3,125,625	Support Services
Kingfisher	2,735,400	General Retailers
Alliance & Leicester	2,448,750	Banking
International Personal Finance	2,350,000	General Financial
Pendragon	1,666,380	General Retailers
	608,423,542	

Distribution of Total Assets
at 31 January 2008

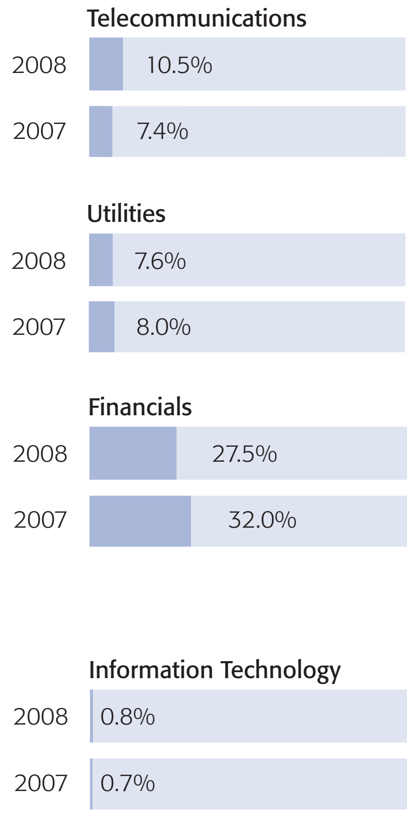
Total Assets (less creditors falling due within one year) £619,601,004 (2007 – £702,382,755)

	Percentage of Total Assets 2008	Percentage of Total Assets 2007
Equities		
Oil & Gas		
Oil & Gas Producers	15.1	14.7
	15.1	14.7
Basic Materials		
Mining	7.5	5.6
	7.5	5.6
Industrials		
Aerospace & Defence	3.7	1.6
Construction & Materials	0.8	2.1
General Industrials	3.0	1.5
Industrial Engineering	0.6	1.2
Support Services	0.5	0.5
	8.6	6.9
Consumer Goods		
Automobiles & Parts	1.1	1.1
Beverages	2.1	2.3
Food Producers	0.7	1.6
Household Goods	0.7	–
Tobacco	2.3	2.8
	6.9	7.8
Healthcare		
Pharmaceuticals & Biotechnology	8.0	7.1
	8.0	7.1
Consumer Services		
Food & Drug Retailers	–	1.5
General Retailers	1.7	1.3
Media	2.6	5.0
Travel & Leisure	1.4	1.1
	5.7	8.9



Distribution of Total Assets
at 31 January 2008

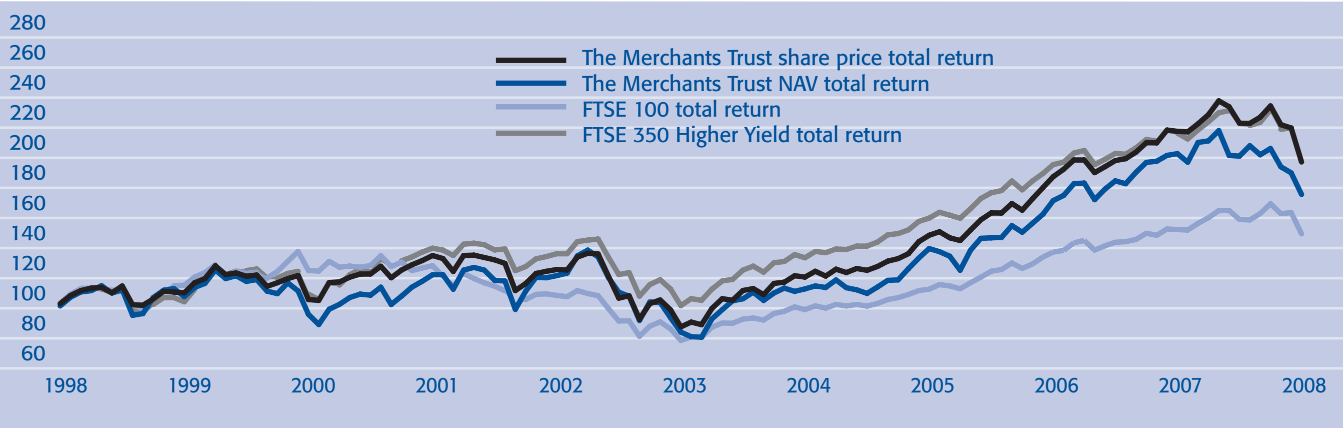
	Percentage of Total Assets 2008	Percentage of Total Assets 2007
Telecommunications		
Fixed Line Telecommunications	2.6	1.7
Mobile Telecommunications	7.9	5.7
	10.5	7.4
Utilities		
Electricity	2.9	4.6
Gas, Water & Multiutilities	4.7	3.4
	7.6	8.0
Financials		
Banks	19.4	23.5
General Financial	1.3	0.8
Life Insurance	5.3	5.5
Non-Life Insurance	0.9	1.1
Real Estate	0.6	1.1
	27.5	32.0
Information Technology		
Software & Computer Services	0.8	0.7
	0.8	0.7
Total Equities	98.2	99.1
Net Current Assets	1.8	0.9
Total Assets	100.0	100.0



Performance Graphs

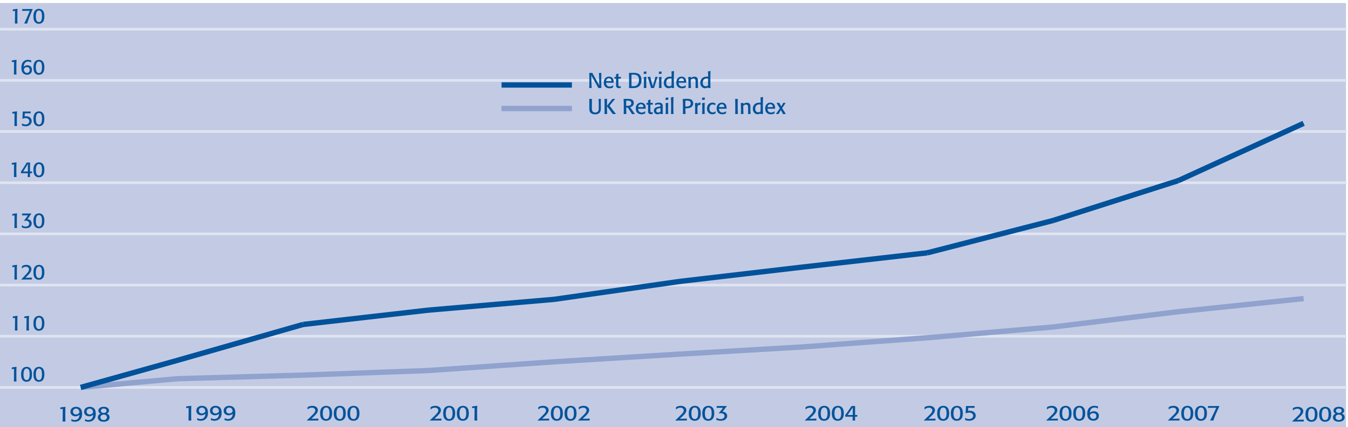
10 year record as at 31 January

The Merchants Trust Total Return compared to key UK equity indices



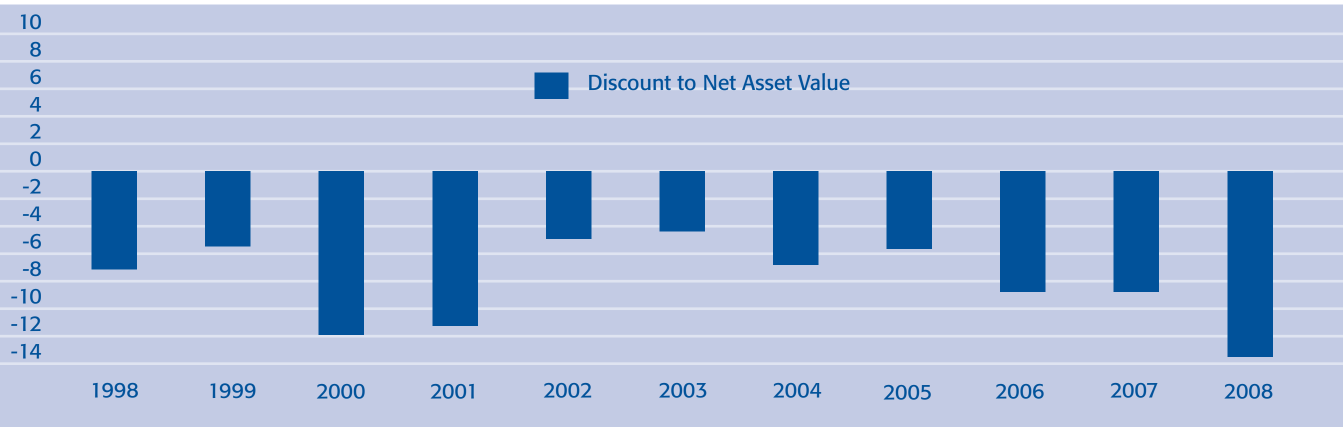
Source: Mellon

The Merchants Trust Net Dividend Growth compared to inflation



Source: Mellon

The Merchants Trust PLC



Source: Datastream

Directors

The current Directors' details are set out below. All Directors are non-executive and independent of the Manager.

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, Chairman of Standard Life Investments, the Senior Independent Director of Standard Life plc, a Non-Executive Director of the Financial Services Authority and a member of the Investment Committee of the Wellcome Trust.

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 The Baillie Gifford Japan Trust PLC, JPMorgan Fleming Overseas Investment Trust PLC, The Edinburgh Investment Trust PLC, Standard Life Investments Property Income Trust Limited and other companies. He is a member of The Professional Oversight Board.

Sir Bob Reid

(Born May 1934) joined the Board in January 1995. He was formerly Deputy Governor of the Bank of Scotland, Chairman of Shell (UK), British Rail, London Electricity plc and Sears PLC. He is Chairman of ICE Futures (Europe) and Senior Non-Executive Director of CHC Helicopter Corporation. Sir Bob will be retiring from the Board at the conclusion of the forthcoming Annual General Meeting.

Sir James Sassoon (Chairman of the Audit Committee)

(Born September 1955) joined the Board in July 2006. He is The Chancellor's Representative for Promotion of the City at HM Treasury, President of the Financial Action Task Force and a Director of Nuclear Liabilities Fund Limited. From 2002 to 2006 he was Managing Director of HM Treasury's Finance and Industry Directorate and a Member of the Treasury Board. Prior to that he had worked at UBS Warburg since 1987 where he held a number of positions, latterly Vice Chairman, Investment Banking. He is a Chartered Accountant.

Mr P. J. Scott Plummer (Senior Independent Director)

(Born August 1943) joined the Board in May 1997. He is a Director of Buccleuch Estates Limited. He was until November 2005 Chairman of Martin Currie Limited, and was formerly a Director of Martin Currie Portfolio Investment Trust PLC and Candover Investments PLC. He is a Chartered Accountant.

Mr Michael McKeon and Mr Henry Staunton will be appointed to the Board with effect from 1 May 2008. Both will be standing for election at the forthcoming Annual General Meeting. Their biographical details are set out below:

Mr M. J. E. McKeon

(Born October 1956) He is Group Finance Director of Severn Trent plc and prior to that, from 2000 until 2005, he was Group Finance Director of Novar plc. He held various senior roles at Rolls-Royce plc from 1997 to 2000. He has extensive experience in a number of overseas positions, having worked at CarnaudMetalbox, Elf Atochem and PricewaterhouseCoopers. He is a Chartered Accountant.

Mr H. E. Staunton

(Born May 1948) He is a non-executive director of Ladbrokes plc, Legal & General plc and Standard Bank Plc. He was previously Finance Director at ITV plc and Granada Group plc. He was also a non-executive director of Emap plc, BSkyB, Independent Television News Limited, Vector Hospitality plc and Ashtead Group plc, of which he was also Chairman between 2001 and 2004. He is a Chartered Accountant.

Directors' Report

The Directors present the annual financial report of the Company and give their report for the year ended 31 January 2008.

Business Review

Business and Status of the Company

The Company is an investment company as defined in Section 266 of the Companies Act 1985.

The Company carries on business as an investment trust and was approved by HM Revenue & Customs as an investment trust in accordance with Section 842 of the Income and Corporation Taxes Act 1988 for the year ended 31 January 2007. In the opinion of the Directors, the Company has subsequently conducted its affairs so that it should continue to qualify. The Company will continue to seek approval under Section 842 of the Income and Corporation Taxes Act 1988 each year. The Company is not a close company for taxation purposes.

Regulatory Environment

The Company is listed on the London Stock Exchange and is subject to UK company law, financial reporting standards, listing rules , tax law and its own Articles of Association. In addition to annual and half yearly financial reports published under these rules, the Company announces net asset values per share on a daily basis for the information of investors. It provides more detailed information on a monthly basis to the Association of Investment Companies, of which the Company is a member, in order for brokers and investors to compare its performance with its peer group. The Board of Directors is charged with ensuring that the Company complies with its own objectives as well as these rules. The Board has appointed RCM (UK) Limited to carry out investment management, accounting, secretarial and administration services on behalf of the Company. The Company has no employees or premises of its own.

Investment Objective and Policies

The Company's objective is 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. 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.

The Company pays quarterly dividends and the Board has a policy of making these progressive from year to year, in keeping with the Company's stated objective to provide an above average level of income and income growth. The dividend has increased every year for the past twenty five years and details of historic dividend payments are set out on page 4.

Performance

In the year to 31 January 2008 the NAV per Share fell by 13.3%. This compares with the capital return on the Company's benchmark indices of -5.2% (FTSE 100) and -12.1% (FTSE 350 Higher Yield). At 31 January 2008 the value of the Company's investment portfolio was £608.5m. The Investment Managers' review on pages 5 to 8 includes a review of developments during the year as well as information on investment activity within the Company's portfolio.

Key Performance Indicators ("KPIs")

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

Performance against the benchmark indices

The Company's performance is benchmarked against the FTSE 100 Index and the FTSE 350 Higher Yield Index. These are the most important KPIs by which performance is judged.

Performance against the Company's peers

The Board also monitors the Company's performance with reference to its investment trust peer group.

Performance Attribution

The performance attribution is considered at each Board Meeting and enables the Directors to judge how the Company achieved its performance relative to the benchmark index and to see the impact on the Company's relative performance of factors including stock and sector allocation. A Performance Attribution Analysis for the year ended 31 January 2008 is given on page 4.

Discount to net asset value ("NAV")

The Board has a share buy back programme which has a role to play in enhancing the NAV for existing shareholders, as shares are bought back at a discount, and in minimising the volatility of movements in the discount. In the year to 31 January 2008 the shares traded between a discount of -5% and a discount of -14% with debt at fair value.

Directors' Report

Total expense ratio ("TER")

The most significant expense for the Company is the cost of the management fee and the costs of interest on the Company's borrowings. Other expenses include the costs of investment transactions, directors' fees and insurance, professional advice and regulatory fees and the costs of production of the reports to shareholders. The TER is calculated by dividing operating expenses by total assets less current liabilities, that is, the Company's management fee and all other operating expenses (including tax relief, where allowable, but excluding interest payments) as a percentage of assets at the year end. The TER for the year ended 31 January 2008 was 0.51% (2007 0.46%).

Revenue

The return attributable to Ordinary Shareholders for the year amounted to £23,649,820 (2007 – £22,854,005).

Earnings per ordinary dividend amounted to 22.86p. The first and second interim dividends of 5.4p and 5.4p respectively have been paid during the year. Since the year end the third interim dividend of 5.4p has been paid. The final proposed dividend of 5.4p is payable on 14 May 2008. In accordance with FRS 21 'Events after the Balance Sheet Date', the third and final dividends are not recognised as liabilities within the financial statements.

Historical Record

The distribution of total assets is shown on pages 11 and 12, and the historical record of the Company's revenue, capital and invested funds over the past ten years is shown on page 4. Graphs appear on page 13 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.

Invested Funds

Sales of investments during the year resulted in net gains based on historical costs of £34,315,606 (2007 – £53,443,663). Provisions contained in the Finance Act 1980 exempt approved Investment Trusts from corporation tax on their chargeable gains. Invested funds at 31 January 2008 had a value of £608,450,967 (2007 – £695,769,971) before deducting net liabilities of £102,263,754 (2007 – £106,935,296).

Principal Risks and Uncertainties

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

Investment Activity and Strategy

An inappropriate investment strategy, e.g., asset allocation or the level of gearing, may lead to under-performance against the Company's benchmark index and peer group companies, and also in the Company's shares trading on a wider discount. The Board manages these risks by diversification of investments through its investment restrictions and guidelines which are monitored and on which the Board receives reports. RCM (UK) Limited ("RCM") provides the Directors with management information including performance data and reports and shareholder analyses. The Board monitors the implementation and results of the investment process with the investment managers, who attend all board meetings, and reviews data which show risk factors and how they affect the portfolio. The Board reviews investment strategy at each board meeting.

Portfolio and Market

Market risk arises from uncertainty about the future prices of the Company's investments. This is commented on in Note 20 on pages 46 to 50. The Board monitors the implementation and results of the investment process with the investment managers.

Accounting, Legal and Regulatory

In order to qualify as an investment trust the Company must comply with Section 842 of the Income and Corporation Taxes Act 1988 ("Section 842"), and details are given above under the heading 'Business of the Company'. A breach of Section 842 could result in the Company losing investment trust status and, as a consequence, gains in the Company's portfolio would be subject to Corporation Tax. The Section 842 criteria are monitored by RCM and results are reported to the Board at each Board Meeting. The Company must comply with the provisions of the Companies Act 1985, and the Companies Act 2006 as it becomes enacted ("Companies Acts"), and, as the Company's shares are listed on the London Stock Exchange, the Company must comply with the UK Listing Authority's Listing Rules and Disclosure Rules ("UKLA Rules"). A breach of the Companies Acts could result in the Company and/or the Directors being fined or becoming the subject of criminal proceedings. Breach of the UKLA Rules could result in the suspension of the Company's shares which would in turn lead to a breach of Section 842. The Board relies on its company

Directors' Report

secretary and its professional advisers to ensure compliance with the Companies Acts and UKLA Rules.

Corporate Governance and Shareholder Relations

Details of the Company's compliance with Corporate Governance best practice, including information on relations with shareholders, are set out in the Corporate Governance Statement on page 24 to 27.

Operational

Disruption to, or failure of, RCM's accounting, dealing or payment systems or the custodian's records may prevent accurate reporting and monitoring of the Company's financial position. RCM has contracted operational functions, principally relating to trade processing and investment administration, to The Bank of New York Mellon – London Branch. Details of how the Board monitors the services provided by RCM and other suppliers and the key elements designed to provide effective internal control are included within the Internal Control section of the Corporate Governance Statement on pages 26 and 27.

Financial

The Directors have reviewed the Manager's statements on the risks associated with the Company and concur with their opinion on these risks. Further analysis of these risks can be found in Note 20 on pages 46 to 50.

Future Development

The future development of the Company is dependent on the success of the Company's investment strategy against the economic environment and market developments. The investment manager discusses his view of the outlook for the Company's portfolio in his report beginning on page 5.

Net Asset Value

The Net Asset Value of the Ordinary Shares of 25p at the year end was 492.3p as compared with a value of 567.5p at 31 January 2007.

Share Capital

Details of the Company's share capital are set out in Note 11 on page 43.

Payment Policy

It is the Company's payment policy for the forthcoming financial year to obtain the best terms for all business and therefore there is no consistent policy as to the terms used. In general, the Company agrees with its suppliers the terms on which business will take place and it is our policy to abide by these terms. The Company had no trade creditors at the year end (2007 – £nil).

Donations and Subscriptions

There were no charitable donations and subscriptions in respect of the year (2007 – £nil). No political donations were made during the year.

Final Dividend

Subject to the final dividend being approved by shareholders at the Annual General Meeting, payment will be made on 14 May 2008 to shareholders on the Register of Members at the close of business on 11 April 2008 at the rate of 5.4p per Ordinary Share. Further details are provided in Note 6 on page 39.

Section 992 of the Companies Act 2006

The following information is disclosed in accordance with Section 992 of the Companies Act 2006.

Capital Structure

The Company's capital structure is summarised on page 43.

Voting Rights in the Company's Shares

The voting rights at 31 December 2007 were:

Share class	Number of shares issued	Voting rights per share	Total voting rights
Ordinary shares of 25p	102,813,464	1	102,813,464
3.65% Cumulative Preference shares of £1	1,178,000	1	1,178,000
Total	103,991,464		103,991,464

These figures remained unchanged at the date of this report.

Substantial Shareholdings

As at 11 April 2008 the following had declared a notifiable interest in the Company's issued share capital:

Ordinary Shares:

Name	Number of Shares	Percentage of Voting Rights
Rensburg Sheppards Investment Management Group Limited	4,524,860	4.4%
Legal & General Group PLC	3,427,541	3.3%

Directors' Report

3.65% Cumulative Preference Stock:

Name	Number of Shares	Percentage of Voting Rights
P. S. & J. M. Allen	185,582	15.8%
Prudential plc	176,000	14.9%
Ecclesiastical Insurance Office plc	134,690	11.4%
F&C Asset Management plc	60,000	5.1%
D. J. Edwards	50,000	4.2%
J. Y. Miller	36,000	3.0%

The rules concerning the appointment and replacement of directors, amendment of the Articles of Association and powers to issue or buy back the Company's shares are contained in the Articles of Association of the Company and the Companies Acts 1985 and 2006.

There are no restrictions concerning the transfer of securities in the Company; no special rights with regard to control attached to securities; no agreements between holders of securities regarding their transfer known to the Company; no agreements which the Company is party to that might affect its control following a takeover bid; and no agreements between the Company and its directors concerning compensation for loss of office.

Directors and Management

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

The Directors retiring by rotation at the Annual General Meeting are Sir Bob Reid, Joe Scott Plummer and Dick Barfield. Joe Scott Plummer and Dick Barfield each offers himself for re-election and both have the full support of the Board in doing so. Sir Bob Reid is retiring from the Board and does not offer himself for re-election. The Board confirms that, since the year end, the performances of Joe Scott Plummer and Dick Barfield have been subject to a formal evaluation and that each continues to be effective in, and to demonstrate commitment to, his role. The Board considers Joe Scott Plummer and Dick Barfield to be independent, notwithstanding their length of service, and continues to be of the view that their extensive experience and active knowledge of industry and financial services are of great benefit to the Board.

Michael McKeon and Henry Staunton will be appointed to the Board with effect from 1 May 2008. In accordance with the Articles, both will retire and each will offer himself for election at the Annual General Meeting.

Biographical details of the current Directors and of Michael McKeon and Henry Staunton are on page 14.

The current Directors and their beneficial interests in the share capital of the Company as at 31 January 2008 and 2007 or at the date of appointment to the Board are listed below:

	Ordinary Shares of 25p	
	2008	2007
R. A. Barfield	2,418	2,343
Sir Bob Reid	5,000	5,000
Sir James Sassoon	35,600	35,600
P. J. Scott Plummer	16,000	1,000
H. A. Stevenson	25,000	25,000

Since the year end, Mr R. A. Barfield has acquired a further 22 Ordinary Shares due to reinvestment of income in a share plan.

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

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

Management Contract and Management Fee

The management contract with RCM (UK) Limited ('RCM') provides for a fee of 0.35% per annum (2007 – 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 RCM. The management contract is terminable at one year's notice (2007 – one year).

The Manager's performance under the contract and the contract terms are reviewed at least annually by the Management Engagement Committee. This committee consists of the Directors not employed by the management company in the past five years and therefore includes the entire Board. During the year, the committee met the Manager to review the current investment framework, including the Trust's performance, marketing activity and total expense ratio.

The committee also reviewed the terms of the management contract and considered the level of the management fee, which it found to be appropriate. The committee was satisfied with its review and believes that the continuing appointment of the Managers is in the best interests of shareholders as a whole.

Directors' Report

Individual Savings Accounts/PEPs

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

Statement of Directors' Responsibilities

The Directors are responsible for preparing the Annual Financial Report, Directors' Remuneration Report and the financial statements in accordance with applicable law and United Kingdom Generally Accepted Accounting Practice. 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 profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to:

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

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the Annual Financial Report, Directors' Remuneration Report and 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 www.allianzglobalinvestors.co.uk, which is a website maintained by the Company's Investment Managers, RCM (UK) Limited. The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. The work undertaken by the Auditors does not involve consideration of the maintenance and integrity of the website 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 other jurisdictions.

Statement under DTR 4.1.12

The Directors at the date of the approval of this Report, each confirm to the best of their knowledge that:

- the financial statements, prepared in accordance with applicable accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company; and
- this Annual Financial Report includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that they face.

Directors' Report

Annual General Meeting

Summary of Revised Articles of Association to take effect from the date of the Annual General Meeting, conditional on the passing of Resolution 10

A copy of the proposed new Articles of Association is available from the Company Secretary on request (contact details are on page 55).

1 Articles which duplicate statutory provisions

Provisions in the current Articles which have the same effect as provisions contained in the Companies Act 2006 are to be amended in the new Articles to bring them into line with the Companies Act 2006. Some examples include provisions concerning the form of resolutions, the variation of class rights, the requirement to keep accounting records and provisions regarding the period of notice required to convene general meetings. The main changes made to reflect this approach are detailed below.

2 Form of resolution

The current Articles contain a provision that, where for any purpose an ordinary resolution is required, a special or extraordinary resolution is also effective and that, where an extraordinary resolution is required, a special resolution is also effective. This provision is being amended as the concept of extraordinary resolutions has not been retained under the Companies Act 2006.

3 Transfer of shares

Under the Companies Act 2006, a company must either register a transfer or give the transferee notice of, and reasons for, its refusal to register the transfer. Any registration of a transfer or notice of refusal must be made or given as soon as practicable and in any event within two months from the date that the transfer is lodged with the company. The proposed new Articles reflect these requirements.

4 Disclosure of interests

The provisions relating to the disclosure of interests in shares contained in the Companies Act 1985 ("the 1985 Act"), including Section 212 on company investigation powers, were repealed in January 2007. Section 793 and related sections in Part 22 of the 2006 Act, which contain the corresponding company investigation powers previously contained in Section 212, were brought into force simultaneously. The proposed new Articles reflect the replacement of Section 212 of the 1985 Act with Section 793 of the 2006 Act.

5 Convening extraordinary and annual general meetings

The provisions in the current Articles dealing with the convening of general meetings and the length of notice required to convene general meetings are being amended to conform to new provisions in the Companies Act 2006. In particular an extraordinary general meeting to consider a special resolution can be convened on 14 days' notice whereas previously 21 days' notice was required.

The proposed new Articles also deal with situations where, because of a postal strike or similar situation beyond the control of the Company, a notice of meeting is not received by a shareholder. The amendment will ensure that such failure does not invalidate proceedings at the meeting in question.

6 Quorum

The proposed new Articles have been amended to make it clear that two persons who are proxies for the same member or representatives of the same body corporate can constitute a quorum.

7 Attending and speaking at meetings

The proposed new Articles now provide that the chairman of the meeting may permit non-members or persons who are not entitled to exercise the rights of members to attend and, at the chairman's discretion, speak at a general meeting.

8 Polls

The proposed new Articles have been amended to clarify that a poll may be demanded before a show of hands, as well as immediately after the result of a show of hands, and to give the directors the right to demand a poll as well as the Chairman of the meeting.

9 Votes of members

Under the Companies Act 2006 proxies are entitled to vote on a show of hands as well as a poll, and members may appoint a proxy to exercise all or any of their rights to attend, speak and vote at meetings. Multiple proxies may be appointed provided that each proxy is appointed to exercise the rights attached to a different share or shares held by the shareholder and multiple corporate representatives may be appointed. The proposed new Articles reflect all of these new provisions and also take account of the ICSA's concerns in relation to Section 323 of the Companies Act 2006.

Directors' Report

10 Receipt of appointments of proxy and termination of proxy authority

The proposed new Articles provide that proxies for a poll to be taken after the date of a meeting or adjourned meeting must be received not less than 24 hours, or such shorter time as the directors may determine, before the time of the poll. The deadlines for receipt of termination of proxy authority have been brought into line with the deadlines for receipt of proxies. They also permit the directors to specify, in a notice of meeting, that in determining the time for delivery of proxies, no account shall be taken of non-working days.

11 Notices and other communications

The Companies Act 2006 enables companies to communicate with their members by electronic communication to a greater extent than previously permitted. The proposed new articles will provide the Company with a general power to send or supply any notice, document or information to any member by a variety of methods – in person, by post or in electronic form (such as by email), or by making it available on the Company's website. In addition to any notice, document or information which is specifically required to be sent or supplied under the 2006 Act, the Company will also be able to send any other document or information to members using this variety of methods.

The proposed new Articles allow proxies to be sent or supplied in electronic form and, where the Company gives an electronic address in a form of proxy, shareholders may send the appointment of proxy to that electronic address, subject to any conditions or limitations specified in the relevant notice of meeting.

There is no present intention to implement electronic communication with shareholders but general powers are being sought in accordance with changing market practice.

The Company may ask each member for his or her consent to receive communications from the Company via its website. If the member does not respond to the request for consent within 28 days, the Company may take that as consent by the member to receive communications in this way. If the Company sends or supplies any notice, document or information to members by making it available on the Company's website, it must notify each member who has consented (or is deemed to have consented) to receive documents via the website, either by post or by email (if the member has specifically agreed to receive communications in electronic form), that the notice, document or information has been placed on the website. A member who has consented or is deemed to have consented to receive communications via the website can request a hard copy of any document at any time. Members can also revoke their consent to receive electronic communications at any time.

In relation to joint holders of shares, the amended Articles provide that the agreement of the first-named holder on the register of members to accept notices, documents or information electronically or via a website shall be binding on the other joint holders. The new Articles would also permit the Company not to send or supply any notice, document or information to a member whose registered address is not in the United Kingdom unless that member gives a non-electronic address in the United Kingdom.

There are new provisions that cater for situations where the provision of corporate information in electronic form or via a website may amount to a breach of securities laws of another jurisdiction. The Company may send hard copies if it needs to restrict the circulation of information in certain circumstances, such as for US securities law reasons.

The proposed new Articles also deal with notices, documents or information sent by the Company to a member which have been returned undelivered on three consecutive occasions. The member will only be entitled to be sent further communications upon provision of a new postal or electronic address to the Company.

Further proposed provisions are included to deal with the validation of documents in electronic form by members where required by the Articles. In the case of notices of meetings or proxies, any validation requirements must be specified in the notice.

12 Directors' indemnities and loans to fund expenditure

The proposed new Articles contain provisions which take advantage of changes to the law relating to the Company's ability to give indemnities to the Directors and others. The changes allow the Company to provide its Directors with funds to cover the costs of defending legal proceedings brought against any director/directors or the directors collectively on an "as incurred" basis. Previously, a company could only fund a director's defence costs once final judgement in his/her favour had been reached. It is therefore proposed that the Company's Articles be amended so that the Company may fund the defence costs of current or former directors or other officers if an action were to be brought against them.

Directors' Report

13 Conflict of Interest Duties

The Companies Act 2006 sets out directors' general duties. The provisions largely codify the existing law, but with some changes. Under the Companies Act 2006, from 1 October 2008 a director must avoid a situation where he has, or can have, a direct or indirect interest that conflicts, or possibly may conflict with the Company's interests. The requirement is very broad and could apply, in some cases, if a director becomes a director of another company or a trustee of another organisation. The Companies Act 2006 allows directors of public companies to authorise conflicts and potential conflicts where the articles of association contain a provision to this effect. The Companies Act 2006 also allows the articles to contain other provisions for dealing with directors' conflicts of interest to avoid a breach of duty. The Articles have been amended so that they confirm that such interests, offices or employment will not infringe the conflicts duty as codified in the Companies Act 2006.

The proposed new Articles give the directors authority to approve conflict situations including other directorships held by the company's directors and include other provisions to allow conflicts of interest to be dealt with in a similar way to the current position.

There are safeguards which will apply when directors decide whether to authorise a conflict or potential conflict. First, only directors who have no interest in the matter being considered will be able to take the relevant decision, and secondly, in taking the decision the directors must act in a way they consider, in good faith, will be most likely to promote the Company's success. The directors will be able to impose limits or conditions when giving authorisation if they think this is appropriate. It is also proposed that the amended Articles should contain provisions relating to confidential information, attendance at board meetings and availability of board papers to protect a director being in breach of duty if a conflict of interest or potential conflict of interest arises. These provisions will only apply where the position giving rise to the potential conflict has previously been authorised by the directors.

It is the board's intention to report annually on the Company's procedures for ensuring that the board's powers of authorisation of conflicts are operated effectively and that the procedures have been followed.

14 Permitted interests and voting

The provisions which previously deemed certain interests of a director's connected persons to be the interests of the director himself for the purposes of this article have been deleted. There is no requirement in the Companies Act 2006 to include such a provision and this Act contains a much wider definition of "connected person" of a director. The director and the Company must still take a view each time a matter is being considered as to whether the interests of the director's connected persons mean that the director should be treated as interested for the purposes of this article.

15 Removal of age limit for directors

The provision requiring a director's age to be disclosed, in a notice of meeting at which that director is to be appointed or reappointed, if that director has attained the age of 70 years or more, has been removed from the proposed new Articles to reflect the repeal of the previous provisions regarding directors over 70 from the Companies Act 1985.

16 The seal

The proposed new Articles provides that instruments (other than share certificates) to which the seal is affixed shall be signed by two authorised persons or by a director in the presence of a witness, whereas previously the requirement was for signature by either the director and secretary or two directors.

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 are 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 £400 million). The rules of the UK Listing Authority ('Listing Rules') limit the price which may be paid by the Company to 105% of the average middle-market quotation for an Ordinary Share on the five business days immediately preceding the date of the relevant purchase. The minimum price to be paid will be 25p

Directors' Report

per Ordinary Share (being the nominal value). Overall, this proposed share buy-back authority, if used, should help to reduce the discount to net asset value at which the Company's shares currently trade.

The Board considers that it will be most advantageous to shareholders for the Company to be able to continue 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.

The Company's Articles of Association permit the Company to redeem or purchase its own shares out of capital profits. Under the Listing Rules, 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 15,411,738 Ordinary Shares, representing 14.99% of the issued share capital, provided that there is no change in the issued share capital between the date of this report and the Annual General Meeting to be held on 13 May 2008.

The authority will last until the Annual General Meeting of the Company to be held in 2009 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 and Disapplication of Pre-emption Rights

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 £8,567,788, representing approximately 33% of the existing Ordinary Share capital. This authority would expire five years from the date of renewal, if not previously revoked or varied.

A resolution was passed at the Annual General Meeting held on 14 May 2007 to authorise the Directors to allot the unissued Ordinary Share capital for cash. The authority is renewable annually and expires at the conclusion of the Annual General Meeting in 2008. A Special Resolution is therefore proposed under special business at the forthcoming Annual General Meeting to renew this authority for a further year.

The power to allot new Ordinary Shares for cash, other than pro rata to existing shareholders, is limited to the aggregate nominal amount of £1,285,168 Ordinary Share capital, being approximately five per cent of the issued Ordinary Share capital of the Company as at the date of this report, provided that there is no change in the issued share capital between the date of this report and the Annual General Meeting to be held on 13 May 2008.

The Directors do not currently intend to allot shares under these authorities other than to take advantage of opportunities in the market as they arise and only if they believe it would be advantageous to the Company's existing shareholders to do so. 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, valuing debt at market value.

Auditors

The Directors will place a resolution before the Annual General Meeting to re-appoint PricewaterhouseCoopers LLP as Auditors for the ensuing year. A resolution to authorise the Directors to determine the Auditors' remuneration will also be proposed at the Annual General Meeting.

By Order of the Board
K. J. Salt
Secretary

14 April 2008

Corporate Governance

The Board has considered the principles and recommendations of the AIC Code of Corporate Governance ("AIC Code") by reference to the AIC Corporate Governance Guide for Investment Companies ("AIC Guide"). The AIC Code, as explained by the AIC Guide, addresses all the principles set out in Section 1 of the Combined Code which was issued by the Financial Reporting Council in June 2006, as well as setting out additional principles and recommendations on issues that are of specific relevance to the Company. The Board considers that reporting against the principles and recommendations of the AIC Code, and by reference to the AIC Guide, will provide better information to shareholders. The Company has complied with the recommendations of the AIC Code and the relevant provisions of Section 1 of the Combined Code, except in relation to the Combined Code provisions relating to:

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

For the reasons set out in the AIC Guide, and in the preamble to the Combined Code, the Board considers these provisions are not relevant to the Company as it is an externally managed investment company. The Company has therefore not reported further in respect of these provisions.

The Board

The Board currently consists of five Directors, all of whom are non-executive and independent of the Company's investment manager. It is intended that there will be six directors after the Annual General Meeting. Their biographies, on page 14, demonstrate a breadth of investment, industrial, commercial and professional experience.

The Chairman of the Company is a non-executive Director and Joe Scott Plummer was appointed as the Senior Independent Director in March 2005.

The Board follows the AIC Code and considers Joe Scott Plummer and Dick Barfield, to be independent, notwithstanding that each has served on the Board for more than nine years. The Board does not consider that length of service has diminished the independence of these directors and continues to be of the view that their extensive experience and active knowledge of the industry is of great benefit to the Board.

The composition of the Board is reviewed regularly. Two new directors will be appointed with effect from 1 May 2008, Michael McKeon and Henry Staunton. This follows an exercise in which external recruitment consultants were appointed to draw up a shortlist of candidates.

The Board's tenure policy is that new Directors stand for election at the first Annual General Meeting following their appointment and then at least one third of Directors retire by rotation at each Annual General Meeting. Every Director is required to seek re-election at least every three years and annually after nine years' service. The names of the Directors retiring by rotation and those other Directors retiring in accordance with the Articles of Association at this year's Annual General Meeting are given on page 18.

The Board meets at least six times a year and convenes other meetings as and when required. Between meetings, regular contact with the investment managers is maintained. The Board has a schedule of matters reserved for its approval to ensure it has full and effective control over appropriate issues. These issues include approval of the Company's investment policy, capital structure, share price and discount, committee membership and terms of reference, financial reporting, risk management, board appointments and removals, corporate governance, internal controls and contracts. A procedure has been 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 the Company complies with applicable rules and regulations. 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 regulatory and statutory requirements and internal financial controls. Changes affecting Directors' responsibilities are advised to the Board as they arise.

During the year, the effectiveness of the Board was assessed through interviews conducted by the Chairman with each Director. In addition, the performance of the Directors was evaluated by each Director, followed by a discussion with the Chairman. The Chairman's own performance was evaluated by the other Directors, who met under the chairmanship of Joe Scott Plummer as Senior Independent Director. The results of the effectiveness assessment and performance evaluation have been presented to the Nomination Committee.

The effectiveness assessment determined that with the planned recruitment of new Directors the balance of the Board was satisfactory.

Corporate Governance

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 full and proper consideration by the Board of the quality and cost of services offered, including the financial 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. The Board's statement on its review of the management contract appears on page 18.

Attendance by Directors at formal Board and committee meetings during the year was as follows:

Director	Board	Audit Committee	Nomination Committee	Management Engagement Committee
No. of meetings	6	2	1	1
H. A. Stevenson	6	2*	1	1
Sir John Banham#	–	–	–	–
R. A. Barfield	6	2	1	1
Sir Bob Reid	5	1	–	–
Sir James Sassoon	6	2	1	1
P. J. Scott Plummer	5	2	1	1

*Invited to attend meetings, although not a committee member.

#Retired from the board in May 2007.

Board Committees

Audit Committee

The Audit Committee consists of all of the independent non-executive Directors, with the exception of the Chairman, and has defined terms of reference and duties. The role of the Audit Committee is to assist the Board in relation to the reporting of financial information. The Audit Committee is chaired by Sir James Sassoon. The committee considers that, collectively, its members have sufficient recent and relevant financial experience to discharge their responsibilities fully. The committee meets at least twice each year and reviews the annual and half yearly financial statements and considers the Auditors' report on the annual accounts, the planning and the process of the audit and the Auditors' independence and objectivity. It has also considered the non-audit services provided by the Auditors and determined that they have had no impact on the Auditors' independence and objectivity. The Audit Committee reviews the Company's accounting policies and considers their appropriateness. The Committee also reviews the terms of appointment of the Auditors together with their remuneration. It meets representatives of the Managers twice-yearly and receives reports on the internal controls maintained on behalf of the Company and reviews the effectiveness of these controls. The Audit Committee continues to believe that the Company does not require an internal audit function of its own as it delegates its day to day operations to third parties from whom it receives internal controls reports.

As the Company has no employees it does not have a formal policy concerning the raising, in confidence, of any concerns about improprieties, whether in matters of financial reporting or otherwise, for appropriate independent investigation. The Audit Committee has, however, received and noted the Manager's policy on this matter.

Nomination Committee

The Nomination Committee meets at least once each year and makes recommendations on the appointment of new Directors and the re-election of existing Directors by shareholders. The committee also determines the process for the annual evaluation of the Board. The Committee is chaired by Hugh Stevenson, the Chairman of the Board. All Directors serve on the committee and consider nominations made in accordance with an agreed procedure.

Management Engagement Committee

The Management Engagement Committee meets at least once each year to review the Management Agreement and the Manager's performance. It has defined terms of reference and consists of the non-executive Directors and excludes any Directors previously employed by the Managers. It is chaired by Hugh Stevenson, the Chairman of the Board.

The Board has not constituted a Remuneration Committee; all Directors are non-executive and remuneration matters are dealt with by the whole Board.

The Terms of Reference for each of the committees may be viewed by shareholders on request and are published on the website www.merchantstrust.co.uk.

Financial Reporting

The Statement of Directors' Responsibilities in respect of the financial statements is on page 19.

The Independent Auditors' Report can be found on pages 29 and 30.

Corporate Governance

Auditors' Information

Each of the persons who is a Director at the date of approval of this report confirms that:

(a) in so far as the Director is aware, there is no relevant audit information of which the Company's auditors are unaware; and

(b) the Director has taken all the steps he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 234ZA of the Companies Act 1985.

Going Concern

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

Internal Control

The Directors have overall responsibility for the Company's system of internal control. 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 a 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 Internal Control Guidance for Directors in the Combined Code published in September 1999 and revised in October 2005 ("the Turnbull guidance"). The process has been fully in place throughout the year under review and up to the date of signing of this Annual Financial Report.

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 Manager, undertook a full review of the Company's business risks and these are analysed and recorded in a risk matrix. Every six months the Board receives from the Manager a formal report which details any known internal controls failures, including those that are not directly the responsibility of the Manager. 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 RCM (UK) Limited ('RCM') as the Manager provides investment management, accounting and company secretarial services to the Company. The Manager therefore maintains 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 Manager. The Manager's 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 its internal audit department. RCM is regulated by the Financial Services Authority ('FSA') and its compliance department regularly monitors compliance with FSA rules. The Company receives reports at least annually from the manager on its internal controls. The Company, in common with other investment trusts, has no internal audit department, but the effectiveness of the Manager's internal controls is monitored by Allianz Global Investors' internal audit function.

- There is a regular review by the Board of asset allocation and any risk implications. There is also regular and comprehensive review by the Board of management accounting information including revenue and expenditure projections, actual revenue against projections and performance comparisons.

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

- The Audit Committee assesses the Manager's and Custodian's systems of controls and approves the appointment of any sub-custodians. The Audit Committee also receives reports from the Manager's and Custodian's internal auditors, compliance department and independent Auditors.

Corporate Governance

- The Board reviews the Internal Control reports of the Managers and third party service providers, including those of the Company's Registrars, Capita Registrars, and Custodian, HSBC Bank plc.

The Directors confirm that the Audit Committee has reviewed the effectiveness of the system of internal control. During the course of its review of the system of internal control, the Board has not identified nor been advised of any failings or weaknesses which it has determined to be significant.

Relations with Shareholders

The Board strongly believes that the annual general meeting should be an event which private shareholders are encouraged to attend. 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 at the meeting. The number of proxy votes cast in respect of each resolution will be made available at the annual general meeting.

The Manager meets with institutional shareholders on a regular basis and report to the Board on matters raised at these meetings.

All correspondence with shareholders is reviewed by the Board.

Shareholders who wish to communicate directly with the Chairman, the Senior Independent Director or other Directors may write care of the Company Secretary at 155 Bishopsgate, London EC2M 3AD.

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

Corporate Social Responsibility and Environmental Policy

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

The Board has noted the Manager's views on Social Responsibility that it adheres to in engaging with the underlying investee companies and in exercising its delegated responsibilities in voting. These are that:

> "We believe that good corporate governance includes the management of the company's impacts on society and the environment, as these are increasingly becoming a factor in contributing towards maximising long term shareholder value."

Exercise of Voting Powers

The Company's investments are held in a nominee name. The Board has delegated discretion to discharge its responsibilities in respect of investments, including the exercise of voting powers on its behalf, to the Manager.

The Board has noted the Manager's statement of its corporate governance aims and objectives, summarised as:

> "Our primary corporate aim is to maximise shareholder value through the securing of corporate performance whilst protecting this value through operating within established rules of conformance.
>
> Our primary investment management aim is to meet or exceed our clients' expectations through generating first class returns within the constraint of their risk tolerance.
>
> RCM votes in all markets wherever possible, and strives actively to encourage both improved levels of disclosure among companies and proper voting infrastructure among custodians and agents globally."

In the UK, RCM is a member of the National Association of Pension Funds (NAPF) and the International Corporate Governance Network (ICGN), and abides by these organisations' founding principles. These guidelines also take into account international codes of corporate governance from a number of sources, including Employment Retirement Income Security Act (ERISA) legislation and Department of Labor recommendations in the U.S. where appropriate.

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.

An extract from the Trust's voting record in the previous calendar year will be available for inspection at the annual general meeting each year.

Directors' Remuneration Report

This report is submitted in accordance with Schedule 7A of the Companies Act 1985 for the year ended 31 January 2008.

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

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, bonuses, pension benefits, share options or other benefits and fees are not related to the individual Director's 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 £150,000 per annum. Subject to this overall limit, it is the Board'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. The Board believes that levels of remuneration should be sufficient to attract and retain non-executive directors to oversee the Company.

Directors' and officers' liability insurance cover is held by the Company. Following the approval of the proposal at last year's Annual General Meeting to change the Company's Articles of Association to enable the Company to grant indemnities to the Directors individually, deeds of indemnity have been entered into with the Directors.

Remuneration

The policy is to review Directors' fees from time to time, but reviews will not necessarily result in a change to the rates. As disclosed in last year's report, in the year under review the Directors were paid at a rate unchanged since June 2006 of £15,000 per annum, with an additional £2,000 payable to the Audit Committee Chairman. The Chairman of the Board was paid at a rate of £25,000 per annum. These rates will be increased with effect from 1 June 2008 to £18,000 per annum for the Directors, with the Audit Committee Chairman receiving an additional £3,000, and £27,500 per annum for the Chairman of the Board.

Directors' Emoluments (Audited)

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

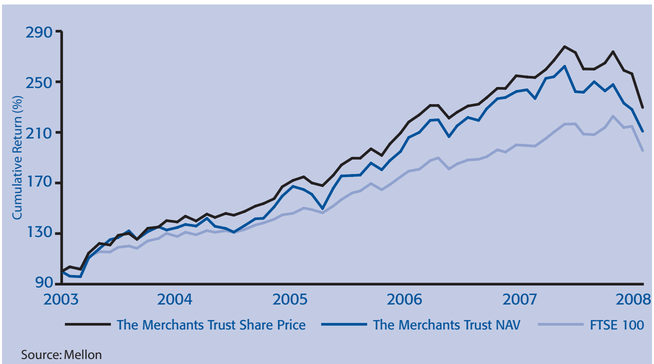
The Directors' Emoluments during the year and in the previous year are as follows:

	Directors' fees	
	2008	2007
	£	£
H. A. Stevenson	25,000	23,334
Sir John Banham	4,327	14,000
R. A. Barfield	15,000	14,000
Sir Bob Reid	15,000	14,000
Sir James Sassoon	17,000	9,062
P. J. Scott Plummer	15,000	15,554
Totals	91,327	89,950

Performance Graph

The graph below measures the Company's share price and net asset value performance against its benchmark index of the FTSE 100 Index.

The Company's performance is measured against the FTSE 100 Index as this is the most appropriate comparator in respect of its asset allocation. An explanation of the Company's performance is given in the Chairman's Statement and the Investment Managers' Review.



By Order of the Board
K. J. Salt
Secretary
14 April 2008

Independent Auditors' Report

Independent Auditors' Report to the Members of The Merchants Trust PLC

We have audited the financial statements of The Merchants Trust PLC for the year ended 31 January 2008 which comprise the Income Statement, the Reconciliation of Movements in Shareholders' Funds, the Balance Sheet, the Cash Flow Statement, and the related notes. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

Respective responsibilities of directors and auditors

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

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing. The information given in the Directors' Report includes that specific information presented in the Investment Managers' Report and other sections of the Annual Financial Report that is cross-referred from the Business Review section of the Directors' Report.

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 part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We review whether the Corporate Governance Statement reflects the company's compliance with the nine provisions of the Combined Code 2006 specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the company's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Financial Report and consider whether it is consistent with the audited financial statements. The other information comprises only the Key Facts, Performance Attribution Analysis, Chairman's Statement, Historical Record, Investment Managers' Review, Listed Holdings, Distribution of Total Assets, Performance Graphs, the Directors' Report, the Corporate Governance Statement and the unaudited part of the Directors' Remuneration Report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the 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 part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Directors' Remuneration Report to be audited.

Independent Auditors' Report

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 January 2008 and of its net return and cash flows for the year then ended;
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London

14 April 2008

Income Statement
for the year ended 31 January 2008

	Note	2008 Revenue Return £	2008 Capital Return £	2008 Total Return £	2007 Revenue Return £	2007 Capital Return £	2007 Total Return £
Net (losses) gains on investments at fair value	8	–	(72,106,540)	(72,106,540)	–	71,440,601	71,440,601
Income	1	28,495,032	–	28,495,032	27,750,450	–	27,750,450
Investment management fee	2	(899,044)	(1,669,652)	(2,568,696)	(961,650)	(1,785,921)	(2,747,571)
Administration expenses	3	(585,839)	(2,560)	(588,399)	(488,138)	(3,021)	(491,159)
Net return before finance costs and taxation		27,010,149	(73,778,752)	(46,768,603)	26,300,662	69,651,659	95,952,321
Finance costs: interest payable and similar charges	4	(3,342,277)	(6,116,736)	(9,459,013)	(3,446,657)	(6,321,084)	(9,767,741)
Net return on ordinary activities before taxation		23,667,872	(79,895,488)	(56,227,616)	22,854,005	63,330,575	86,184,580
Taxation on ordinary activities	5	(18,052)	–	(18,052)	–	–	–
Net return on ordinary activities attributable to Ordinary Shareholders		23,649,820	(79,895,488)	(56,245,668)	22,854,005	63,330,575	86,184,580
Return per Ordinary Share (basic and diluted)	7	22.86p	(77.23p)	(54.37p)	22.17p	61.44p	83.61p

Dividends in respect of the financial year ended 31 January 2008 total 21.60p (2007 – 20.00p), costing £22,278,168 (2007 – £20,745,854). Details are set out in Note 6 on page 39.

The total return column of this statement is the profit and loss account of the Company. The supplementary revenue return and capital return columns are both prepared under the guidance published by the Association of Investment Companies.

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

A Statement of Total Recognised Gains and Losses is not required as all gains and losses of the Company have been reflected in the above statement.

The Notes on pages 35 to 50 form an integral part of these Financial Statements.

Reconciliation of Movements in Shareholders' Funds

for the year ended 31 January 2008

	Note	Called up Share Capital £	Share Premium Account £	Capital Redemption Reserve £	Capital Reserve Realised £	Capital Reserve Unrealised £	Revenue Reserve £	Total £
Net Assets at 31 January 2006		25,525,984	39,809	56,250	351,107,802	118,104,550	19,878,801	514,713,196
Revenue Return		–	–	–	–	–	22,854,005	22,854,005
Dividends on Ordinary Shares	6	–	–	–	–	–	(19,964,324)	(19,964,324)
Capital Return		–	–	–	50,187,850	13,142,725	–	63,330,575
Shares issued during the year		413,985	7,487,238	–	–	–	–	7,901,223
Net Assets at 31 January 2007	11	25,939,969	7,527,047	56,250	401,295,652	131,247,275	22,768,482	588,834,675
Net Assets at 31 January 2007		25,939,969	7,527,047	56,250	401,295,652	131,247,275	22,768,482	588,834,675
Revenue Return		–	–	–	–	–	23,649,820	23,649,820
Dividends on Ordinary Shares	6	–	–	–	–	–	(21,757,822)	(21,757,822)
Capital Return		–	–	–	34,707,261	(114,602,749)	–	(79,895,488)
Shares repurchased during the year	11	(236,603)	–	236,603	(4,643,972)	–	–	(4,643,972)
Net Assets at 31 January 2008		25,703,366	7,527,047	292,853	431,358,941	16,644,526	24,660,480	506,187,213

The Notes on pages 35 to 50 form an integral part of these Financial Statements.

Balance Sheet
as at 31 January 2008

	Note	2008 £	2008 £	2007 £
Fixed Assets				
Investments held at fair value through profit or loss	8		608,450,967	695,769,971
Current Assets				
Debtors	10	7,333,938		2,836,903
Cash at bank	10	5,945,385		7,003,101
		13,279,323		9,840,004
Creditors: Amounts falling due within one year	10	(2,129,286)		(3,227,220)
Net Current Assets			11,150,037	6,612,784
Total Assets Less Current Liabilities			619,601,004	702,382,755
Creditors: Amounts falling due after more than one year	10		(113,413,791)	(113,548,080)
Total Net Assets			506,187,213	588,834,675
Capital and Reserves				
Called up Share Capital	11		25,703,366	25,939,969
Share Premium Account			7,527,047	7,527,047
Capital Redemption Reserve	12		292,853	56,250
Capital Reserves: Realised	13	431,358,941		401,295,652
Unrealised	13	16,644,526		131,247,275
			448,003,467	532,542,927
Revenue Reserve	14		24,660,480	22,768,482
Equity Shareholders' Funds	15		506,187,213	588,834,675
Net Asset Value per Ordinary Share	15		492.3p	567.5p

The financial statements on pages 31 to 50 were approved and authorised for issue by the Board of Directors on 14 April 2008 and signed on its behalf by

Hugh Stevenson
Chairman

The Notes on pages 35 to 50 form an integral part of these Financial Statements.

Cash Flow Statement
for the year ended 31 January 2008

	Note	2008 £	2008 £	2007 £
Net cash inflow from operating activities	18		33,677,949	28,262,666
Returns on investment and servicing of finance				
Interest paid		(9,553,292)		(9,530,065)
Dividends on Preference Stock		(42,997)		(42,997)
Net cash outflow from servicing of finance			(9,596,289)	(9,573,062)
Capital expenditure and financial investment				
Purchases of fixed asset investments		(188,448,230)		(236,518,625)
Sales of fixed asset investments		189,710,648		238,513,660
Net cash inflow from capital expenditure and financial investment			1,262,418	1,995,035
Equity dividends paid	6		(21,757,822)	(19,964,324)
Net cash inflow before financing			3,586,256	720,315
Financing				
Purchase of Ordinary Shares for cancellation	11		(4,643,972)	–
Cash transferred from Allianz Dresdner Income Growth Investment Trust plc in connection with the issue of Ordinary Shares			–	907,990
(Decrease) Increase in cash	19		(1,057,716)	1,628,305

The Notes on pages 35 to 50 form an integral part of these Financial Statements.

Statement of Accounting Policies
for the year ended 31 January 2008

1. The financial statements have been prepared under the historical cost convention, modified to include the revaluation of investments, and in accordance with the United Kingdom law, United Kingdom Generally Accepted Accounting Practice (UK GAAP) and the Statement of Recommended Practice – 'Financial Statements of Investment Trust Companies' (SORP) revised in December 2005 by the Association of Investment Companies.

   In order better to reflect the activities of an investment trust company and in accordance with guidance issued by the AIC, supplementary information which analyses the Income Statement between items of a revenue and capital nature has been presented alongside the Income Statement. In accordance with the Company's status as a UK investment company under section 266 of the Companies Act 1985, net capital returns may not be distributed by way of dividend.

2. Revenue – Dividends on equity shares are accounted for on an ex-dividend basis. UK dividends are shown net of tax credits.

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

   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 stocklending fees are accounted for on an accruals basis. Underwriting commission is recognised when the issue underwritten closes.

3. Investment management fees and administrative expenses – 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 Board's investment policy and prospective split of capital and income returns. Other administrative expenses are charged in full to revenue, except handling charges which are charged to capital. All expenses are recognised on an accrual basis.

4. Valuation – As the Company's business is investing in financial assets with a view to profiting from their total return in the form of increases in fair value, investments are designated as held at fair value through profit or loss on initial recognition in accordance with FRS 26 'Financial Instruments: Recognition and Measurement'. The Company manages and evaluates the performance of these investments on a fair value basis in accordance with its investment strategy, and information about the investments is provided on this basis to the Board of Directors.

   Investments held at fair value through profit and loss are initially recognised at fair value. After initial recognition, these continue to be measured at fair value, which for quoted investments is either the bid price or the last traded price depending on the convention of the exchange on which the investment is listed. The unrealised Capital Reserve reflects differences between fair value and book cost. Net gains and losses on the realisation of investments are recognised in the capital column of the Income Statement and are taken to the realised Capital Reserve.

5. Finance costs – In accordance with the Financial Reporting Standard 25 'Financial Instruments: Disclosure and Presentation' and FRS 26 'Financial Instruments: Recognition and Measurement', long term borrowings are stated at the amount of net proceeds on issue plus accrued finance costs to date. Finance costs are calculated over the term of the debt on the effective interest rate basis.

   Where debt is issued at a premium, the premium is amortised over the term of the debt on the effective interest rate basis.

Statement of Accounting Policies
for the year ended 31 January 2008

Finance costs net of amortised premiums are charged to capital and revenue in the ratio 65:35 to reflect the Board's investment policy and prospective split of capital and revenue returns.

Dividends payable on the 3.65% Cumulative Preference Stock are classified as an interest expense and are charged in full to revenue.

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.

   Deferred taxation is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date, where transactions or events that result in an obligation to pay more tax or a right to pay less tax in the future have occurred. Timing differences are differences between the Company's taxable profits and its results as stated in the financial statements.

   A deferred tax asset is recognised when it is more likely than not that the asset will be recoverable. Deferred tax is measured on a non-discounted basis at the rate of Corporation tax that is expected to apply when the timing differences are expected to reverse.

7. Foreign currency – In accordance with FRS 23 'The effect of changes in Foreign Currency Exchange Rates', the Company is required to nominate a functional currency, being the currency in which the Company predominately operates. The functional and reporting currency is pound sterling, reflecting the primary economic environment in which the Company operates. 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. Dividends – In accordance with FRS 21 'Events after the Balance Sheet Date', the final dividend payable on Ordinary Shares is recognised as a liability when approved by shareholders. Interim dividends are recognised only when paid.

9. Preference Stock – Following the introduction of FRS 25 'Financial Instruments: Disclosure and Presentation', the 3.65% Cumulative Preference Stock is classified as a liability as the rights of the stockholders to receive dividend payments are not calculated by reference to the Company's profits.

10. Shares repurchased and subsequently cancelled – Share Capital is reduced by the nominal value of the shares repurchased, and the Capital Redemption Reserve is correspondingly increased in accordance with Section 170 Companies Act 1985. The full cost of the repurchase is charged to the realised Capital Reserve.

11. FRS 29 'Financial Instruments: Disclosures introduces additional disclosures relating to financial instruments. This standard does not have any impact on the classification and/or valuation of the Company's financial instruments. The additional disclosures provided in accordance with the requirements of the standard are set out in Note 20 to the financial statements.

Notes to the Financial Statements

for the year ended 31 January 2008

1. Income

	2008 £	2008 £	2007 £
Income from investments:*			
Franked income:			
Equity income from UK investments†		28,043,754	27,334,101
Income from fixed interest securities		–	7,325
Unfranked income:			
Equity income from UK investments		77,388	–
		28,121,142	27,341,426
Other income:			
Deposit interest	350,513		274,898
Underwriting commission	–		124,962
Stocklending fees	23,377		9,164
		373,890	409,024
Total income		28,495,032	27,750,450

*All equity income is derived from listed investments.
†Includes special dividends of £502,450 (2007 – £1,302,224).

2. Investment Management Fee

	2008 £ Revenue	2008 £ Capital	2008 £ Total	2007 £ Revenue	2007 £ Capital	2007 £ Total
Investment management fee	899,044	1,669,652	2,568,696	961,650	1,785,921	2,747,571

The management contract with RCM (UK) Limited ('RCM'), terminable at one year's notice, provides for a management fee based on 0.35% (2007 – 0.35%) per annum of the value of the Company's assets calculated monthly after deduction of current liabilities, short term loans under one year and any funds within the portfolio managed by RCM. The amounts stated include VAT of £108,856 (2007 – £409,213). Due to the ECJ ruling in the VAT case brought by JP Morgan Fleming Claverhouse Trust plc in conjunction with the AIC on 28 June 2007, VAT has not been charged on management fees since 1 May 2007. Under the contract, RCM provides the Company with investment management, accounting, secretarial and administration services.

3. Administration Expenses

	2008 £	2007 £
Auditors' remuneration:		
for audit services	24,087	21,626
for non-audit services	3,525	3,525
	27,612	25,151
Directors' fees	91,327	89,950
Marketing costs of Share Plan	165,276	76,907
Other administrative expenses	301,624	296,130
	585,839	488,138

(i) The above expenses include value added tax where applicable.
(ii) Directors' fees are set out in the Directors' Remuneration Report on page 28.
(iii) Auditors' remuneration includes VAT of £4,113 (2007 – £3,763). Auditors' remuneration for non-audit services represents fees for reviewing compliance with loan covenants.

Notes to the Financial Statements

for the year ended 31 January 2008

4. Finance Costs: Interest Payable and Similar Charges

	2008 £ Revenue	2008 £ Capital	2008 £ Total	2007 £ Revenue	2007 £ Capital	2007 £ Total
On Stepped Rate Interest Loan repayable after more than five years	1,338,486	2,485,760	3,824,246	1,445,140	2,683,832	4,128,972
On Fixed Rate Interest Loan repayable after more than five years	1,312,402	2,437,318	3,749,720	1,315,731	2,443,501	3,759,232
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	623,489	1,157,908	1,781,397	623,539	1,158,001	1,781,540
On 3.65% Cumulative Preference Stock repayable after more than five years	42,997	–	42,997	42,997	–	42,997
On Sterling overdraft	5,653	–	5,653	–	–	–
	3,342,277	6,116,736	9,459,013	3,446,657	6,321,084	9,767,741

5. Taxation

	2008 £ Revenue	2008 £ Capital	2008 £ Total	2007 £ Revenue	2007 £ Capital	2007 £ Total
(a) Analysis of tax charge for the year:						
Overseas taxation	18,052	–	18,052	–	–	–
Current tax charge	18,052	–	18,052	–	–	–
(b) Factors affecting the current tax charge for the year:						
Return on ordinary activities before taxation	23,667,872	(79,895,488)	(56,227,616)	22,854,005	63,330,575	86,184,580
Tax on return on ordinary activities at 30% (2007 – 30%)	7,100,362	(23,968,646)	(16,868,284)	6,856,201	18,999,173	25,855,374
Reconciling factors:						
Non taxable income	(8,413,126)	–	(8,413,126)	(8,200,230)	–	(8,200,230)
Non taxable capital losses (gains)	–	21,631,962	21,631,962	–	(21,432,180)	(21,432,180)
Disallowable expenses	62,629	492	63,121	69,595	63,350	132,945
Excess of allowable expenses over taxable income	1,250,135	2,336,192	3,586,327	1,274,434	2,369,657	3,644,091
Overseas tax suffered	18,052	–	18,052	–	–	–
Current tax charge	18,052	–	18,052	–	–	–

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 £114.2m (2007 – £102.2m). Given the Company's current investment strategy, it is unlikely to generate sufficient UK taxable profits to relieve these expenses.

As at 31 January 2008 there is an unrecognised deferred tax asset of £32.0m (2007 – £30.7m). This deferred tax asset relates to the current and prior year unutilised expenses. It is considered unlikely that there will be a liability in the future against which the deferred tax asset can be offset. Therefore, the tax asset has not been recognised.

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

Notes to the Financial Statements
for the year ended 31 January 2008

6. Dividends on Ordinary Shares

	2008 £	2007 £
Dividends on Ordinary Shares of 25p each:		
Third interim dividend 5.1p paid 16 February 2007 (2006 – 4.8p)	5,291,754	4,900,989
Final dividend 5.1p paid 16 May 2007 (2006 – 4.8p)	5,291,754	4,900,989
First interim dividend 5.4p paid 16 August 2007 (2006 – 4.9p)	5,596,931	5,084,234
Second interim dividend 5.4p paid 15 November 2007 (2006 – 4.9p)	5,577,383	5,084,234
Prior period uncollected dividends	–	(6,122)
	21,757,822	19,964,324

Dividends payable at the year end are not recognised as a liability under FRS 21 'Events after the Balance Sheet Date' (see pages 35 and 36 Statement of Accounting Policies). Details of these dividends are set out below.

	2008 £	2007 £
Third interim dividend 5.4p payable 13 February 2008 (2007 – 5.1p)	5,551,927	5,291,754
Final proposed dividend 5.4p payable 14 May 2008 (2007 – 5.1p)	5,551,927	5,291,754
	11,103,854	10,583,508

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 cancellations of shares by the Company settled subsequent to the year end.

Ordinary dividends paid by the Company carry a tax credit at a rate 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.

7. Return per Ordinary Share

	2008 £ Revenue	2008 £ Capital	2008 £ Total Return	2007 £ Revenue	2007 £ Capital	2007 £ Total Return
Return attributable to Ordinary Shareholders	23,649,820	(79,895,488)	(56,245,658)	22,854,005	63,330,575	86,184,580
Return per Ordinary Share	22.86p	(77.23p)	(54.37p)	22.17p	61.44p	83.61p

The weighted average number of shares in issue during the year was 103,451,633 (2007 – 103,083,890).

Notes to the Financial Statements
for the year ended 31 January 2008

8. Fixed Asset Investments

	2008 £	2007 £
Listed on The London Stock Exchange at market valuation	608,423,542	695,742,546
Unlisted at fair value	27,425	27,425
Total fixed asset investments	608,450,967	695,769,971
Market value of investments brought forward	695,769,971	621,948,270
Unrealised gains brought forward	(131,247,275)	(118,104,550)
Cost of investments held brought forward	564,522,696	503,843,720
Additions at cost	187,418,494	244,541,594
Disposals at cost	(160,134,749)	(183,862,618)
Cost of investments held at 31 January	591,806,441	564,522,696
Unrealised gains at 31 January	16,644,526	131,247,275
Market value of investments held at 31 January	608,450,967	695,769,971
Net (losses) gains on investments		
Net realised gains based on historical costs	34,315,606	53,443,663
Adjustment for net unrealised gains recognised in previous years	(42,276,719)	(37,189,607)
Net realised (losses) gains based on carrying value at previous balance sheet date	(7,961,113)	16,254,056
Net unrealised (losses) gains arising in the year	(72,326,030)	50,332,332
Net (losses) gains on investments before special dividends	(80,287,143)	66,586,388
Special dividends credited to capital	8,180,603	4,854,213
Net (losses) gains on investments	(72,106,540)	71,440,601

Transaction costs on purchases amounted to £1,176,671 (2007 – £1,502,518) and transaction costs on sales amounted to £291,295 (2007 – £369,855).

Stocklending

	2008	2007
Aggregate value of securities on loan at year-end	£14.6m	£0m
Maximum aggregate value of securities on loan during the year	£62.3m	£72.0m
Fee income from stocklending during the year	£23,377	£9,164

In respect of securities on loan at the year-end, the Company held £15.3m (2007 – £Nil) as collateral, the value of which exceeded the value of the loan securities by £0.7m (2007 – £Nil).

In respect of the maximum aggregate value of securities on loan during the year, the Company held £64.8m (2007 – £75.6m) as collateral, the value of which exceeded the value of securities on loan by £2.5m (2007 – £3.6m).

Notes to the Financial Statements

for the year ended 31 January 2008

9. Investments in Other Companies

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')	(4,750,170)	'A' Shares	39.2	
		'B' Shares	59.2	49.2
		'C' Shares	45.6	
		'D' Shares	53.3	
Fintrust Debenture PLC ('Fintrust')	15,760	Ordinary	50.0	50.0

In the opinion of the Directors, the Company is not in a position to exert significant influence over the financial or operating policies of FDF or Fintrust, either through voting rights or through agreement with those companies' other shareholders, due to provisions in FDF and Fintrust's Articles of Association and in certain contracts between the Company and each of FDF and Fintrust. The aggregate share capital, reserves and results are immaterial to the Company's financial statements. 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 10(ii), respectively. Apart from the finance costs, there were no other transactions between FDF, Fintrust and the Company during the year.

* As at the date of the latest published financial statements of FDF or Fintrust, as appropriate.

10. Current Assets and Creditors

	2008 £	2007 £
Debtors:		
Sales for future settlement	5,784,892	1,045,185
Accrued income	1,493,835	1,693,069
Other debtors	55,211	98,649
	7,333,938	2,836,903
Cash at bank:		
Current account	5,945,385	7,003,101

Notes to the Financial Statements

for the year ended 31 January 2008

10. Current Assets and Creditors (continued)

	Note	2008 £	2007 £
Creditors: Amounts falling due within one year –			
Purchases for future settlement		–	1,029,736
Other creditors		813,007	878,218
Interest on borrowings	10(vi)	1,316,279	1,319,266
		2,129,286	3,227,220
Creditors: Amounts falling due after more than one year –			
Stepped Rate Interest Loan	10(i)	35,825,047	35,829,571
Fixed Rate Interest Loan	10(ii)	45,962,363	46,111,863
5.875% Secured Bonds 2029	10(iii)	29,073,381	29,053,646
4% Perpetual Debenture Stock	10(iv)	1,375,000	1,375,000
3.65% Cumulative Preference Stock	10(v)	1,178,000	1,178,000
		113,413,791	113,548,080

(i) The effective interest rate on 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 2 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 (65.15%) of the required amount to enable FDF to meet all of its liabilities to repay principal and interest on its £52.2 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 generally or 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 10(i) above.

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 Financial Statements
for the year ended 31 January 2008

10. Current Assets and Creditors (continued)

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 were identical to the Company's existing loan of £30,000,000. 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, as set out in the Statement of Accounting Policies. At 31 January 2008, the unamortised premium included within the Fixed Rate Interest Loan balance of greater than one year amounted to £4,077,022 (2007 – £4,229,629).

(iii) The £30,000,000 5.875% Secured Bonds, repayable on 20 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 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 10(i) and 10(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 3.65% Cumulative Preference Stock is recognised as a creditor due after more than one year under the provisions of FRS25 'Financial Instruments: Disclosure and Presentation'. The right of the Stock to receive payments is 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 1 August and 1 February.

(vi) Interest on outstanding borrowings consists of:

	2008 £	2007 £
Bank overdraft interest	4,180	–
Stepped Rate Interest Loan	312,004	313,728
Fixed Rate Interest Loan	779,240	783,545
5.875% Secured Bonds 2029	207,105	208,243
4% Perpetual Debenture Stock	13,750	13,750
	1,316,279	1,319,266

11. Called up Share Capital

	2008 £	2007 £
Authorised		
150,403,747 Ordinary Shares of 25p (2007 – 150,403,747)	37,600,936	37,600,936
Allotted and fully paid		
102,813,464 Ordinary Shares of 25p (2007 – 103,759,877)	25,703,366	25,939,969

The directors are authorised by an ordinary resolution passed on 14 May 2007 to allot relevant securities, in accordance with Section 80 of the Companies Act 1985, up to a maximum of 15,553,605 Ordinary Shares of 25p each. This authority expires on 13 May 2008 and accordingly a renewed authority will be sought at the Annual General Meeting on 13 May 2008.

During the year the Company repurchased and cancelled 946,413 Ordinary Shares at a cost of £4,643,972. The nominal value of the Ordinary Shares repurchased was £236,603 and represented 0.91% of the Company's share capital at the beginning of the financial year.

No further ordinary shares have been repurchased since the year end.

Notes to the Financial Statements
for the year ended 31 January 2008

12. Capital Redemption Reserve

	£
Balance at 1 February 2007	56,250
Movement in the year	236,603
Balance at 31 January 2008	292,853

The balance on this account was increased by the increased by the transfer of £236,603 in respect of 946,413 Ordinary Shares purchased by the Company and cancelled.

13. Capital Reserves

	Realised £	Unrealised £	Total £
Balance at 1 February 2007	401,295,652	131,247,275	532,542,927
Net losses on realisation of investments	(7,961,113)	–	(7,961,113)
Special dividends	8,180,603	–	8,180,603
Transfer on disposal of investments	42,276,719	(42,276,719)	–
Net unrealised losses arising in year	–	(72,326,030)	(72,326,030)
Purchase of Ordinary Shares for cancellation	(4,643,972)	–	(4,643,972)
Investment management fee	(1,669,652)	–	(1,669,652)
Finance costs: interest payable and similar charges	(6,116,736)	–	(6,116,736)
Other capital charges	(2,560)	–	(2,560)
Balance at 31 January 2008	431,358,941	16,644,526	448,003,467

The Institute of Accountants in England and Wales, has issued guidance (TECH 01/08), stating that profits arising out of a change in fair value of assets, recognised in accordance with Accounting Standards, may be distributed, provided the relevant assets can be readily converted into cash. Securities listed on a recognised stock exchange are generally regarded as being readily convertible into cash and hence unrealised profits amounting to £16,644,526 in respect of such securities, currently included within the Capital Reserve - Unrealised, may be regarded as distributable under Company Law.

However, under the terms of the Company's Articles of Association, Capital Reserves are available for distribution only by way of redemption or purchase of any of the Company's own shares and not for any other purpose. The Company may therefore only distribute, by way of dividend, accumulated amounts credited to the Revenue Reserve.

14. Revenue Reserve

	£
Balance at 1 February 2007	22,768,482
Revenue return for the year	23,649,820
Ordinary dividends paid during the year	(21,757,822)
Balance at 31 January 2008	24,660,480

15. Net Asset Value per Share

The Net Asset Value per share was as follows:

	Net Asset Value per Share attributable	
	2008	2007
Ordinary Shares of 25p	492.3p	567.5p

	Net Asset Value attributable	
	2008	2007
Ordinary Shares of 25p	£506,187,213	£588,834,675

The Net Asset Value per Ordinary Share is based on 102,813,464 Ordinary Shares in issue at the year end (2007 – 103,759,877).

Notes to the Financial Statements

for the year ended 31 January 2008

16. Contingent Assets

The Company has a contingent asset as at the balance sheet date relating to VAT recoverable. The contingent asset has arisen as a result of the European Court of Justice ruling on 28 June 2007 in the VAT case, brought by JP Morgan Fleming Claverhouse Trust plc in conjunction with the Association of Investment Companies concerning VAT exemption on management expenses for investment trusts. An amount of VAT payable in previous years may be recoverable but it is not yet possible to quantify an amount pending the conclusion of discussions with the Manager.

17. Contingent Liabilities and Commitments

At 31 January 2008 there were no outstanding contingent liabilities (2007 – £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 42.

18. Reconciliation of Return on Ordinary Activities before Taxation to Net Cash Flow from Operating Activities

	2008 £	2007 £
Total return before finance costs and taxation	(46,768,603)	95,952,321
Add: Special dividends credited to capital	8,180,603	4,854,213
Less: Net losses (gains) on investments at fair value	72,106,540	(71,440,601)
	33,518,540	29,365,933
Decrease (increase) in debtors	224,620	(457,602)
Decrease in creditors	(65,211)	(645,665)
Net cash inflow from operating activities	33,677,949	28,262,666

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

(i) Analysis of changes in net debt

	Cash £	Stepped and Fixed Rate loans £	5.875% Secured Bonds 2029 £	4% Perpetual Debenture Stock £	3.65% Cumulative Preference Stock £	Net Debt £
At 1 February 2007	7,003,101	(81,941,434)	(29,053,646)	(1,375,000)	(1,178,000)	(106,544,979)
Movement in year	(1,057,716)	154,024	(19,735)	–	–	(923,427)
At 31 January 2008	5,945,385	(81,787,410)	(29,073,381)	(1,375,000)	(1,178,000)	(107,468,406)

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

	2008 £	2007 £
Net cash (outflow) inflow	(1,057,716)	1,628,305
Decrease (increase) in long term loans	134,289	(194,679)
Movement in net funds	(923,427)	1,433,626
Net debt brought forward	(106,544,979)	(107,978,605)
Net debt carried forward	(107,468,406)	(106,544,979)

Notes to the Financial Statements

for the year ended 31 January 2008

20.Financial Risk Management policies and procedures

The Company invests in equities and other investments in accordance with its investment objective as stated on page 2. In pursuing its investment objective, the Company is exposed to certain inherent risks that could result in either a reduction in the Company's net assets or a reduction in the profits available for distribution by way of dividends.

The main risks arising from the Company's financial instruments are: market risk (comprising market price risk, currency risk and interest rate risk), liquidity risk and credit risk. The Directors' approach to the management of these risks are set out below. The Investment Manager, in close cooperation with the Board of Directors, coordinates the Company's risk management. The Board determines the objectives and agrees policies for managing each of these risks, as set out below. These policies have remained substantially unchanged during the current and preceding period.

Market Risk

The fair value and/or future cash flows of a financial instrument held by the Company may fluctuate due to changes in market prices. Market risk comprises market price risk, currency risk and interest rate risk. The Investment Manager assesses the exposure to market risk when making each investment decision, and monitors the overall level of market risk on the whole of the investment portfolio on an ongoing basis.

(i) **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 Company's investment portfolio is based wholly in the United Kingdom and hence is chiefly exposed to economic conditions in that country. An analysis of the Company's portfolio is shown on pages 9 and 10.

Management of market price risk

The Board meets regularly to monitor the diversification of assets within the portfolio and the investment performance, 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.

The value of the Company's listed investments which were exposed to market price risk as at 31 January was as follows:

	2008 £000s	2007 £000s
Investments held at fair value through profit or loss	608,424	695,743

Market price risk sensitivity

The following illustrates the sensitivity of the return after taxation for the year and the net assets to an increase or decrease of 20% (2007: 20%) in the fair values of the Company's quoted equities. This level of change is considered to be reasonably possible based on observation of market conditions in the year. The sensitivity analysis on the net return after taxation and net assets is based on the impact of a 20% increase or decrease in the value of the Company's investments at each closing balance sheet date and the consequent impact on the investment management fees for the year, with all other variables held constant.

Notes to the Financial Statements

for the year ended 31 January 2008

20. Financial Risk Management policies and procedures (continued)

	2008 20% Increase in fair value £000s	2008 20% Decrease in fair value £000s	2007 20% Increase in fair value £000s	2007 20% Decrease in fair value £000s
Income statement – net return after tax				
Revenue return	(180)	180	(192)	192
Capital return	121,351	(121,351)	138,791	(138,791)
Change in net return on ordinary activities attributable to Ordinary Shareholders	121,171	(121,171)	138,599	(138,599)
Change in total net assets	121,171	(121,171)	138,599	(138,599)

(ii) **Foreign Currency Risk**

Foreign currency risk is the risk of movement in the values of overseas financial instruments as a result of fluctuations in exchange rates. A number of the investments have global operations and therefore profits received from them can be affected by currency movements, both on a transactional and transitional basis. This is incorporated within the market price of each investment.

Management of currency risk

The Company invests predominantly in UK listed securities with the effect that the total net assets and the total return are not materially affected by currency movements.

Any income denominated in foreign currencies is converted into sterling on receipt (e.g. as a result of a corporate action). The Company does not use financial instruments to mitigate the currency exposure in the period between the time that income is included in the financial statements and its receipt.

(iii) **Interest Rate Risk**

Interest rate risk is the risk of movements in the value of financial instruments as a result of fluctuations in interest rates.

Management of 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. In the year to 31 January 2008, the Company held no fixed interest securities. The Company's policy is to remain substantially fully invested and thus does not expect to hold significant cash balances.

The Company finances its operations through a mixture of share capital, retained earnings and long term borrowings. Movement in interest rates will not affect the finance costs and financial liabilities and net assets of the Company as all the borrowings of the Company carry fixed rates of interest and were issued as a planned level of gearing. The borrowings are carried in the balance sheet at amortised cost rather than fair value. Therefore the impact of sensitivity to interest rate risk is not material and accordingly the Company's net assets and total return are not materially affected.

Interest rate exposure

The Company's exposure to floating rate interest on assets as at 31 January 2008 was £5,945,000 (2007 – £7,003,000).

The Company's exposure to fixed interest rates on liabilities as at 31 January 2008 was £113,414,000 (2007 – £113,548,000).

Interest rates received on cash balances, or paid on bank overdrafts respectively, is approximate to 5.00% and 6.35% per annum (2007: 5.25% and 6.10% per annum).

Notes to the Financial Statements
for the year ended 31 January 2008

20. Financial Risk Management policies and procedures (continued)

The fixed rate interest bearing liabilities bear the following coupon and effective rates as at 31 January 2008 and 31 January 2007

	Maturity date	Amount borrowed £000s	Coupon Rate	Effective rate since Inception*
Stepped Rate Interest Loan	2/1/2018	25,668	14.75%	11.28%
Fixed Rate Interest Loan – original loan	20/11/2023	30,000	9.25125%	9.51%
Fixed Rate Interest Loan – additional loan	20/11/2023	12,000	9.25125%	6.00%
5.875% Secured Bonds 2029	20/12/2029	30,000	5.875%	6.23%
4% Perpetual Debenture Stock	n/a	1.375	4.00%	4.00%
3.65% Cumulative Preference Stock	n/a	1,178	3.65%	3.65%

*The effective rates are calculated in accordance with FRS 26 'Financial Instruments: Recognition and Measurement' as detailed in the Statement of Accounting Policies.

The weighted average effective rate of the Company's fixed interest bearing liabilities (excluding the 4% Perpetual Debenture Stock and the 5% Cumulative Preference Stock is 8.54% (2007 – 8.54%) and the weighted average period to maturity of these liabilities is 16.2 years (2007 – 17.2 years).

The above year end amounts are reasonably representative of the exposure to interest rates during the year, as the level of exposure does not change materially. Therefore the Company's net return and net assets are not materially affected by changes in interest rates.

Liquidity risk

Liquidity risk relates to the capacity to meet liabilities.

Management of liquidity risk

Liquidity risk is not significant as the Company's assets mainly comprise realisable securities, which can be sold to meet funding requirements if necessary. The Board gives guidance to the Investment Manager as to the maximum amount of the Company's resources that should be invested in any one company. The Company's policy is to remain substantially fully invested. Short term flexibility can be achieved through the use of overdraft facilities, where necessary. The Company has an undrawn committed borrowing facility of £10 million (2007: £10 million).

The maturity profile of the Company's financial liabilities at 31 January 2008, (being the borrowings from the Stepped Rate Interest Loan, the Fixed Rate Interest Loan, the 5.875% Secured Bonds, the 4% Perpetual Debenture Stock and the 3.65% Preference Stock), is detailed in Note 10 'Current Assets and Creditors on pages 42 and 43.

The contractual maturities of the financial liabilities at 31 January, based on the earliest date on which payment can be required to be made was as follows:

		More than 3 months			
2008	3 months or less £000s	Not more than one year £000s	Between one year and five years £000s	More than five years £000s	Total £000s
Creditors: Amounts falling due within one year					
Debt interest due within one year	–	1,312	–	–	1,312
Bank overdraft interest	4	–	–	–	4
Other creditors	813	–	–	–	813
Creditors: Amounts falling due after more than one year					
Debt due after more than one year	–	–	–	113,414	113,414
	817	1,312	–	113,414	115,543

Notes to the Financial Statements
for the year ended 31 January 2008

20. Financial Risk Management policies and procedures (continued)

2007	3 months or less £000s	More than 3 months Not more than one year £000s	Between one year and five years £000s	More than five years £000s	Total £000s
Creditors: Amounts falling due within one year					
Debt interest due within one year	–	1,320	–	–	1,320
Bank overdraft interest	–	–	–	–	–
Other creditors	1,908	–	–	–	1,908
Creditors: Amounts falling due after more than one year					
Debt due after more than one year	–	–	–	113,548	113,548
	1,908	1,320	–	113,548	116,776

Credit Risk

Credit risk is the risk of default by a counterparty.

Management of credit risk

The risk is not significant. Credit risk is managed by ensuring that transactions are carried out with approved brokers. The credit ratings of brokers counterparties are reviewed quarterly by the Investment Manager to mitigate the 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 market value of the stock on loan. The level of collateral is recalculated on a daily basis. Further details on stock lending can be found in Note 8 on page 40.

In summary, the exposure to credit risk at 31 January was as follows:

	2008 £000s	2007 £000s
Current Assets		
Debtors:		
Outstanding settlements	5,785	1,045
Accrued income	1,494	1,693
Other debtors	55	99
Cash at bank	5,945	7,003
	13,279	9,840

Fair Values of Financial Assets and Financial Liabilities

With the exception of those financial liabilities measured at amortised cost, the financial assets and financial liabilities, are either carried in the Balance Sheet at their fair value (investments) or the balance sheet amount is a reasonable approximation of fair value (due to/from brokers, dividends and interest receivable, accruals, cash at bank and bank overdrafts).

Notes to the Financial Statements
for the year ended 31 January 2008

20 Financial Risk Management policies and procedures (continued)

Financial liabilities measured at amortised cost:

	2008 Book value £000s	2008 Fair value £000s	2007 Book value £000s	2007 Fair value £000s
Stepped Rate Interest Loan	35,825	48,390	35,830	48,354
Fixed Rate Interest Loan	45,962	57,710	46,112	57,741
5.875% Secured Bonds 2029	29,073	30,813	29,054	31,130
4% Perpetual Debenture Stock	1,375	1,112	1,375	1,130
3.65% Cumulative Preference Stock	1,178	787	1,178	787

The fair value is derived from the closing market value as at 31 January 2008 and 31 January 2007.

Hedging Instruments

At the year end the Company had no hedging arrangements in place (2007 – Nil).

21. Capital Management Policies and Procedures

The Company's objective is to provide an above average level of income and income growth together with long term capital growth.

The Company's capital at 31 January comprises:

	2008 £000s	2007 £000s
Debt		
Creditors: Amounts falling due within one year	1,316	1,320
Creditors: Amounts falling due after more than one year	113,414	113,548
	114,730	114,868
Equity		
Called up Share Capital	25,703	25,940
Share Premium Account and Other Reserves	480,484	562,895
	506,187	588,835
Total Capital	620,917	703,703
Debt as a percentage of total capital	18.5%	16.3%

The Board with the assistance of the Investment Manager monitors and reviews the broad structure of the Company's capital on an ongoing basis. The level of gearing is monitored, taking into account the Investment Managers' view on the market and the future prospects of the trust's performance. Capital management also involves reviewing the difference between the net asset value per share and the share price (i.e. the level of share price discount or premium) to assess the need to repurchase shares for cancellation.

The Company's objectives, policies and processes for managing capital are unchanged from the preceding accounting period. The Company is subject to several externally imposed capital requirements; the bank borrowings under the overdraft facility are not to exceed £10m, as a public company the minimum share capital is £50,000.

These requirements are unchanged from last year, and the Company has complied with them.

Notice of Meeting

Notice is hereby given that the Annual General Meeting of The Merchants Trust PLC will be held at 20 Moorgate, London EC2R 6DA, on 13 May 2008 at 12.00 noon to transact the following business.

Routine Business

1 To receive and adopt the Report of the Directors and the Financial Statements for the year ended 31 January 2008 together with the Auditors' Report thereon.

2 To declare a final dividend of 5.4p per Ordinary Share.

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

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

5 To elect Mr M. J. E. McKeon as a Director.

6 To elect Mr H. E. Staunton as a Director.

7 To approve the Directors' Remuneration Report.

8 To re-appoint PricewaterhouseCoopers LLP as Auditors of the Company, to hold office until the conclusion of the next general meeting at which financial statements are laid before the Company.

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

Special Business

To consider and if thought fit to pass the following resolutions. Resolution 12 will be proposed as an Ordinary Resolution and Resolutions 10, 11 and 13 as Special Resolutions:

10 That the regulations contained in the printed document produced to the meeting and marked "A" (and for the purposes of identification initialled by the Chairman of the meeting) be hereby approved and adopted as the Articles of Association of the Company in substitution for and for the exclusion of all existing Articles of Association.

11 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 15,411,738;

(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% of the average of the middle-market quotations for an Ordinary Share taken from the London Stock Exchange Official List for the five 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 2008 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.

12 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 £8,567,788 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 or might require relevant securities to be allotted after such expiry and the Directors may allot relevant securities in pursuance of any such offer or agreement as if that authority had not expired.

Notice of Meeting

13 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 pursuant to the authority conferred by Resolution 10 as if sub-section (1) of Section 89 of the Act did not apply to any such allotment provided that:

(i) the power granted shall be limited to the allotment of equity securities wholly for cash up to an aggregate nominal amount of £1,285,168;

(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 pursuance of such offer or agreement as if that power had not expired.

155 Bishopsgate
London EC2M 3AD
14 April 2008

By Order of the Board
K. J. Salt
Secretary

Notes:

1. 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 Financial Report. Completion of the enclosed form of proxy does not preclude a Member from attending the Meeting and voting in person.

2. In order to facilitate voting by corporate representatives at the meeting, arrangements will be put in place at the meeting so that (i) if a corporate shareholder has appointed the Chairman of the meeting as its corporate representative with instructions to vote on a poll in accordance with the directions of all of the other corporate representatives for that shareholder at the meeting, then on a poll those corporate representatives will give voting directions to the Chairman and the Chairman will vote (or withhold a vote) as corporate representative in accordance with those directions; and (ii) if more than one corporate representative for the same corporate shareholder attends the meeting but the corporate shareholder has not appointed the Chairman of the meeting as its corporate representative, a designated corporate representative will be nominated, from those corporate representatives who attend, who will vote on a poll and the other corporate representatives will give voting directions to that designated corporate representative. Corporate shareholders are referred to the guidance issued by the Institute of Chartered Secretaries and Administrators on proxies and corporate representatives (www.icsa.org.uk) for further details of this procedure. The guidance includes a sample form of representation letter if the Chairman is being appointed as described in (i) above.

3. Persons nominated to receive information rights under Section 146 of the Act who have been sent a copy of this notice of meeting are hereby informed, in accordance with Section 149(2) of the Act, that they may have a right under an agreement with the registered member by whom they were nominated to be appointed, or to have someone else appointed, as a proxy for this meeting. If they have no such right, or do not wish to exercise it, they may have a right under such an agreement to give instructions to the member as to the exercise of voting rights.

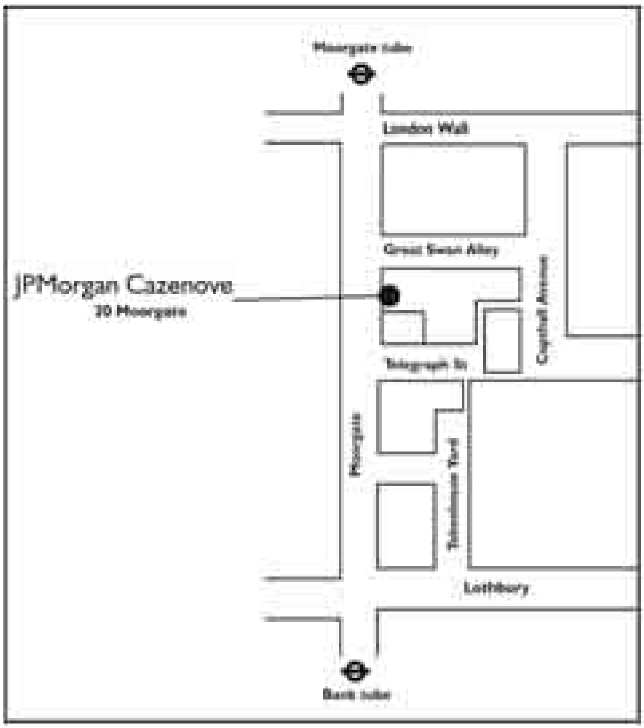
   Nominated persons should contact the registered member by whom they were nominated in respect of these arrangements.

4. Shares held in uncertificated form (i.e., in CREST) may be voted through the CREST Proxy Voting Service in accordance with the procedures set out in the CREST manual.

5. 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 6p.m. on 11 May 2008 ('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.

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

Annual General Meeting Venue



Investor Information & Contact Details

The Managers
Allianz Global Investors is the marketing name of RCM (UK) Limited, Allianz Group's regulated UK fund management company, which is authorised and regulated by the Financial Services Authority.

Allianz Global Investors is one of the largest fund managers in the World, and as at 31 December 2007, had combined assets of £561.9 billion under management. Through its predecessors, it has a heritage of investment trust management expertise in the UK stretching back to the nineteenth century and had £1.3 billion assets under management in a range of investment trusts as at 31 December 2007.

Results
Half-year announced in September
Full-year announced in March
Annual Financial Report posted to shareholders in April
Annual General Meeting held in May

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

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

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 the Registrars, Capita Registrars, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4TU. 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.

Dividend Reinvestment Plan for Ordinary Shareholders
A Dividend Reinvestment Plan is operated by the Company's Registrars, Capita Registrars. The Plan offers Ordinary Shareholders the opportunity to use their cash dividend to buy further shares in the Company under a special low-cost dealing arrangement. Capita will enclose a copy of the Terms and Conditions and a personalised application form with each future dividend payment.

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 Regulatory News Service. The geographical spread of investments and ten largest holdings are also published monthly by the London Stock Exchange Regulatory News Service. They are also available to any enquirer of Allianz Global Investors, either via Investor Services on 0800 317 573 or on the Manager's website: www.allianzglobalinvestors.co.uk.

Share Prices
The share prices quoted in the London Stock Exchange Daily Official List for 31 January 2008 were 424.75p – 425.25p.

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

Website
Further information about the The Merchants Trust PLC is available on the Manager's website: www.allianzglobalinvestors.co.uk.

Association of Investment Companies (AIC)
The Company is a member of the AIC, the trade body of the investment trust industry, which provides a range of literature including fact sheets and a monthly statistical service. Copies of these publications can be obtained from the AIC, 9th Floor, 24 Chiswell Street, London EC1Y 4YY, or at www.theaic.co.uk.

AIC Category: UK Growth and Income.

Investment Trust Share Plan and ISA
Following a strategic review of services provided for Investment Trust investors, Allianz Global Investors as announced that it will no longer act as Share Plan manager or PEP/ISA manager from 29 February 2008. Since that date, however, a share plan and ISA have been available from Alliance Trust Savings (ATS). ATS offer a comprehensive range of products and services – including Share Plans, ISAs and PEPs as well as pension products. They also invest in and maintain online and telephone-based dealing facilities and online valuations. Existing Allianz Global Investors Investment Trust ISA, PEP and Share Plan wrapper investors have had the opportunity to transfer at no cost to ATS. More information is available from the Allianz Global Investors Helpline on 08457 127 128 or from the Manager's website: www.allianzglobalinvestors.co.uk, or after 1 March 2008 from Alliance Trust Savings Customer Services Department on 01382 326323 or e-mail: contact@alliancetrust.co.uk.

Investor Information & Contact Details

Capita Registrars – Share Dealing Services

Capita Registrars, the Company's Registrars, operate an on-line and telephone dealing facility for UK resident shareholders with share certificates. Stamp duty may also be payable on purchases.

Capita Registrars have provided the following details of the current charges for these services:

On-line	Telephone
1% of the value of the deal	1.5% of the value of the deal
(Minimum £20,	(Minimum £25,
maximum £50)	maximum £100)

There is no need to pre-register and there are no forms to fill in. The on-line and telephone dealing services allow shareholders to trade "real time" at a known price which will be given to you at the time you give your instruction.

To deal on-line or by telephone you need to supply your surname, shareholder reference number, share certificate, full postcode and your date of birth. Your shareholder reference number can be found on your share certificate where it is shown as an "investor code". Please have the appropriate documents to hand when you log on or call, as this information will be needed before you can buy or sell shares.

For further information on these services please contact: www.capitadeal.com (on-line dealing) or 0871 664 0454 (telephone dealing) (Calls cost 10p per minute plus network extras).

Shareholder Portal

The Company's Registrars, Capita Registrars, are now able to offer shareholders a free on-line service called The Share Portal, enabling shareholders to access a comprehensive range of shareholder related information.

Through The Share Portal, shareholders can:

- View their current and historical shareholding details.
- Obtain an indicative share price and valuation.
- Amend address details.
- View details of dividend payments
- Apply for dividends to be paid directly to a bank or to change existing bank details.

Shareholders can access these services at www.capitaregistrars.com and selecting Share Portal (Shareholders) from the drop down menu, or alternatively via the Portals: Quick Links, and selecting Share Portal.

Shareholders will need to register for a Share Portal Account by completing an on-screen registration form. An email address is required.

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 0871 664 0300 (calls cost 10p per minute plus network charges) or, if telephoning from overseas, +44 20 8639 3399. 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, 155 Bishopsgate, London EC2M 3AD.
Telephone: 020 7065 1513. Email: kirsten.salt@uk.rcm.com

CREST Proxy Voting

Shares held in uncertificated form (i.e., in CREST) may be voted through the CREST Proxy Voting Service in accordance with the procedures set out in the CREST manual.

Analysis of Share Register

	Shareholder Accounts				Ordinary Shares held			
	Number		%		000's		%	
	2008	2007	2008	2007	2008	2007	2008	2007
Private holders	7,860	7,980	64.7	65.0	20,580	20,756	20.0	20.0
Nominees	3,973	3,820	32.7	31.1	77,267	77,613	75.2	74.8
Limited Companies	164	173	1.4	1.4	2,195	2,537	2.1	2.5
Investment Trusts and Funds	51	104	0.4	1.0	559	752	0.5	0.7
Bank and Bank Nominees	9	11	0.1	0.1	1,778	1,274	1.7	1.2
Insurance Companies	12	12	0.1	0.1	65	67	0.1	0.1
Pension Funds	4	5	0.0	0.0	20	23	0.0	0.0
Other holders	70	163	0.6	1.3	349	737	0.4	0.7
	12,143	12,268	100.0	100.0	102,813	103,759	100.0	100.0

Based on an analysis of the Ordinary Share register at 31 March 2008 (2007 – 2 April).

Investor Information & Contact Details

Managers and Advisers

Fund Manager
RCM (UK) Limited
Represented by Simon Gergel, Portfolio Manager, and
Simon White, Head of Investment Trusts

Secretary and Registered Office
Kirsten Salt BA (Hons) ACIS
155 Bishopsgate
London EC2M 3AD
Telephone: 020 7065 1513
Email: kirsten.salt@uk.rcm.com

Registered Number 28276

Registrars and Transfer Office
Capita Registrars
The Registry
34 Beckenham Road
Beckenham
Kent BR3 4TU
Telephone (if calling from within the UK): 0871 664 0300
(Calls cost 10p per minute plus network charges)
Telephone (if calling from overseas): +44 20 8639 3399
Email: ssd@capitaregistrars.com

Independent Auditors
PricewaterhouseCoopers LLP
Hay's Galleria
1 Hay's Lane
London SE1 2RD

Bankers
HSBC Bank
Barclays Bank

Stockbroker
JPMorgan Cazenove

Legal Advisers
Herbert Smith LLP

Allianz Global Investors
Telephone: 0800 317 573 or
www.allianzglobalinvestors.co.uk.

Allianz Global Investors
Phone 0800 317 573
Fax 020 7638 3508
www.allianzglobalinvestors.co.uk