The Mercantile Investment Trust plc

Annual Report & Accounts for the year ended 31st January 2011

J.P.Morgan
Asset Management

Features

Contents

Objective

Long term capital growth from a portfolio of UK medium and smaller companies.

Investment Policy

- To emphasise growth from medium and smaller companies. Long term dividend growth at least in line with inflation.
- To use long term gearing to increase potential returns to shareholders. The Company's gearing policy is to operate within a range of 90% to 120% invested.
- To invest no more than 15% of gross assets in other UK listed investment companies (including investment trusts).

Benchmark

The FTSE All-Share Index excluding constituents of the FTSE 100 Index and investment trusts.

Capital Structure

At 31st January 2011 the Company's share capital comprised 99,035,719 ordinary shares of 25p each.

At 31st January 2011, the Company also had in issue, a £3,850,000 4.25% perpetual debenture and a £175 million 6.125% debenture repayable on 25th February 2030.

Management Company

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

Financial Highlights

Total returns (includes dividends reinvested)

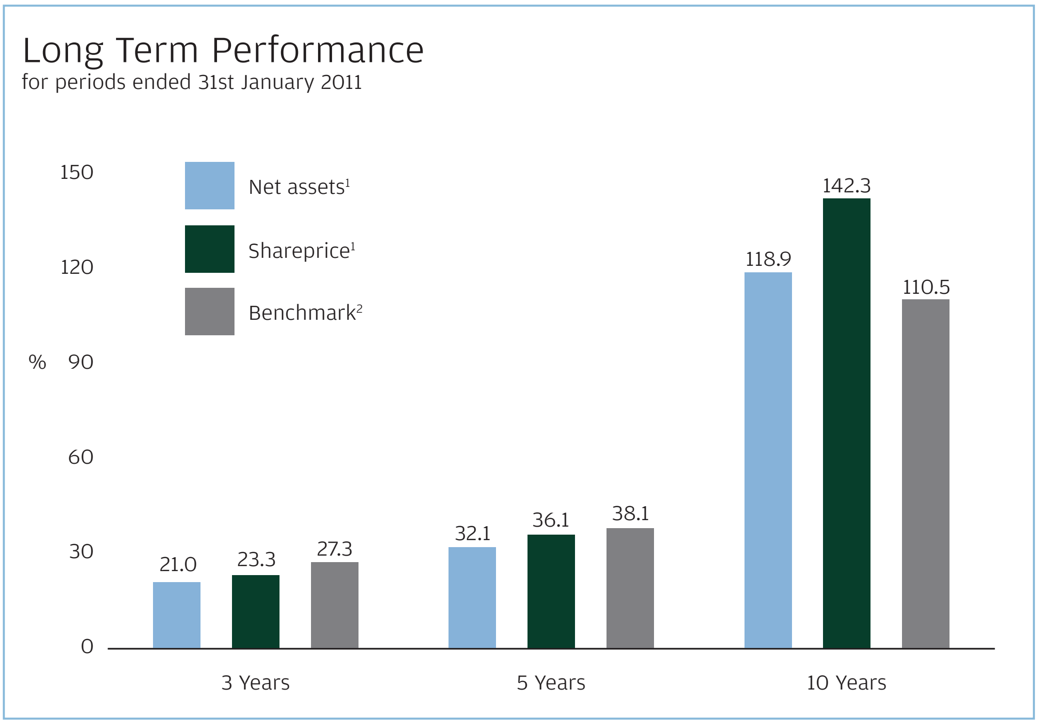
+27.4%
Return on net assets[1]
(2010: +56.3%)

+33.8%
Return to shareholders[2]
(2010: +51.6%)

+26.6%
Benchmark[3]
(2010: +57.6%)

36.0p
Dividend
(2010: 36.0p)

[1]Source: J.P. Morgan.
[2]Source: Morningstar.
[3]Source: Russell/Mellon CAPS. The Company's benchmark is the FTSE All-Share Index (excluding FTSE 100 constituents and investment trusts).



A glossary of terms and definitions is provided on page 55.

[1]Source: Morningstar.
[2]Source: Russell/Mellon CAPS. The Company's benchmark is the FTSE All-Share Index (excluding FTSE 100 constituents and investment trusts).

Chairman's Statement

Over the year to 31st January 2011, the Company's total return on net assets (ie with net income reinvested) was 27.4%, which compares with a return of 26.6% from the Company's benchmark index, the FTSE All-Share (excluding FTSE 100 constituents and investment trusts). The dividend payment to shareholders will, once again, be partially funded from reserves, to the value of £9 million (2010: £10million), which has reduced the total return on net assets by 0.9%.

Returns and Dividends

Earnings per share increased by 15.9% for the year, from 23.2p to 26.9p, partly due to an increase in dividend income received.

The Company has paid three interim dividends of 6.0p per ordinary share, and the Directors have declared a fourth quarterly interim dividend of 18.0p, giving a total dividend of 36.0p for the year, maintaining last year's dividend of 36.0p. The Board recognises, as in previous years, that it is essential to make an appropriate distribution, which both meets shareholders' legitimate expectations, and is prudent in the light of what may be continuing difficult times ahead.

The Board intends therefore to continue to pay three interim dividends at the current rate of 6.0p per ordinary share throughout the year ending 31st January 2012. The level of the fourth quarterly interim dividend will be determined by the Board based on the level of income received by the Company during the year and with regard to the Company's revenue reserve of 19.7p per share.

Share Price Discount

The share price rose by 29.0% during the year and, including dividends paid, the total return to shareholders was 33.8%. The discount to net asset value at year end was 10.3% compared to 14.5% (with debt at fair value) the previous year. The average daily discount, with debt at fair value, during the year, was 12.3%.

Share Repurchases

During the year under review a total of 2,912,249 shares were repurchased for cancellation, amounting to 2.9% of issued share capital at the beginning of the year, at a total cost of £27.3 million. Share repurchases during the year under review have added approximately 4.1 pence to the net asset value per share.

The Board's objective remains to use the share repurchase authority to manage imbalances between the supply and demand of the Company's shares, thereby reducing the volatility of the discount. The Board believes that, to date, this mechanism has been helpful and therefore proposes and recommends that the powers to repurchase up to 14.99% of the Company's shares for cancellation be renewed for a further period.

Gearing

The Company ended the year with gearing of 108.9%. During the year the gearing varied between 97% and 115%. It is the Board's intention to continue to operate within the range of 90% to 120% invested, under normal market conditions, and at the present time, the Board is maintaining gearing in the middle part of the range. Gearing is regularly discussed between the Board and the Investment Manager. A new borrowing facility of £45 million was negotiated with ING Bank in January 2011 in order to provide the Investment Manager with adequate flexibility with respect to gearing. This facility can be used tactically as investment opportunities present themselves.

Board

The new UK Corporate Governance Code introduced in June 2010 requires all directors of companies within the FTSE 350 Index to offer themselves for annual re-election, and with this in mind all of the Company's Directors are standing for re-election from this year onwards. I refer you to the Directors' biographies on page 17 for further details.

Investment Managers

The Company's investment management team comprises Martin Hudson and Jane Lennard working together with the JPMorgan Asset Management European Equity Group.

The Board continues to monitor the performance of the Manager on a regular basis.

Brokers

As part of the Board's regular review of service providers, it was agreed to appoint Oriel Securities Limited, to act as joint broker with Cenkos Securities plc.

VAT Case

In my statement last year I reported on two ongoing issues relating to VAT. First, the Company's intention to pursue a claim for compound interest on the VAT recovered from HMRC, for which only simple interest has so far been paid. Secondly, the Company is seeking to recover VAT paid over the years 1997 to 2000. Both these issues are unresolved, and may remain so for several years, but the risk/reward ratio is such that it is in the interests of shareholders to see them through to conclusion, although I must emphasise that there is no guarantee of success.

Annual General Meeting

The Company's one hundred and twenty fifth Annual General Meeting will be held at Trinity House, Tower Hill, London EC3N 4DH on Wednesday 18th May 2011 at 12noon. In addition to the formal part of the meeting, there will be a presentation from the Investment Managers who will answer questions on the portfolio and performance. The meeting will be followed by a buffet lunch which will give shareholders an opportunity to meet the Board, the Investment Managers and representatives of JPMAM. I look forward to seeing as many of you as possible at the meeting.

Please submit, via the Company's website (www.mercantileit.co.uk and click on the Investment Trust Information link) or in writing (to the Company Secretary at Finsbury Dials, 20 Finsbury Street, London EC2Y 9AQ) any detailed questions that you wish to raise at the AGM. Shareholders who are unable to attend the AGM in person are encouraged to use their proxy votes. Shareholders are now able to

Chairman's Statement – continued

lodge their proxy votes electronically, whether their shares are held through CREST or in certificate form, and full details are set out on the form of proxy.

Outlook

The outcome of events in Japan and the Middle East is currently unclear, as is the resolution of the debate with respect to sovereign debt in certain European countries. Conditions in the UK are likely to be difficult due to the Government's imperative of reducing the deficit. However, the Stock Market in the UK appears reasonable value based on historic parameters, and earnings of UK companies are, on the whole, in positive territory.

The Board is confident that the Investment Managers are well positioned to identify and act on suitable investment opportunities.

Hamish Leslie Melville
Chairman 31st March 2011

For further information, please contact:
Juliet Dearlove
For and on behalf of
JPMorgan Asset Management (UK) Limited – Secretary
020 7742 6000

Investment Managers' Report

Performance attribution for the year ended 31st January 2011

	%	1 Year %
Contributions to total returns		
Benchmark total return		26.6
Allocation effect	-4.9	
Selection effect	6.3	
Gearing/cash effect	0.5	
Portfolio total return		1.9
Fees/expenses	-0.6	
Share buybacks	0.4	
Proposed dividend	-0.9	
Net asset value total return		27.4
Effect of decreases in discount	6.4	
Share price total return		33.8

Source: Xamin/JPMAM/AIC/Morningstar.

The table provides a breakdown, relative to the benchmark, of the contributions to total return.

A glossary of terms and definitions is provided on page 55.

Market Background

The stockmarket continued to recover during the year ended 31st January 2011. With interest rates remaining low and most companies continuing to see recovery in demand, the attraction of equities continued to grow.

After a positive start to the year the stockmarket was hit in May by the prospect of a European Sovereign debt crisis but it recovered strongly from September in anticipation of the US Federal Reserve announcing a further round of Quantitative Easing. In November the Fed announced its intention to purchase $600 billion of Treasuries to reflate the US economy. Meanwhile in the UK the new Government announced its austerity measures to address the budget deficit.

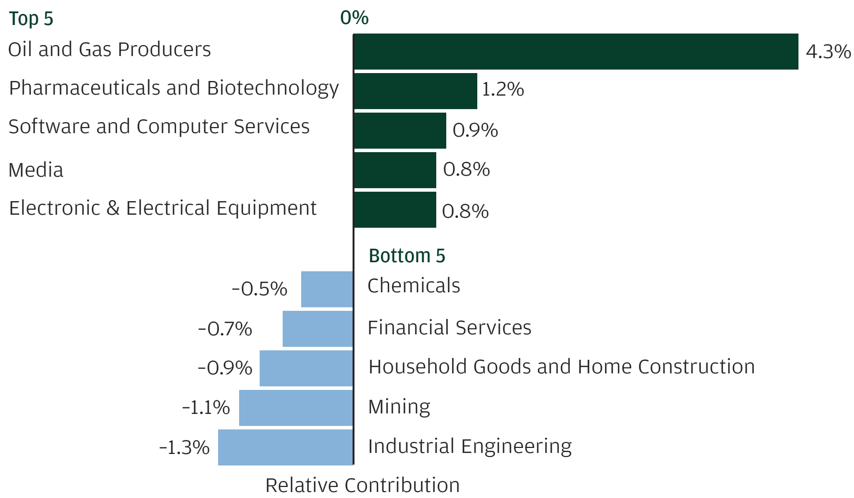
Performance

Small and mid sized UK companies continued to recover more strongly than the stockmarket as a whole as three themes predominated: corporate activity especially takeovers; growth from emerging markets; and re-rating of those stocks where confidence in earnings growth was increasing.

The net asset value total return for the year ended 31st January 2011 was +27.4% which was ahead of the Company's benchmark index, the FTSE All-Share excluding FTSE 100 constituents and investment companies, which returned +26.6%. This compares with a return of 18.1% for the broader FTSE All-Share Index. The contributors to performance are analysed in the table to the left.

The bar chart shows the relative contributions to performance for the year for the five best and five worst sectors within the portfolio. The dark green bars to the right show the positive contributors relative to the benchmark index and reflect both sector weightings and stock selection. The light blue bars to the left show the negative relative contributors.

Sector performance contribution analysis.
Year to 31st January 2011



Source: Factset

Investment Managers' Report – continued

This shows that the biggest contributor to performance was the Oil and Gas Producers sector, where we benefited from Cove Energy making four big gas discoveries in offshore Mozambique and from Dana Petroleum agreeing to a takeover bid from Korea National Oil Corporation. The portfolio also gained substantially from agreed takeovers for Chloride Group, Tomkins and BSS Group. Some of the cash proceeds from the takeover bids was invested in a range of smaller biotechnology companies such as Renovo, Vectura and Biocompatibles which performed strongly during the year, although Renovo has had a disappointing result on its lead drug since our year end. The new issue market got underway during the year and we had a strong contribution from our investment in Supergroup, the designer and retailer of Superdry clothing. In terms of emerging market exposure, our holdings in palm oil plantations performed well, with New Britain Palm Oil in particular being a strong performer. Turning to the third investment theme of last year, the rerating of stocks with strong earnings momentum, we lost relative performance in Industrial Engineering and Chemicals by not holding stocks such as Weir Group and Croda which benefited from profits forecast upgrades but which we wrongly judged to be too expensive. The mining sector cost us relative performance; despite a strong gold price African Barrick Gold and Petropavlovsk underperformed when they disappointed the stockmarket by missing production targets.

Activity

The investment managers have the flexibility to operate within a gearing range of 90% to 120% invested and a more specific tactical range is agreed regularly with the Board.

Gearing was reduced in the first part of the year reflecting macroeconomic uncertainty after a strong recovery in stock markets and as cash was received from agreed takeover bids, for example, for Dana Petroleum, Chloride Group, Tomkins, Arriva and Dimension Data. As the stockmarket steadied during September, gearing was gradually increased again, ending the year at 108.9%. The new investments were generally biased towards smaller, growth companies and mid sized companies with value characteristics.

Value stocks have underperformed since the credit crisis took hold in 2007. Value stocks are those companies which are valued at a lower than average multiple of profits or assets. Growth stocks are those companies growing profits or assets at a higher than average rate and associated momentum stocks are those where the share price is showing strength usually in response to profit forecasts continually being upgraded. Over the long term value stocks generally outperform growth stocks and, as a class, we now see them offering opportunities as the market turns its attention back to the fundamentals of companies.

The portfolio retains its style of broad diversification across all sectors, holding about 150 stocks of which 90 are mid-sized and 60 are smaller companies. By value, approximately 75% of the portfolio is invested in mid sized stocks and 25% in smaller companies.

The table below shows that our holdings in companies which are larger than £1 billion in market capitalisation account for more than half of the portfolio. We focus on those successful large companies which are progressing towards promotion into the FTSE 100 index and also newer holdings in a number of those out of favour companies which have recently fallen out of the FTSE 100 Index but which have good recovery prospects. The portfolio is also overweight in the very smallest companies including those capitalised at less than £100 million, which can present outstanding growth opportunities.

Portfolio Size Distribution

Market capitalisation	Benchmark index weighting %	Fund weighting %	Relative weighting %
More than £1.5bn	37.2	30.6	–6.6
£1.0bn to £1.5bn	22.4	24.7	2.3
£500m to £1.0bn	22.3	19.7	–2.6
£300m to £500m	8.6	7.2	–1.4
£100m to £300m	8.5	12.0	3.5
£50m to £100m	0.9	3.8	2.9
Less than £50m	0.1	2.0	1.9
Total	**100.0**	**100.0**	**0.0**

As at 31st January 2011

Of the ten largest holdings at the year end only two, ITV and Pennon, were in the top ten a year ago. The largest holding, Cove Energy, had just been bought a year ago, and was an exceptionally strong performer last year after making major gas discoveries. Cable and Wireless Worldwide, Cable and Wireless Communications and London Stock Exchange are examples of value companies which were bought following their demotion from the FTSE 100. The remaining four top ten holdings, Jardine Lloyd Thompson, Persimmon, Hiscox and Tate & Lyle were all held within the portfolio a year ago and the size of those holdings was increased during the year.

Of those no longer in the top ten of a year ago, GKN was sold on its promotion into the FTSE 100, Premier Oil was reduced following its strong performance in sympathy with takeover target Dana, Misys is still held having returned substantial funds to shareholders following the disposal of its US healthcare software business and the positions in Imagination Technologies, Drax, First Group and Songbird Estates have all been reduced.

At the sector level the portfolio is overweight in basic materials and consumer goods because of our exposure to gold miners and to palm oil plantations. It is underweight in consumer services such as retailers and travel & leisure because of the economic headwinds the consumer is facing but offsetting this we have increased our exposure to housebuilders which are very cheaply rated. The portfolio is overweight in healthcare for its growth characteristics and overweight in telecommunications and utilities for their value bias. The largest underweight position is in the large industrials grouping where we are underweight in aerospace & defence, construction and support services

Investment Managers' Report – continued

which are all facing Government cutbacks and also in industrial engineering which we believe is generally too highly rated following a trend of strong profit growth.

During the year we met or visited more than 250 companies and this remains an important component in our process of evaluating companies. We believe that properly targeted company meetings can help us to analyse smaller companies that are often overlooked by the mainstream, evaluate managers and resolve issues. Our fundamental analysis of companies is aided by JPMorgan's in-house proprietary screening process which helps us to identify companies that exhibit the best value and growth characteristics.

Outlook

The macroeconomic fears are many and varied as a result of public finances having become so strained in the developed world. The problems of Greece and Ireland remind us that Sovereign debt will remain an issue, the US is continuing to grapple with its unsustainable fiscal trajectory by printing money but unemployment there is remaining high and growth low, China is dealing with the problems of overheating and an asset price bubble in the property market and there are fears that currency wars may erupt and spill over into protectionism. All that was the case before the eyes of the world focussed on North Africa and the Middle East. The ramifications of the current unrest will be felt globally. Oil prices have already risen in response to the disruption to supply. Continued uncertainty or more political change in the region could produce a further spike in the oil price which would act as a headwind to the fragile global economic recovery. We therefore expect markets to be volatile in 2011.

In the UK the consumer is facing a difficult year as public sector cuts and tax increases are implemented and the threat of inflation has increased the likelihood of interest rates rising this year. Food prices, vehicle tax and insurance, rail fares and petrol prices have all been rising strongly since 2009 and the offsetting deflationary influence of falling mortgage interest payments and clothing prices have now started to reverse.

Of course some inflation helps to make the debt burden more manageable and makes real assets such as equities more attractive. In fact UK companies have been benefiting in many cases from being able to pass on raw material price increases to their customers but have not been experiencing wage inflation as there is plenty of spare capacity in the economy. This has helped profit margins to recover strongly and together with the stockmarket equity issuance of last year means that, generally, small and mid sized quoted company balance sheets have been repaired. As order books and sales have grown there is a real sense of companies having recovered confidence and that they are returning to businesses as usual. This is being reflected in an increase in capital expenditure from the minimal levels of the last two years. As confidence returns we expect corporate activity to increase and that the targets will be strong well managed companies with substantial market shares or assets; just the sort of companies we invest in and which are plentiful in the small and mid sized market. Despite the strong recovery of the last two years, stockmarket valuations in terms of yield and price to earnings ratios still remain below the medium term average and our small and mid cap benchmark index is currently valued on a forward price to earnings ratio of 12.5x. Reflecting a modest value bias, the price to earnings ratio of Mercantile's underlying portfolio is 10.9x.

Therefore, whilst for macroeconomic reasons we expect to see some stockmarket volatility returning during the course of the year, we believe that the environment is still positive for equities. That belief is reflected in your Company's gearing level which is currently 109%.

Martin Hudson
Jane Lennard
Investment Managers 31st March 2011

Summary of Results

	2011	2010	
Total returns for the year ended 31st January			
Return on net assets[1]	+27.4%	+56.3%	
Return to shareholders[2]	+33.8%	+51.6%	
Benchmark[3]	+26.6%	+57.6%	
Net asset value and discount at 31st January			% change
Shareholders' funds (£'000)	1,237,266	1,035,376	+19.5
Net asset value per share with debt at par value	1,249.3p	1,015.6p	+23.0
Net asset value per share with debt at fair value[4]	1,236.7p	1,005.5p	+23.0
Share price discount to net asset value with debt at par value	11.2%	15.3%	
Share price discount to net asset value with debt at fair value	10.3%	14.5%	
Market Data			
FTSE All-Share Index (capital only) (excluding FTSE 100 Index constituents and investment trusts)[5]	2,313.2	1,877.7	+23.2
Share price	1,109.0p	860.0p	+29.0
Revenue for the year ended 31st January			
Net revenue available for shareholders (£'000)	26,769	23,703	+12.9
Return per share	26.9p	23.2p	+15.9
Dividend per share	36.0p	36.0p	0.0
Total Expense Ratio[6]	0.49%	0.54%	
Actual Gearing Factor[7]	108.9%	111.9%	

A glossary of terms and definitions is provided on page 55.

[1]Source: J.P. Morgan.

[2]Source: Morningstar.

[3]Source: Russell/Mellon CAPS. The Company's benchmark is the FTSE All-Share Index excluding constituents of the FTSE 100 Index and investment trusts.

[4]The fair value of the Company's debentures have been calculated using discounted cash flow techniques, using the yield from a similar dated gilt plus a margin based on the 5 year average for the AA Barclays Sterling Corporate Bond spread.

[5]Source: Datastream.

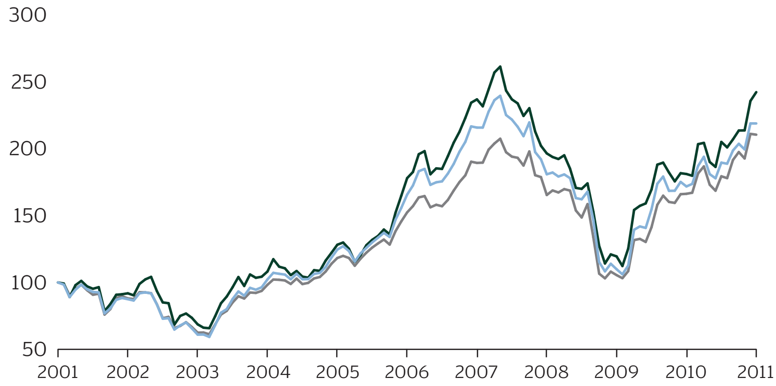
[6]Management fees and all other operating expenses, excluding interest, expressed as a percentage of the average of the month end net assets during the year.

[7]Actual gearing means investments expressed as a percentage of shareholders' funds.

Performance

Ten Year Performance

Figures have been rebased to 100 at 31st January 2001



The Mercantile – net asset value total return.

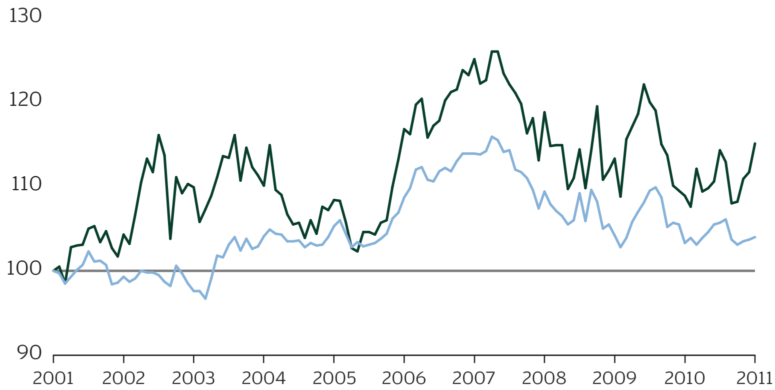
The Mercantile – share price total return.

Benchmark.

Source: Morningstar, Russell/Mellon CAPS.

Performance relative to Benchmark

Figures have been rebased to 100 at 31st January 2001



The Mercantile – net asset value total return.

The Mercantile – share price total return.

The benchmark is represented by the grey horizontal line.

Source: Morningstar, Russell/Mellon CAPS.

Ten Year Financial Record

At 31st January	2001	2002	2003	2004	2005[1]	2006	2007	2008	2009	2010	2011
Total assets less current liabilities (£'m)	1,153.3	1,076.8	791.5	1,156.8	1,321.0	1,621.5	1,920.5	1,384.9	874.1	1,212.3	1,414.3
Net asset value per share (p)	755.8	644.7	434.6	703.5	842.6	1,090.6	1,394.4	1,158.3	681.5	1,015.6	1,249.3
Share price (p)	635.5	567.0	408.5	620.0	713.5	965.0	1,258.0	1,020.0	592.5	860.0	1,109.0
Year to 31st January											
Gross revenue (£'000)	34,391	39,435	34,584	34,050	34,970	39,899	45,493	51,684	51,750	32,248	32,237
Revenue available for shareholders (£'000)	24,124	28,364	24,169	24,555	24,820	29,373	35,043	44,345	43,028	23,703	26,769
Earnings per share (p)	17.6	20.9	17.8	18.1	18.3	21.8	27.5	39.8	41.7	23.2	26.9
Dividend per share (net) (p)[2]	14.8	17.5	18.0	18.8	19.8	21.8	25.0	38.0	36.0	36.0	36.0
Discount	15.9	12.1	6.0	11.9	15.3	11.5	9.8	11.9	13.0	15.3	11.2
Actual gearing	114.0	110.0	113.1	112.6	115.5	111.2	102.0	94.8	102.8	111.9	108.9
Total expense ratio[3]	0.65	0.63	0.73	0.69	0.60	0.56	0.55	0.59	0.56	0.54	0.49
Rebased to 100 at 31st January 2001											
Net asset value per share	100.0	85.3	57.7	93.1	111.5	144.3	184.5	153.3	90.2	134.4	165.3
Net asset value per share – total return[4]	100.0	87.5	61.0	102.3	124.6	165.7	215.8	180.9	109.9	171.8	218.9
Share price	100.0	89.2	64.3	97.6	112.3	151.8	198.0	160.5	93.2	135.3	174.5
Share price – total return[4]	100.0	91.0	68.7	108.2	128.2	178.0	236.9	196.5	119.5	181.1	242.3
Benchmark[4]	100.0	88.1	62.5	98.3	118.3	152.4	189.4	165.4	105.5	166.3	210.5
Earnings per share	100.0	118.8	101.1	102.8	104.0	123.9	156.3	226.1	236.9	131.8	153.0
Dividends per share[2]	100.0	118.2	121.6	127.0	133.8	147.3	168.9	256.8	243.2	243.2	243.2

[1]The results for the year ended 31st January 2005 have been restated, where necessary, in accordance with Financial Reporting Standards 21, 25 and 26. Years prior to 2005 have not been restated.

[2]2008 includes ordinary dividends of 34.0p and a special dividend of 4.0p.

[3]Management fees and all other operating expenses, excluding interest, expressed as a percentage of the average of the month end net assets during the year (2008 and prior years: the average of the opening and closing net assets).

[4]Source: Morningstar, Russell/Mellon CAPS.

Ten Largest Investments

Company	At 31st January 2011 Valuation £'000	%[1]	At 31st January 2010 Valuation £'000	%[1]
Cove Energy[2] An oil and gas exploration and development company. The company's focus is on emerging basins in Africa and the Mediterranean.	33,716	2.4	5,036	0.4
Cable & Wireless Communications[3] A global provider of telecommunications and internet services. The company's global communication services offer internet protocol, data, voice and hosting services to businesses located in the UK, USA, Europe and Japan. Cable & Wireless telecommunication services provide fixed and mobile voice, data, and internet protocol services to consumers and businesses located in the Caribbean.	33,073	2.3	–	–
ITV A United Kingdom media company covering broadcasting, news and production. The company owns all of the regional Channel 3 licences in England and Wales. ITV owns ITV1, ITV2 and commercial television channels.	32,179	2.3	35,915	3.0
Pennon Operates and invests in water and sewerage services, waste management and renewable energy.	30,704	2.2	23,754	2.0
Jardine Lloyd Thompson[2] Operates a wholesale insurance and reinsurance broking company. The company's businesses offer marine, aviation, property and casualty plans, in addition to reinsurance services. Jardine Lloyd Thompson, which operates as a Lloyd's broker, also provides a range of innovative risk solutions and transactional services.	28,484	2.0	17,792	1.5
Cable & Wireless Worldwide[3] Provides critical communication infrastructure and services for users of telecommunications. The company provides data, applications, and internet protocol based services. Cable & Wireless operates globally, serving users in the United Kingdom, Asia-Pacific, India, the Middle East, Continental Europe, and the United States.	27,402	1.9	–	–
Persimmon[2] Designs, builds and develops residential housing. The company has regional branches in Yorkshire, the North East and North West, Scotland, the Midlands, Anglia, Wessex, Thames Valley, the South East, South Coast, South West and Wales.	24,648	1.7	17,312	1.4
London Stock Exchange[3] Is the United Kingdom's primary stock exchange. The LSE provides markets that facilitate the raising of capital and the trading of corporate securities, access to a trading environment, as well as real-time pricing and reference information services worldwide. Market coverage includes equities, derivatives and fixed-interest securities.	24,421	1.7	–	–
Hiscox[2] Operates in the United Kingdom insurance market. The company's services include underwriting managed syndicates, underwriting a range of personal and commercial insurance and other underwriting services. Hiscox provides its services for customers in the United Kingdom and Continental Europe.	21,868	1.6	11,356	0.9
Tate & Lyle[2] A multinational company which manufactures, refines, processes, distributes and trades sweeteners, starches and their by-products. The company's products include white sugar, molasses, low-calorie sweeteners, and an assortment of fermentation products, including ethanol, citric acid, potable alcohol, amino acids and polyols.	21,360	1.5	19,268	1.6
Total[4]	**277,855**	**19.6**		

All of the above investments are listed in UK.

[1]Based on total assets less current liabilities of £1,414m (2010: £1,212m).

[2]Not Included in the ten largest investments at 31st January 2010.

[3]Not held in the portfolio at 31st January 2010.

[4]At 31st January 2010, the value of the ten largest investments amounted to £244m representing 20.1% of total assets less current liabilities.

Portfolio Analyses

Listed Equity Market Capitalisation
at 31st January

	2011 %	2010 %
UK FTSE Mid 250 Companies	67.5	77.1
UK Smaller Companies	25.2	16.0
UK FTSE 100	1.1	–
UK Unquoted	0.4	1.5
Overseas Companies	1.1	0.9
Net Current Assets	4.7	4.5
Total	100.0	100.0

Based on total assets less current liabilities of £1,414m (2010: £1,212m).

Sector Analysis
at 31st January

	Portfolio 2011 %	Benchmark 2011 %	Portfolio 2010 %	Benchmark 2010 %
Consumer Services	18.0	21.5	22.0	21.7
Financials	17.6	19.6	20.7	17.4
Consumer Goods	11.1	6.7	14.0	9.4
Industrials	11.1	27.2	17.1	28.3
Basic Materials	9.0	7.3	4.5	5.0
Oil & Gas	8.4	5.7	6.4	4.6
Technology	6.2	5.8	5.6	8.2
Telecommunications	5.0	2.1	0.7	0.9
Utilities	4.7	2.1	4.5	2.3
Health Care	4.2	2.0	–	2.2
Net Current Assets	4.7	–	4.5	–
Total	100.0	100.0	100.0	100.0

Based on total assets less current liabilities of £1,414m (2010: £1,212m).

List of Investments

at 31st January 2011

Company	£'000
United Kingdom	
Consumer Services	
ITV	32,179
Go-Ahead	21,024
Aegis	16,853
First Group	15,885
Mitchells & Butlers	15,662
Marston's	15,208
Debenhams	10,052
Chime Communications	9,463
Dunelm	8,403
Supergroup	8,081
William Hill	7,941
Young & Co's Brewery[1]	7,388
National Express	7,366
WH Smith	7,139
United Business Media	6,594
Easyjet	6,467
Entertainment One	6,413
Stagecoach	6,078
Aer Lingus[3]	5,931
Informa	5,612
Pendragon	5,603
CVS	5,481
Bloomsbury Publishing	4,076
M&S Saatchi	4,002
Sportech	3,770
Topps Tiles	2,378
Avis Europe	2,185
Ashley (Laura)	2,159
Chrysalis[2]	1,891
The Hotel Corporation[1]	1,686
Peel Hotels[1]	806
Pinewood Shepperton	600
	254,376
Financials	
Jardine Lloyd Thompson	28,484
London Stock Exchange	24,421
Hiscox	21,868
Songbird Estates[1]	17,742
Catlin	15,094
Phoenix Holdings	11,065
Segro	10,021

Company	£'000
London & Stamford[1]	9,658
St James's Place	9,461
Shaftesbury	9,366
Tullett Prebon	8,051
Amlin	6,824
Hansteen	6,413
Shore Capital[1]	6,345
Hardy	5,902
Aberdeen Asset Management	5,806
Chaucer Holdings	5,636
Helical Bar	5,346
Workspace	5,047
St Peter Port[1]	4,717
Max Property	4,537
Rathbone Brothers	3,888
NBNK Investments	3,333
DTZ	3,324
Puma Brandenburg[3]	3,071
Mountview Estates	2,987
Camellia	2,882
Cenkos Securities[1]	2,334
Channel Islands Property Fund	2,170
JPMorgan Cazenove Holdings[2]	1,761
Orchid Development[1]	1,200
	248,754
Consumer Goods	
Persimmon	24,648
Tate & Lyle	21,360
Bovis Homes	18,725
MP Evans[1]	14,868
New Britain Palm Oil	12,200
Barratt Developments	11,730
Berkeley	10,523
Bellway	10,068
Cranswick	8,064
AGA Rangemaster	7,123
Asian Citrus	4,428
R.E.A.	3,257
Anglo-Eastern Plantations	3,132
Redrow	2,681
Devro	2,413
Landkom International[1]	2,316
UNIQ	137
	157,673

List of Investments – continued

Company	£'000
Industrials	
Rentokil Initial	21,118
Travis Perkins	13,186
Smith (DS)	12,311
Xchanging	10,947
VP	10,812
SIG	9,024
Ricardo	8,530
Ultra Electronics	8,127
Senior	7,614
Robert Walters	7,489
Charter International	7,319
Premier Farnell	6,987
Morgan Crucible	6,792
BBA Aviation	6,202
Fenner	3,804
Shaft Sinkers	3,740
Babcock International	3,514
Skil Ports & Logistics	2,783
Spirax Sarco	2,614
Spectris	2,238
Smiths News	1,141
Forth Ports	1,095
	157,387
Basic Materials	
Centamin Egypt	20,297
Petropavlovsk	19,702
Aquarius Platinum	15,643
African Barrick Gold	14,868
Ferrexpo	8,694
Mondi	8,314
Carclo	7,284
Medusa Mining	6,343
Gem Diamonds	6,186
Kenmare Resources[3]	6,095
Hochschild Mining	5,789
Yule Catto & Co	5,188
Tennants Consolidated[2,4]	2,313
	126,716
Oil & Gas	
Cove Energy[1]	33,716
Wood (John)	19,117
SOCO International	15,750
Premier Oil	11,309
Hunting	10,288

Company	£'000
Heritage Oil	8,159
Caza Oil & Gas	4,343
Lamprell	3,979
Northern Petroleum[1]	3,789
Infrastrata	2,855
Ithaca Energy[1]	2,265
Amerisur Resources	2,045
IGAS Energy[1]	682
	118,297
Technology	
Logica CMG	21,293
Misys	16,010
Imagination Technologies	15,174
Wolfson Microelectronics	13,684
CSR	11,275
Spirent Communications	6,385
Advanced Computer Software	2,000
Vislink	1,116
	86,937
Telecommunications	
Cable & Wireless Communications	33,073
Cable & Wireless Worldwide	27,402
Colt Telecom	10,686
	71,161
Utilities	
Pennon	30,704
Northumbrian Water	19,431
Drax	16,265
	66,400
Health Care	
Genus	14,723
Renovo	13,964
Vectura	10,573
Hikma Pharmaceuticals	7,805
BTG	5,156
Oxford Biomedica	4,629
Vernalis	3,011
	59,861
Total Portfolio[5]	**1,347,562**

[1]AIM listed investment.

[2]Unquoted investment.

[3]Listed overseas.

[4]Includes a fixed interest investment.

[5]The portfolio comprises investments in equity shares and a fixed interest investment.

Board of Directors

Hamish Leslie Melville (Chairman)
A Director since 1996 and Chairman since September 2003.

He is Chairman of the Investment Banking Committee at The Royal Bank of Scotland, and was formerly Managing Director of Credit Suisse Securities (Europe) Limited, and Chairman or a Director of a number of UK listed companies.

Sir Richard Beckett
A Director since September 2009.

Sir Richard was called to the bar in 1965 and took silk in 1987. He was one of the pre-eminent practitioners in regulatory and licensing matters. He is also a non-executive director of JD Wetherspoon Plc.

The Right Hon. The Earl of Halifax
A Director since December 2007.

Formerly Vice-Chairman of Christie, Manson & Woods, the European Division of Christie's International Fine Arts Auctioneers, and a non-executive director of Hambros Bank. He is Deputy Lieutenant of The East Riding of Yorkshire, High Steward of York Minster and a JP.

Sandy Nairn
A Director since December 2003. He is Chief Executive of Edinburgh Partners Ltd. Previously, he served on the boards of Vebnet (Holdings) plc, Vebnet Ltd, Franklin Templeton Investment Management Limited, Hill Samuel Asset Management International Limited, Waverley General Private Equity Limited and Scottish Widows Investment Partnership Limited.

Charles Peel
A Director since October 2005.

A founding director of Peel Hunt and Co. Limited in 1989. He is actively involved with a number of private companies. Previously, he was a director of Ingenious Music VCT plc, and held senior positions with Fielding Newson-Smith & Co. and Morgan Grenfell Securities.

Ian Russell
A Director since January 2007 and Chairman of the Audit Committee since May 2007. He is Chairman of Johnston Press plc, Advanced Power AG, Remploy Limited and the University of Edinburgh's Campaign Board. He is also a director of British Assets Trust plc and an advisor to the Clyde Bergemann Power Group. Previously, he held senior positions with Scottish Power, Tomkins and HSBC.

All Directors were members of the Audit Committee throughout the year, with the exception of Hamish Leslie Melville.

All Directors were members of the Nomination Committee throughout the year.

All Directors are considered independent of the Manager.

Directors' Report

The Directors present their report and audited financial statements for the year ended 31st January 2011.

Business Review

Business of the Company

The Company carries on business as an investment trust and was approved by HM Revenue & Customs as an investment trust in accordance with Section 1158 of the Corporation Tax Act 2010 (formerly Section 842 of the Income and Corporation Taxes Act 1988) for the year ended 31st January 2010. 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 1158 of the Corporation Tax Act 2010 each year.

Approval in previous years is subject to review should there be any subsequent enquiry under Corporation Tax Self Assessment.

The Company is an investment company within the meaning of Section 833 of the Companies Act 2006. The Company is not a close company for taxation purposes.

A review of the Company's activities and prospects is given in the Chairman's Statement on pages 2 to 4, and in the Investment Managers' Report on pages 5 to 9.

Investment Objective

The Company's objective is to achieve long term capital growth from a portfolio of UK medium and smaller companies.

Investment Policies and Risk Management

In order to achieve its objective, the Company invests in a diversified portfolio and employs a Manager with a strong focus on research that enables it to identify what it believes to be the most attractive stocks in the market.

The Board has sought to manage the Company's risk by imposing various investment limits and restrictions. These limits and restrictions may be varied at any time by the Board at its discretion.

Investment Limits and Restrictions

- The Company invests in medium and smaller companies which are listed mainly on the London Stock Exchange.
- At time of purchase the maximum exposure to any individual stock is 8% of gross assets.
- Investment growth is emphasised, with long-term dividend growth at least in line with inflation.
- Gearing may be used when appropriate in order to increase potential returns to shareholders. Such gearing will be long-term in nature and will operate within a range of 90% to 120% invested.
- The Company does not invest more than 15% of its gross assets in other UK listed investment companies (including investment trusts).
- The Company will not invest more than 10% of assets in companies that themselves may invest more than 15% of gross assets in UK listed investment companies.

Performance

In the year to 31st January 2011, the Company produced a total return to shareholders of +33.8% and a total return on net assets of +27.4%. This compares with the return on the Company's benchmark of +26.6%. At 31st January 2011, the value of the Company's investment portfolio was £1,348 million. The Investment Managers' Report on pages 5 to 9 includes a review of developments during the year as well as information on investment activity within the Company's portfolio.

Total Return, Revenue and Dividends

Gross total return for the year amounted to £281.5 million (2010: £394.2 million loss) and net total return after deducting interest, management expenses and taxation amounted to £265.0 million (2010: £378.2 million). Distributable income for the year amounted to £26.8 million (2010: £23.7 million). The Directors have declared quarterly interim dividends totalling 36.0p per ordinary share (2010: 36.0p) for the year which totalled £35.7 million (2010: £36.8 million). The year end revenue reserve after allowing for these dividends will amount to £19.5 million (2010: £28.0 million).

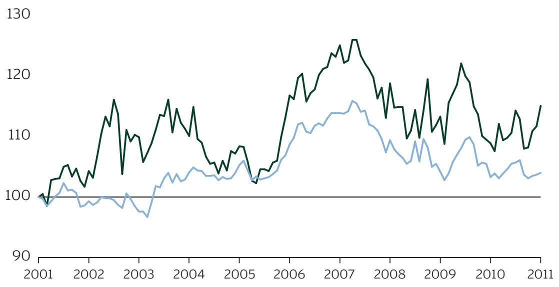
Key Performance Indicators ('KPIs')

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

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

Performance relative to Benchmark Index

Figures have been rebased to 100 at 31st January 2001



The Mercantile – net asset value total return.
The Mercantile – share price total return.
The benchmark is represented by the grey horizontal line.

Source: Morningstar, Russell/Mellon CAPS.

Ten Year Performance

Figures have been rebased to 100 at 31st January 2001

The Mercantile – net asset value total return.
The Mercantile – share price total return.
Benchmark.

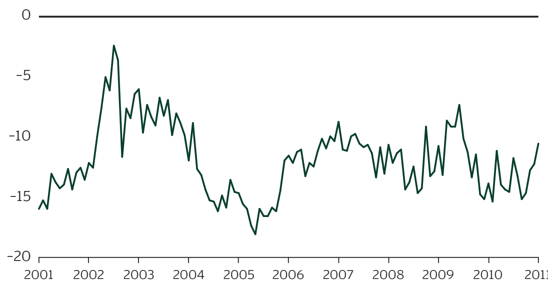
Source: Morningstar, Russell/Mellon CAPS.

- Performance against the Company's peers
  The principal objective is to achieve capital growth relative to the benchmark. The Board also monitors the performance relative to a broad range of competitor funds.

- Performance attribution
  The purpose of performance attribution analysis is to assess how the Company achieved its performance relative to its benchmark index, i.e. to understand the impact on the Company's relative performance of the various components such as asset allocation and stock selection. Details of the attribution analysis for the year ended 31st January 2011 are given in the Investment Managers' Report on page 5.

- Share price discount to net asset value ('NAV')
  The Board operates a share repurchase programme that seeks to address imbalances in supply and demand of the Company's shares within the market and thereby reduce the volatility and absolute level of the discount to NAV at which the Company's shares trade.

Discount Performance



The Mercantile – Discount.

Source: Datastream.

- Total expense ratio ('TER')
  The TER represents management fees and all other operating expenses excluding interest, expressed as a percentage of the average of the month end net assets during the year. The method of calculating the TER has changed this year and the prior year figure restated. In previous years the TER represented management fees and all other operating expenses excluding interest calculated as above, expressed as a percentage of the average of the opening and closing net assets. The new methodology more accurately reflects the way the management fee is calculated, which is based on the Company's month end market capitalisation. The TER for the year ended 31st January 2011 is 0.49% and for the year ended 31st January 2010 is 0.54% as restated (previously 0.57%). The Board reviews each year an analysis which shows a comparison of the Company's TER and its main expenses with those of its peers.

Share Capital

During the year the Company repurchased a total of 2,912,249 ordinary shares for cancellation. This amount represented 2.9% of the issued share capital at the beginning of the year. As the shares were repurchased at a discount to the underlying net asset value ('NAV') they enhanced the NAV of the remaining shares. The Company has repurchased no further shares for cancellation since the year end.

A resolution to renew the authority to repurchase shares will be put to shareholders at the forthcoming Annual General Meeting.

The Company did not issue any shares during the year.

Directors' Report – continued

Principal Risks

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

- Investment and Strategy: An inappropriate investment strategy, for example asset allocation or the level of gearing, may lead to underperformance against the Company's benchmark index and peer companies, resulting in the Company's shares trading on a wider discount. The Board manages these risks by diversification of investments through its investment restrictions and guidelines which are monitored and reported by the Manager. JPMAM provides the Directors with timely and accurate management information, including performance data and attribution analyses, revenue estimates, liquidity reports and shareholder analyses. The Board monitors the implementation and results of the investment process with the Investment Managers, who attend all Board meetings, and reviews data which show statistical measures of the Company's risk profile. The Investment Managers employ the Company's gearing tactically, within a strategic range set by the Board.
- Accounting, Legal and Regulatory: In order to qualify as an investment trust, the Company must comply with Section 1158 of the Corporation Tax Act 2010 ('Section 1158') (formerly Section 842 of the Income and Corporation Taxes Act 1988). Details of the Company's approval are given under 'Business of the Company' above. Were the Company to breach Section 1158, it might lose investment trust status and, as a consequence, gains within the Company's portfolio could be subject to Capital Gains Tax. The Section 1158 qualification criteria are continually monitored by JPMAM and the results reported to the Board each month. The Company must also comply with the provisions of the Companies Acts and, since its shares are listed on the London Stock Exchange, the UKLA Listing Rules and Disclosure & Transparency Rules ('DTRs'). A breach of the Companies Acts could result in the Company and/or the Directors being fined or the subject of criminal proceedings. Breach of the UKLA Listing Rules or DTRs could result in the Company's shares being suspended from listing which in turn would breach Section 1158. The Board relies on the services of its Company Secretary, JPMAM, to ensure compliance with The Companies Acts and The UKLA Listing Rules.
- Corporate Governance and Shareholder Relations: Details of the Company's compliance with Corporate Governance best practice, including information on relations with shareholders, are set out in the Corporate Governance report on pages 23 to 26.
- Operational: Disruption to, or failure of, JPMAM's accounting, dealing or payments systems or the custodian's records could prevent accurate reporting and monitoring of the Company's financial position. Details of how the Board monitors the services provided by JPMAM and its associates and the key elements designed to provide effective internal control are included within the Internal Control section of the Corporate Governance report on page 25.
- Financial: The financial risks faced by the Company include market price risk, interest rate risk, liquidity risk and credit risk. Bank counterparties are subject to daily credit analysis by the Manager and regular consideration at meetings of the Board. In addition the Board receives regular reports on the Manager's monitoring and mitigation of credit risks on share transactions carried out by the Company. Further details are disclosed in note 23 on pages 46 to 50.

Future Developments

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

Management

The Manager and Secretary is JPMorgan Asset Management (UK) Limited ('JPMAM'). JPMAM is employed under a contract terminable on six months' notice, without penalty. If the Company wishes to terminate the contract on shorter notice, the balance of remuneration is payable by way of compensation.

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

The Board has evaluated the performance of the Manager and confirms that it is satisfied that the continuing appointment of the Manager on the terms agreed is in the interests of shareholders as a whole. In arriving at this view, the Board considered the investment strategy and process of the Investment Managers, noting performance against the benchmark over the long term and the support that the Company receives from JPMAM.

Management Fee

The management fee is charged at the rate of 0.5% of the value of the Company's market capitalisation and is calculated and paid monthly in arrears. If the Company invests in funds managed or advised by JPMAM, or any of its associated companies, they are excluded from the calculation and therefore attract no fee.

Going Concern

The Directors believe that having considered the Company's investment objective (see page 18), risk management policies (see page 46), capital management policies and procedures (see page 51), nature of the portfolio and expenditure projections, that the Company has adequate resources, an appropriate financial structure and suitable management arrangements in place to continue in operational existence for the foreseeable future. For these reasons, they consider that there is reasonable evidence to continue to adopt the going concern basis in preparing the accounts.

Payment Policy

It is the Company's policy to obtain the best terms for all business and therefore there are no standard payment terms. In general, the Company agrees with its suppliers the terms on which business will take place and it is the Company's policy to abide by these terms. As at 31st January 2011, the Company had no outstanding trade creditors.

Directors

The Directors of the Company at the end of the year, together with their beneficial interests in the Company's ordinary share capital, were:

	31st January 2011	1st February 2010 or at date of appointment
Hamish Leslie Melville	30,000	30,000
Sir Richard Beckett	4,100	4,000
The Right Hon. The Earl of Halifax	2,000	2,000
Sandy Nairn	5,000	5,000
Charles Peel	33,100	33,100
Ian Russell	5,000	5,000

No changes in the above holdings have been recorded at the date of this report.

As explained in the Chairman's statement, in accordance with corporate governance best practice, all Directors will retire at the Company's forthcoming Annual General Meeting, and, being eligible, will offer themselves for re-election by shareholders.

The Nomination Committee, having considered their qualifications, performance and contribution to the Board and its committees, confirms that each Director continues to be effective and demonstrates commitment to the role and the Board recommends to shareholders that they be re-elected.

Director Indemnification and Insurance

As permitted by the Company's Articles of Association, the Directors have the benefit of an indemnity which is a qualifying third party indemnity, as defined by Section 234 of the Companies Act 2006. The indemnities were executed on 19th May 2010 and are currently in force.

An insurance policy is maintained by the Company which indemnifies the Directors of the Company against certain liabilities arising in the conduct of their duties. There is no cover against fraudulent or dishonest actions.

Disclosure of Information to Auditors

In the case of each of the persons who are Directors of the Company at the time when this report was approved:

(a) so far as each of the Directors is aware, there is no relevant audit information (as defined in the Companies Act) of which the Company's Auditors are unaware; and

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

The above confirmation is given and should be interpreted in accordance with the provisions of Section 418(2) of the Companies Act 2006.

Independent Auditors

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

Directors' Report – continued

Annual General Meeting

Note: This section is important and requires your immediate attention. If you are in any doubt as to the action you should take you should seek your own personal financial advice from your stock broker, bank manager, solicitor, or other financial advisor authorised under the Financial Services and Markets Act 2000.

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

Authority to allot new shares and to disapply statutory pre-emption rights (resolutions 10 and 11)

The Directors will seek renewal of the authority at the AGM to issue up to 4,951,784 Ordinary shares for cash up to an aggregate nominal amount of £1,237,946 such amount being equivalent to 5% of the present issued ordinary share capital as at the last practicable date before the publication of this document. The full text of the resolutions is set out in the Notice of Meeting on page 52. This authority will expire at the conclusion of the AGM of the Company in 2012 unless renewed at a prior general meeting.

It is advantageous for the Company to be able to issue new shares to participants purchasing shares through the JPMorgan savings products and also to other investors when the Directors consider that it is in the best interests of shareholders to do so. As such issues are only made at prices greater than the net asset value (the 'NAV'), they increase the NAV per share and spread the Company's administrative expenses, other than the management fee which is charged on the value of the Company's market capitalisation, over a greater number of shares. The issue proceeds are available for investment in line with the Company's investment policies. The Company currently does not hold any shares in the capital of the Company in Treasury.

Authority to repurchase the Company's shares for cancellation (resolution 12)

At the Annual General Meeting held in May 2010, shareholders gave authority to the Company to enable it to purchase up to 14.99% of its then issued share capital. This authority will expire on 18th November 2011 unless renewed by shareholders. The Directors consider that the renewing of the authority is in the interests of shareholders as a whole, as the repurchase of shares at a discount to the underlying net asset value ('NAV') enhances the NAV of the remaining shares.

Recommendation

The Board considers resolutions 10-12 are likely to promote the success of the Company and are in the best interests of the Company and its shareholders as a whole. The Directors unanimously recommend that you vote in favour of the resolutions as they intend to do in respect of their own beneficial holdings which amount in aggregate to 79,200 shares representing approximately 0.08% of the existing issued ordinary share capital of the Company. The full text of the resolutions are set out in the Notice of Meeting on pages 52 to 53.

Corporate Governance

Compliance

The Company is committed to high standards of corporate governance. This statement, together with the Statement of Directors' Responsibilities on page 28, indicates how the Company has applied the principles of good governance of the Financial Reporting Council Combined Code 2008 (the 'Combined Code') and the AIC's Code of Corporate Governance, (the 'AIC Code'), which complements the Combined Code and provides a framework of best practice for investment trusts.

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

Role of the Board

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

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

The Board has procedures in place to deal with potential conflicts of interest and confirms that the procedures have operated effectively during the year under review.

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

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

Board Composition

The Board consists of six non-executive Directors, all of whom are regarded by the Board as independent, including the Chairman. The Directors have a breadth of investment, business and financial skills and experience relevant to the Company's business and brief biographical details of each Director are set out on page 17.

A review of Board composition and balance is included as part of the annual performance evaluation of the Board. The Board has considered whether a senior independent director should be appointed and has concluded that, as the Board consists entirely of non-executive directors, this is unnecessary.

Tenure

The Chairman, having been a Director of the Company for more than 9 years, has retained his independence by submitting to annual re-election.

Directors are initially appointed until the following Annual General Meeting when, under the Company's Articles of Association, it is required that they be elected by shareholders. Thereafter, subject to the performance evaluation carried out each year, the Board will agree whether it is appropriate for each Director to seek re-election. In accordance with the new UK Corporate Governance Code, from 2011 onwards, Directors continuing in office will seek annual re-election.

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

The Board recommends the re-election of the Directors who each seek re-election at this year's AGM.

Meetings and Committees

The Board delegates certain responsibilities and functions to committees. Details of membership of committees are shown with the Directors' profiles on page 17. Directors who are not members of Committees may attend at the invitation of the Chairman.

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

Director	Board Meetings Attended	Audit Committee Meetings Attended	Nomination Committee Meetings Attended
Hamish Leslie Melville	5	n/a*	1
Sir Richard Beckett	5	2	1
The Right Hon. The Earl of Halifax	5	2	1
Sandy Nairn	4	1	1
Charles Peel	4	2	1
Ian Russell	5	2	1

*Attended by invitation

Training and Appraisal

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

The Board has undertaken an evaluation of the Manager, its own performance and that of its committees and individual Directors. The evaluation of individual Directors is led by the Chairman and another Director leads the evaluation of the Chairman's performance. The Board as a whole evaluates the Manager, its own performance and that of its committees.

Board Committees

Nomination Committee

The Nomination Committee, chaired by Hamish Leslie Melville, consists of all the Directors and meets at least annually to ensure that the Board has an appropriate balance of skills to carry out its fiduciary

Directors' Report – continued

duties and to select and propose suitable candidates for appointment when necessary.

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

On an annual basis each Director submits a list of potential conflicts of interest for approval at the Nomination Committee meeting. These are considered carefully, taking into account the circumstances surrounding them, and, if considered appropriate, are approved for a period of one year.

Audit Committee

The Audit Committee, chaired by Ian Russell, consists of all the Directors other than the Chairman and meets at least twice each year. The members of the Committee consider that they have the requisite skills and experience to fulfil the responsibilities of the Committee.

The Committee reviews the actions and judgements of the Manager in relation to the half year and annual accounts and the Company's compliance with the Combined Code. It reviews the terms of the management agreement and examines the effectiveness of the Company's internal control systems, receives information from the Manager's Compliance department and reviews the scope and results of the external audit, its cost effectiveness, the balance of audit and non-audit services, and the independence and objectivity of the external auditors. In the Directors' opinion, the Auditors are considered independent.

The Audit Committee also has a primary responsibility for making recommendations to the Board on the re-appointment and removal of external auditors. Representatives of the Company's Auditors attend the Audit Committee meeting at which the draft Annual Report & Accounts are considered. Having reviewed the performance of the external auditors, the Committee considered it appropriate to recommend their reappointment. The Board supported this recommendation which will be put to shareholders at the forthcoming Annual General Meeting.

In order to safeguard the Auditors' objectivity and independence, any significant non-audit services are carried out through a partner other than the audit engagement partner where appropriate.

Representatives of the Company's auditors attend the Committee meeting at which the draft annual report and accounts are considered. The Directors' statement on the Company's system of internal control is set out on page 25.

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

Relations with Shareholders

The Board regularly monitors the shareholder profile of the Company. It aims to provide shareholders with a full understanding of the Company's activities and performance and reports formally to shareholders four times a year by way of the Annual Report and Accounts, Half Year Financial Report and two Interim Management Statements. This is supplemented by the daily publication, through the London Stock Exchange, of the net asset value of the Company's shares.

All shareholders have the opportunity, and are encouraged, to attend the Company's Annual General Meeting at which the Directors and representatives of the Manager are available in person to meet with shareholders and answer questions. In addition, a presentation is given by the Investment Managers who review the Company's performance. During the year the Company's brokers and the Investment Managers hold regular discussions with larger shareholders. The Directors are made fully aware of their views. The Chairman and Directors make themselves available as and when required to address shareholder queries. The Directors may be contacted through the Company Secretary whose details are shown on page 57.

The Company's Annual Report and Accounts is published in time to give shareholders at least 20 working days' notice of the Annual General Meeting. Shareholders wishing to raise questions in advance of the meeting are encouraged to submit questions via the Company's website or write to the Company Secretary at the address shown on page 57.

Details of the proxy voting position on each resolution will be published on the Company's website shortly after the Annual General Meeting.

Section 992 Companies Act 2006

The following disclosures are made in accordance with Section 992 Companies Act 2006.

Capital Structure

The Company's capital structure is summarised on the inside front cover of this report.

Voting Rights in the Company's shares

As at 31st March 2011 (being the latest business day prior to the publication of this Notice), the Company's issued share capital consists of 99,035,719 Ordinary shares, carrying one vote each. Therefore the total voting rights of the Company are 99,035,719.

Environmental Matters, Social and Community Issues

Information about environmental matters, and social and community issues is set out on page 26. The Company has no employees.

Notifiable Interests in the Company's Voting Rights

At the date of this report, the following had declared a notifiable interest in the Company's voting rights:

Shareholders	Number of voting rights	%
AXA Investment Managers UK Ltd	11,758,440	11.87
Brewin Dolphin Ltd	7,448,588	7.52
Chase Nominees Ltd[1]	7,245,306	7.32
Rathbone Investment Management Ltd	6,719,966	6.79
Rensburg Sheppards Investment Management Ltd	4,523,961	4.57
JPMorgan Asset Management (UK) Ltd	4,218,921	4.26
Quilter	4,146,509	4.19
Legal & General Group plc	3,668,138	3.70

[1]Held on behalf of JPMAM Share Plan and ISA participants.

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.

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 affect its control following a takeover bid; and no agreements between the Company and its directors concerning compensation for loss of office.

Internal Control

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

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

Since investment management, custody of assets and all administrative services are provided to the Company by JPMAM and its associates, the Company's system of internal control mainly consists of monitoring the services provided by JPMAM and its associates, including the operating controls established by them, to ensure they meet the Company's business objectives. There is an ongoing process for identifying, evaluating and managing the significant risks faced by the Company (see Principal Risks on page 20). This process has been in place for the year under review and up to the date of approval of the Annual Report & Accounts and it accords with the Turnbull guidance. The Company does not have an internal audit function of its own, but relies on the internal audit department of JPMAM. This arrangement is kept under annual review. The key elements designed to provide effective internal control are as follows:

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

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

Management Systems – The Manager's system of internal control includes organisational agreements which clearly define the lines of responsibility,

Directors' Report – continued

delegated authority, control procedures and systems. These are monitored by JPMAM's Compliance department which regularly monitors compliance with FSA rules.

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

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

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

By the means of the procedures set out above, the Board confirms that it has reviewed the effectiveness of the Company's system of internal control for the year ended 31st January 2011, and to the date of approval of this Annual Report and Accounts.

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.

Corporate Governance and Voting Policy

The Company delegates responsibility for voting to JPMAM.

The following is a summary of JPMAM's policy statements on corporate governance, voting policy and social and environmental issues, which has been reviewed and noted by the Board.

Corporate Governance

JPMAM believes that corporate governance is integral to our investment process. As part of our commitment to delivering superior investment performance to our clients, we expect and encourage the companies in which we invest to demonstrate the highest standards of corporate governance and best business practice. We examine the share structure and voting structure of the companies in which we invest, as well as the board balance, oversight functions and remuneration policy. These analyses then form the basis of our proxy voting and engagement activity.

Proxy Voting

JPMAM manages the voting rights of the shares entrusted to it as it would manage any other asset. It is the policy of JPMAM to vote in a prudent and diligent manner, based exclusively on our reasonable judgement of what will best serve the financial interests of our clients. So far as is practicable, we will vote at all of the meetings called by companies in which we are invested.

Stewardship/Engagement

JPMAM recognises its wider stewardship responsibilities to its clients as a major asset owner. To this end, we support the introduction of the FRC Stewardship Code, which sets out the responsibilities of institutional shareholders in respect of investee companies. Under the Code, managers should:

- *publicly disclose their policy on how they will discharge their stewardship responsibilities to their clients;*
- *disclose their policy on managing conflicts of interest;*
- *monitor their investee companies;*
- *establish clear guidelines on how they escalate engagement;*
- *be willing to act collectively with other investors where appropriate;*
- *have a clear policy on proxy voting and disclose their voting record; and*
- *report to clients.*

JPMAM endorses the Stewardship Code for its UK investments and supports the principles as best practice elsewhere. We believe that regular contact with the companies in which we invest is central to our investment process and we also recognise the importance of being an 'active' owner on behalf of our clients.

Social & Environmental

JPMAM believes that companies should act in a socially responsible manner. Although our priority at all times is the best economic interests of our clients, we recognise that, increasingly, non-financial issues such as social and environmental factors have the potential to impact the share price, as well as the reputation of companies. Specialists within JPMAM's environmental, social and governance ('ESG') team are tasked with assessing how companies deal with and report on social and environmental risks and issues specific to their industry.

JPMAM is also a signatory to the United Nations Principles of Responsible Investment, which commits participants to six principles, with the aim of incorporating ESG criteria into their processes when making stock selection decisions and promoting ESG disclosure. Our detailed approach to how we implement the principles is available on request. JPMAM is *also a signatory to Carbon Disclosure Project. JPMorgan Chase is a signatory to the Equator Principles on managing social and environmental risk in project finance.*

JPMAM's Voting Policy and Corporate Governance Guidelines are available on request from the Company Secretary or can be downloaded from JPMAM's website: http://www.jpmorganassetmanagement.co.uk/Institutional/CommentaryAndAnalysis/CorporateGovernance, which also sets out its approach to the seven principles of the FRC Stewardship Code, its policy relating to conflicts of interest and its detailed voting record.

By order of the Board
Juliet Dearlove, for and on behalf of
JPMorgan Asset Management (UK) Limited,
Secretary
31st March 2011

Copies of the Combined Code and the AIC Code may be found on the respective organisations' websites: www.frc.org.uk and www.theaic.co.uk

Directors' Remuneration Report

The Board has prepared this report in accordance with the requirements of Section 421 of the Companies Act 2006. An ordinary resolution to approve this report will be put to the members at the forthcoming Annual General Meeting.

The law requires the Company's auditors to audit certain of the disclosures provided. Where disclosures have been audited they are indicated as such. The auditors' opinion is included in their report on pages 29 to 30.

With effect from 1st May 2007 Directors' fees were raised from the rate of £35,000 per annum to the rate of £45,000 per annum for the Chairman and from the rate of £25,000 per annum to the rate of £30,000 per annum for the other Directors. With effect from 17th May 2007 the fee received by the Chairman of the Audit Committee was increased from the rate of £30,000 per annum to the rate of £35,000 per annum.

In recognition of his ongoing work in respect of VAT recovery, the Chairman of the Audit Committee was awarded a discretionary bonus of £5,000 during the year under review.

The Nomination Committee reviews Directors' fees on a regular basis and makes recommendations to the Board as and when appropriate. Reviews are based on information provided by the Manager and relevant third parties on the level of fees paid to the directors of the Company's peers and within the investment trust industry generally. The Directors' fees are not performance-related. Any increase in the aggregate level of Directors' fees requires both Board and shareholder approval.

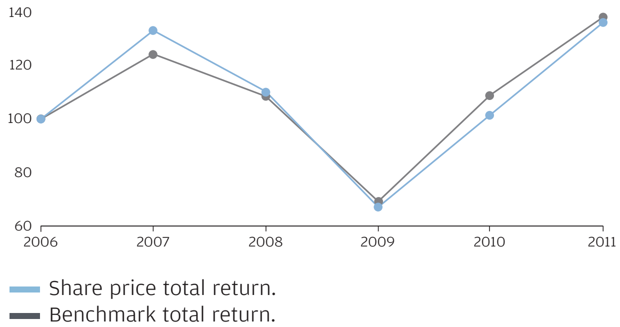
The Board's policy is that Directors' fees should properly reflect the time spent by the Directors on the Company's business and should be at a level to ensure that candidates of a high calibre are recruited to the Board. The Chairman of the Board and the Chairman of the Audit Committee are paid higher fees than the other Directors, reflecting the greater time commitment involved in fulfiling those roles.

The terms and conditions of the Directors' appointments are set out in formal letters of appointment. Details of the Board's policy on tenure are set out on page 23.

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

A graph showing the Company's share price total return compared with its benchmark index, the FTSE All-Share Index excluding FTSE 100 constituents and investment trusts, over the last five years is shown below.

Five year share price and benchmark total return to 31st January



Source: Morningstar, Russell/Mellon CAPS.

Directors' Remuneration

(Audited Information) Directors' Name	2011 £	2010 £
Hamish Leslie Melville (Chairman)	45,000	45,000
Sir Richard Beckett[1]	30,000	12,500
Richard Hambro[2]	–	7,077
Sandy Nairn	30,000	30,000
Charles Peel	30,000	30,000
Ian Russell	40,000	35,000
The Right Hon. The Earl of Halifax	30,000	30,000
Total	**205,000**	**189,577**

[1]Appointed on 1st September 2009.

[2]Died on 25th April 2009.

By order of the Board
Juliet Dearlove, for and on behalf of
JPMorgan Asset Management (UK) Limited,
Secretary
31st March 2011

Statement of Directors' Responsibilities

The Directors are responsible for preparing the Annual Report, the Directors' Remuneration Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the Directors must not approve the financial statements unless they are satisfied that they 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 accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements respectively.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements and the Directors' Remuneration Report comply with the Companies Act 2006. 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.

Each of the Directors, whose names and functions are listed in the Directors' Report confirm that, to the best of their knowledge:

- the financial statements, which have been prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), give a true and fair view of the assets, liabilities, financial position and return or loss of the Company; and
- the Directors' 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 it faces.

For and on behalf of the Board
Hamish Leslie Melville
Chairman
31st March 2011

Independent Auditors' Report

To the members of The Mercantile Investment Trust plc

We have audited the financial statements of The Mercantile Investment Trust plc for the year ended 31st January 2011 which comprise the Income Statement, Reconciliation of Movements in Shareholders' Funds, Balance Sheet, Cash Flow Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Respective responsibilities of Directors and Auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 28, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 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.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the financial statements.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31st January 2011 and of its net return and cash flows for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the Directors' statement, set out on page 21, in relation to going concern; and
- the parts of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the 2008 Combined Code specified for our review.

Jeremy Jensen (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London

31st March 2011

Notes:

(a) The maintenance and integrity of The Mercantile Investment Trust plc website (www.mercantileit.co.uk) is the responsibility of the Directors; the work carried out by the Auditors does not involve consideration of these matters and, accordingly, the Auditors accept no responsibility for any changes that may have occurred to the accounts since they were initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Income Statement

for the year ended 31st January 2011

	Notes	2011 Revenue £'000	2011 Capital £'000	2011 Total £'000	2010 Revenue £'000	2010 Capital £'000	2010 Total £'000
Gains on investments held at fair value through profit or loss	2	–	249,190	249,190	–	362,020	362,020
Net foreign currency gains/(losses)		–	26	26	–	(78)	(78)
Income from investments	3	30,631	–	30,631	27,899	–	27,899
Other interest receivable and similar income	3	1,606	–	1,606	4,349	–	4,349
Gross return		32,237	249,216	281,453	32,248	361,942	394,190
Management fee	4	(1,407)	(3,282)	(4,689)	(1,971)	(1,971)	(3,942)
Other administrative expenses	5	(723)	–	(723)	(1,022)	–	(1,022)
Net return on ordinary activities before finance costs and taxation		30,107	245,934	276,041	29,255	359,971	389,226
Finance costs	6	(3,320)	(7,748)	(11,068)	(5,489)	(5,489)	(10,978)
Net return on ordinary activities before taxation		26,787	238,186	264,973	23,766	354,482	378,248
Taxation	7	(18)	–	(18)	(63)	–	(63)
Net return on ordinary activities after taxation		26,769	238,186	264,955	23,703	354,482	378,185
Return per share	9	26.91p	239.48p	266.39p	23.18p	346.63p	369.81p

Dividends declared in respect of the financial year ended 31st January 2011 total 36.0p (2010: 36.0p) per share amounting to £35,657,000 (2010: £36,753,000). Further information on dividends is given in note 8 on page 40.

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

The 'total' column of this statement is the profit and loss account of the Company, and the 'revenue' and 'capital' columns represent supplementary information prepared under guidance issued by the Association of Investment Companies. The total column represents all the information that is required to be disclosed in a Statement of Total Recognised Gains and Losses ('STRGL'). For this reason, a STRGL has not been presented.

The notes on pages 35 to 51 form an integral part of these accounts.

Reconciliation of Movements in Shareholders' Funds

for the year ended 31st January 2011

	Called up share capital £'000	Share premium £'000	Capital redemption reserve £'000	Capital reserves £'000	Revenue reserve £'000	Total £'000
At 31st January 2009	25,580	23,459	11,190	577,602	59,467	697,298
Repurchase and cancellation of the Company's own shares	(93)	–	93	(3,299)	–	(3,299)
Net return on ordinary activities	–	–	–	354,482	23,703	378,185
Dividends appropriated in the year	–	–	–	–	(36,808)	(36,808)
At 31st January 2010	25,487	23,459	11,283	928,785	46,362	1,035,376
Repurchase and cancellation of the Company's own shares	(728)	–	728	(27,273)	–	(27,273)
Net return on ordinary activities	–	–	–	238,186	26,769	264,955
Dividends appropriated in the year	–	–	–	–	(35,792)	(35,792)
At 31st January 2011	24,759	23,459	12,011	1,139,698	37,339	1,237,266

The notes on pages 35 to 51 form an integral part of these accounts.

Balance Sheet

at 31st January 2011

	Notes	2011 £'000	2010 £'000
Fixed assets			
Investments held at fair value through profit or loss	10	1,347,562	1,158,236
Current assets	12		
Debtors		4,030	19,647
Cash and short term deposits		89,530	40,225
		93,560	59,872
Creditors: amounts falling due within one year	13	(26,859)	(5,831)
Net current assets		66,701	54,041
Total assets less current liabilities		1,414,263	1,212,277
Creditors: amounts falling due after more than one year	14	(176,997)	(176,901)
Net assets		1,237,266	1,035,376
Capital and reserves			
Called up share capital	15	24,759	25,487
Share premium	16	23,459	23,459
Capital redemption reserve	16	12,011	11,283
Capital reserves	16	1,139,698	928,785
Revenue reserve	16	37,339	46,362
Total equity shareholders' funds		1,237,266	1,035,376
Net asset value per share	17	1,249.3p	1,015.6p

The accounts on pages 31 to 51 were approved and authorised for issue by the Directors on 30th March 2011 and are signed on their behalf by:

Hamish Leslie Melville
Chairman

The notes on pages 35 to 51 form an integral part of these accounts.

The Mercantile Investment Trust plc

Company registration number 20537

Cash Flow Statement

for the year ended 31st January 2011

	Notes	2011 £'000	2010 £'000
Net cash inflow from operating activities	18	26,671	25,045
Servicing of finance			
Interest paid		(10,954)	(10,882)
Net cash outflow from servicing of finance		(10,954)	(10,882)
Financial investment			
Purchases of investments		(1,154,341)	(1,019,054)
Sales of investments		1,236,936	912,996
Other capital charges		(31)	(24)
Net cash inflow/(outflow) from financial investment		82,564	(106,082)
Dividends paid		(35,780)	(36,820)
Net cash inflow/(outflow) before financing		62,501	(128,739)
Financing			
Increase in short term loans		15,000	–
Repurchase and cancellation of the Company's own shares		(28,222)	(2,350)
Net cash outflow from financing		(13,222)	(2,350)
Increase/(decrease) in cash in the year	19	49,279	(131,089)

The notes on pages 35 to 51 form an integral part of these accounts.

Notes to the Accounts

for the year ended 31st January 2011

1. Accounting Policies

(a) Basis of accounting

The accounts are prepared in accordance with the Companies Act 2006. United Kingdom Generally Accepted Accounting Practice ('UK GAAP') and with the Statement of Recommended Practice 'Financial Statements of Investment Trust Companies and Venture Capital Trusts' (the 'SORP') issued by the Association of Investment Companies in January 2009. All of the Company's operations are of a continuing nature.

The accounts have been prepared on a going concern basis under the historical cost convention, as modified by the revaluation of investments at fair value.

The policies applied in these accounts are consistent with those applied in the preceding year.

(b) Valuation of investments

The Company's business is investing in financial assets with a view to profiting from their total return in the form of income and capital growth. This portfolio of financial assets is managed and its performance evaluated on a fair value basis, in accordance with a documented investment strategy and information is provided internally on that basis to the Company's Board of Directors. Accordingly, upon initial recognition the investments are designated by the Company as 'held at fair value through profit or loss'. They are included initially at fair value which is taken to be their cost, excluding expenses incidental to purchase which are written off to capital at the time of acquisition. Subsequently the investments are valued at fair value, which are quoted bid prices for investments traded in active markets. For investments which are not traded in active markets, unlisted and restricted investments, the Board takes into account the latest traded prices, other observable market data and asset values based on the latest management accounts.

Gains and losses on sales of investments including the related foreign exchange gains and losses of a capital nature, are included in the Income Statement and in capital reserves within 'Gains and losses on sales of investments'. Increases and decreases in the valuation of investments held at the year end, including the related gains and losses arising from changes in foreign exchange rates, are included in the Income Statement and in capital reserves within 'Holding gains and losses on investments'.

All purchases and sales are accounted for on a trade date basis.

(c) Income

Dividends receivable from equity shares are included in revenue on an ex-dividend basis except where, in the opinion of the Board, the dividend is capital in nature, in which case it is included in capital.

UK dividends are included net of tax credits. Overseas dividends are included gross of any withholding tax.

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

Interest receivable from debt securities, together with any premiums or discounts on purchase, are allocated to revenue on a time apportionment basis so as to reflect the effective interest rate of those securities.

Deposit interest receivable is taken to revenue on an accruals basis.

Underwriting commission is taken to revenue on a receipts basis. Underwriting commission is recognised in revenue where it relates to shares that the Company is not required to take up. Where the Company is required to take up a proportion of the shares underwritten, the same proportion of commission received is deducted from the cost of the shares taken up, with the balance taken to revenue.

(d) Expenses

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

- With effect from 1st February 2010 the Company allocates 70% of the management fee to capital and the remaining 30% to revenue. It had previously allocated 50% of the management fee to capital and 50% to revenue. It remains the Board's determination that the capital return should reflect the indirect costs of earning capital returns and it monitors the assumptions that underpin the basis of allocation. It concluded from its most recent review that a greater proportion of the Company's long term investment returns will come from capital than was previously expected. The effect of this change is to increase the net revenue return after taxation by £938,000 and to reduce the net capital return by the same amount. Total net return after taxation is unaffected by the change. The comparative figures have not been restated.
- expenses incidental to the purchase of an investment are included within the cost of the investment and those incidental to the sale are deducted from the sale proceeds. These expenses are commonly referred to as transaction costs and comprise brokerage commission and stamp duty. Details of transaction costs are given in note 10 on page 41.

Notes to the Accounts – continued

(e) **Finance costs**

Finance costs are accounted for on an accruals basis using the effective interest rate method and in accordance with the provisions of FRS 25 'Financial Instruments: Presentation' and FRS 26 'Financial Instruments: Measurement'.

With effect from 1st February 2010 the Company allocates 70% of finance costs to capital and the remaining 30% to revenue. It had previously allocated 50% of finance costs to capital and 50% to revenue. It remains the Board's determination that the capital return should reflect the indirect costs of earning capital returns and it monitors the assumptions that underpin the basis of allocation. It concluded from its most recent review that a greater proportion of the Company's long term investment returns will come from capital than was previously expected. The effect of this change is to increase the net revenue return after taxation by £2,214,000 and to reduce the net capital return by the same amount. Total net return after taxation is unaffected by the change. The comparative figures have not been restated.

Breakage costs incurred on the early repayment of loans are charged 100% to capital.

(f) **Financial instruments**

Cash and short term deposits may comprise cash and demand deposits which are readily convertible to a known amount of cash and are subject to insignificant risk of changes in value.

Other debtors and creditors do not carry any interest, are short term in nature and are accordingly stated at nominal value, with debtors reduced by appropriate allowances for estimated irrecoverable amounts.

The debentures in issue, bank loans and overdrafts are classified as loans and receivables and are measured at amortised cost. They are recorded at the proceeds received net of direct issue costs. Finance costs, including any premiums payable on settlement or redemption and direct issue costs, are accounted for on an accruals basis using the effective interest rate method.

(g) **Taxation**

Deferred tax is accounted for in accordance with FRS 19: 'Deferred Tax'.

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

Tax relief is allocated to expenses charged to the capital column of the income statement on the 'marginal basis'. On this basis, if taxable income is capable of being entirely offset by revenue expenses, then no tax relief is transferred to the capital column.

Deferred tax is measured at the tax rate which is expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates that have been enacted or substantively enacted at the balance sheet date and is measured on an undiscounted basis.

(h) **VAT**

Expenses are disclosed inclusive of the related irrecoverable VAT. Recoverable VAT is calculated using the partial exemption method, based on the proportion of zero rated supplies to total supplies.

(i) **Foreign currency**

In accordance with FRS 23: 'The effects of changes in Foreign Currency Exchange Rates' the Company is required to nominate a functional currency, being the currency in which the Company predominantly operates. The Board, having regard to the currency of the Company's share capital and the predominant currency in which its shareholders operate, has determined that sterling is the functional currency. Sterling is the also the currency in which the accounts are presented.

Transactions denominated in foreign currencies are converted at actual exchange rates as at the date of the transaction. Monetary assets, liabilities and equity investments held at fair value, denominated in foreign currencies at the year end are translated at the rates of exchange prevailing at the year end.

Foreign exchange gains and losses on cash and deposit balances are included in the Income Statement and in capital reserves within 'Gains and losses on sales of investments'.

(j) **Dividends payable**

In accordance with FRS 21: 'Events after the Balance Sheet Date', dividends are included in the accounts in the year in which they are paid.

(k) **Repurchases of ordinary shares for cancellation**

The cost of repurchasing ordinary shares including the related stamp duty and transactions costs is charged to capital reserves and dealt with in the Reconciliation of Movement in Shareholders' Funds. Share repurchase transactions are accounted for on a trade date basis. The nominal value of ordinary share capital repurchased and cancelled is transferred out of a called up share capital and into the capital redemption reserve.

2. Gains on investments held at fair value through profit or loss

	2011 £'000	2010 £'000
Gains/(losses) on investments held at fair value through profit or loss based on historical cost	144,292	(62,046)
Amounts recognised in investment holding gains and losses in the previous year in respect of investments sold during the year	(45,924)	211,772
Gains on sales of investments based on the carrying value at the previous balance sheet date	98,368	149,726
Net movement in investment holding gains and losses	150,858	212,317
Other capital charges	(36)	(23)
Total capital gains on investments held at fair value through profit or loss	249,190	362,020

3. Income

	2011 £'000	2010 £'000
Income from investments		
UK dividends	24,858	23,817
UK bond interest	438	451
Property income distributions	362	575
Overseas dividends	4,917	3,056
Scrip dividends	56	–
	30,631	27,899
Other interest receivable and similar income		
Deposit interest	364	323
Underwriting commission	1,242	3,989
Distribution on dissolution of subsidiary	–	37
	1,606	4,349
Total income	32,237	32,248

Notes to the Accounts – continued

	2011 Revenue £'000	2011 Capital £'000	2011 Total £'000	2010 Revenue £'000	2010 Capital £'000	2010 Total £'000
4. Management fee						
Management fee[1]	1,407	3,282	4,689	1,971	1,971	3,942

[1]Details of the management fee are given in the Directors' Report on page 21.

	2011 £'000	2010 £'000
5. Other administrative expenses		
Administration expenses	370	534
Directors' fees[1]	205	190
Savings scheme costs[2]	111	164
Auditors' remuneration for audit services[3]	36	35
Auditors' remuneration for all other services[4]	1	99
	723	1,022

[1]Full disclosure is given in the Directors' Remuneration Report on page 27.

[2]These amounts were paid to JPMAM for the marketing and administration of saving scheme products.

[3]Includes £6,000 (2010: £5,000) irrecoverable VAT.

[4]Includes £200 (2010: £13,000) irrecoverable VAT. The comparative figure includes £98,000 in respect of an action against HMRC to recover VAT paid on management fees.

	2011 Revenue £'000	2011 Capital £'000	2011 Total £'000	2010 Revenue £'000	2010 Capital £'000	2010 Total £'000
6. Finance costs						
Interest on bank loans and overdrafts	27	63	90	–	–	–
Debenture interest	3,264	7,618	10,882	5,441	5,441	10,882
Amortisation of debenture issue costs	29	67	96	48	48	96
	3,320	7,748	11,068	5,489	5,489	10,978

	2011 £'000	2010 £'000
7. Taxation		
(a) Analysis of tax charge in the year		
Overseas withholding tax	18	63
Current tax charge for the year	18	63

(b) Factors affecting the current tax charge for the year

The tax assessed for the year is lower (2010: lower) than the standard rate of corporation tax in the UK of 28% (2010: 28%). The factors affecting the current tax charge for the year are as follows:

	2011			2010		
	Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
Net return on ordinary activities before taxation	26,787	238,186	264,973	23,766	354,482	378,248
Net return on ordinary activities before taxation multiplied by the Company's applicable rate of corporation tax of 28% (2010: 28%)	7,500	66,692	74,192	6,655	99,255	105,910
Effect of:						
Non taxable scrip dividends	(16)	–	(16)	–	–	–
Non taxable UK dividend income	(6,960)	–	(6,960)	(6,669)	–	(6,669)
Non taxable overseas dividend income	(1,377)	–	(1.377)	(392)	–	(392)
Non taxable capital return	–	(69,780)	(69,780)	–	(101,344)	(101,344)
Unrelieved expenses	853	3,088	3,941	406	2,089	2,495
Overseas withholding tax	18	–	18	63	–	63
	18	–	18	63	–	63

(c) Deferred taxation

The Company has an unrecognised deferred tax asset of £42,610,000 (2010: £40,248,000) based on a prospective corporation tax rate of 27%. The Finance Act 2010, which provides for a reduction in the main rate of corporation tax from 28% to 27% effective from 1st April 2011, was substantively enacted on 21st July 2010. The Government has also indicated that it intends to enact future reductions in the main rate of corporation tax of 1% each year, down to 24% by 1st April 2014. The deferred tax asset has arisen due to the cumulative excess of deductible expenses over taxable income. Given the composition of the Company's portfolio, it is not likely that this asset will be utilised in the foreseeable future.

Given the Company's status as an investment trust company, and the intention to continue meeting the conditions required to obtain approval, the Company has not provided for deferred tax on any capital gains or losses arising on the revaluation or disposal of investments.

Notes to the Accounts – continued

8. Dividends

(a) Dividends paid and declared

	2011 £'000	2010 £'000
Unclaimed dividends refunded to the Company[1]	–	(12)
2010 fourth quarterly dividend of 18.0p (2009: 18.0p) paid to shareholders in May	17,961	18,418
First quarterly dividend of 6.0p (2010: 6.0p) paid to shareholders in August	5,945	6,139
Second quarterly dividend of 6.0p (2010: 6.0p) paid to shareholders in November	5,944	6,139
Third quarterly dividend of 6.0p (2010: 6.0p) paid to shareholders in February[2]	5,942	6,124
Total dividends paid in the year	35,792	36,808

[1]Represents dividends which remain unclaimed after a period of 6 years and thereby become the property of the Company.
[2]Paid to the Registrars in January.

	2011 £'000	2010 £'000
Fourth quarterly dividend declared of 18.0p (2010: 18.0p) payable to shareholders in May	17,826	18,351

The fourth quarterly dividend declared in respect of the year ended 31st January 2010 amounted to £18,351,000, however the actual payment amounted to £17,961,000 due to shares repurchased and cancelled after the Balance Sheet date but prior to the share register Record Date.

The fourth quarterly dividend has been declared in respect of the year ended 31st January 2011. In accordance with the accounting policy of the Company, this dividend will be reflected in the accounts for the year ending 31st January 2012.

(b) Dividends for the purposes of Section 1158 of the Corporation Tax Act 2010 ('Section 1158')

The requirements of Section 1158 are considered on the basis of dividends declared in respect of the financial year as shown below. The revenue available for distribution by way of dividend for the year is £26,769,000 (2010: £23,703,000).

	2011 £'000	2010 £'000
First quarterly dividend of 6.0p (2010: 6.0p) paid in August	5,945	6,139
Second quarterly dividend of 6.0p (2010: 6.0p) paid in November	5,944	6,139
Third quarterly dividend of 6.0p (2010: 6.0p) paid in February	5,942	6,124
Fourth quarterly dividend of 18.0p (2010: 18.0p) payable in May	17,826	18,351
	35,657	36,753

9. Return per share

The revenue return per share is based on the earnings attributable to the ordinary shares of £26,769,000 (2010: £23,703,000) and on the weighted average number of ordinary shares in issue during the year of 99,461,672 (2010: 102,264,780).

The capital return per share is based on the capital return attributable to the ordinary shares of £238,186,000 (2010: £354,482,000) and on the weighted average number of ordinary shares in issue during the year of 99,461,672 (2010: 102,264,780).

The total return per share is based on the total return attributable to the ordinary shares of £264,955,000 (2010: £378,185,000) and on the weighted average number of ordinary shares in issue during the year of 99,461,672 (2010: 102,264,780).

	2011 £'000	2010 £'000
10. Investments		
Investments listed on a recognised stock exchange	1,232,085	1,046,524
Investments listed on AIM and unlisted investments	115,586	111,712
	1,347,671	1,158,236

	Listed in UK £'000	Listed Overseas £'000	AIM and Unlisted £'000	Total £'000
Opening book cost	961,114	16,041	107,207	1,084,362
Opening investment holding gains/(losses)	74,132	(4,763)	4,505	73,874
Opening valuation	1,035,246	11,278	111,712	1,158,236
Movements in the year:				
Purchases at cost	1,134,582	8,003	18,802	1,161,387
Sales – proceeds	(1,165,354)	(12,283)	(43,650)	(1,221,287)
Gains on sales of investments based on the carrying value at the previous balance sheet date	83,261	(114)	15,221	98,368
Transfer – stock suspended pending delisting	(1,891)	–	1,891	–
Net movement in investment holding gains and losses	131,144	8,213	11,501	150,858
	1,216,988	15,097	115,477	1,347,562
Closing book cost	1,075,314	6,884	86,556	1,168,754
Closing investment holding gains	141,674	8,213	28,921	178,808
Total investments held at fair value through profit or loss	1,216,988	15,097	115,477	1,347,562

Transaction costs on purchases during the year amounted to £6,128,000 (2010: £4,884,000) and on sales during the year amounted to £1,610,000 (2010: £1,257,000). These costs comprise stamp duty and brokerage commission.

Investments include Alternative Investment Market stocks which are valued at £109,512,000 (2010: £91,409,000).

During the year, prior year revaluation gains amounting to £45,924,000 have been transferred to gains on sales of investments as disclosed in note 16.

11. Significant interests

Details of investments in which the Company has an interest of 3% or more of the nominal value of the allotted shares of any class and which are valued in the portfolio in excess of £10 million, are as follows:

Name of company	Country of registration	Class of share	% of class held
Renovo	UK	Ordinary	10.0
VP	UK	Ordinary	9.6
Cove Energy	UK	Ordinary	6.6
MP Evans	UK	Ordinary	6.0
Xchanging	UK	Ordinary	4.1
Vectura	UK	Ordinary	4.0
Wolfson Microelectronics	UK	Ordinary	4.0
Go-Ahead	UK	Ordinary	3.9
Bovis Homes	UK	Ordinary	3.2

The Company has interests of 3% or more in the share capital of 31 (2010: 32) investee companies.

The Company does not exercise significant influence over the operating and financial policies of the above mentioned companies which are therefore not considered to be associated companies. The total value of investments in which the Company had an interest of 3% or more at 31st January 2011 was £277,040,000 (2010: £162,488,000).

Notes to the Accounts – continued

	2011 £'000	2010 £'000
12. Current assets		
Debtors		
Securities sold awaiting settlement	2,078	17,727
Dividends and interest receivable	1,783	1,788
Other debtors	169	132
	4,030	19,647

The Directors consider that the carrying amount of debtors approximates to their fair value.

Cash and short term deposits

Cash and short term deposits comprises bank balances and short term deposits. The carrying amount of these represents their fair value. Cash balances in excess of a predetermined amount are placed on short term deposit at market rates of interest.

	2011 £'000	2010 £'000
13. Creditors: amounts falling due within one year		
Securities purchased awaiting settlement	6,990	–
Repurchases of the Company's own shares awaiting settlement	–	949
Bank loan	15,000	–
Other creditors and accruals	4,869	4,882
	26,859	5,831

The bank loan is unsecured and is drawn down on the Company's £45 million loan facility with ING Bank. Further details are given in note 23(a)(i) on page 47.

The Directors consider that the carrying amount of creditors falling due within one year approximates to their fair value.

	2011 £'000	2010 £'000
14. Creditors: amounts falling due after more than one year		
Falling due after more than five years		
£3,850,000 4.25% perpetual debenture stock[1]	3,850	3,850
£175 million 6.125% debenture stock[2]	173,147	173,051
	176,997	176,901

[1]The £3,850,000 4.25% debenture stock is irredeemable and secured by a floating charge over the assets of the Company. The debenture is repayable at 105% if the Company goes into default and the security is enforced.

[2]The £175 million 6.125% debenture stock is repayable on 25th February 2030 and is secured by a floating charge over the assets of the Company.

	2011 £'000	2010 £'000
15. Called up share capital		
Allotted and fully paid:		
Opening balance of 101,947,968 (2010: 102,321,968) shares of 25p each	25,487	25,580
Repurchase and cancellation of 2,912,249 (2010: 374,000) shares	(728)	(93)
Closing balance of 99,035,719 (2010: 101,947,968) shares of 25p each	24,759	25,487

During the year, the Company made market purchases of 2,912,249 of its own shares, nominal value £728,000, for cancellation, representing 2.9% of the shares outstanding at the beginning of the year. The total consideration paid for these shares amounted to £27,273,000.

16. Reserves

	Called up share capital £'000	Share premium £'000	Capital redemption reserve £'000	Capital reserves: Gains on sales of investments £'000	Capital reserves: Investment holding gains £'000	Revenue reserve £'000	Total £'000
Opening balance	25,487	23,459	11,283	854,911	73,874	46,362	1,035,376
Net currency gains on cash and short term deposits held during the year	–	–	–	26	–	–	26
Gains on sales of investments based on the carrying value at the previous balance sheet date	–	–	–	98,368	–	–	98,368
Net movement in investment holding gains and losses	–	–	–	–	150,858	–	150,858
Transfer on disposal of investments	–	–	–	45,924	(45,924)	–	–
Repurchase and cancellation of the Company's own shares	(728)	–	728	(27,273)	–	–	(27,273)
Management fee and finance costs charged to capital	–	–	–	(11,030)	–	–	(11,030)
Other capital charges	–	–	–	(36)	–	–	(36)
Dividends appropriated in the year	–	–	–	–	–	(35,792)	(35,792)
Retained revenue for the year	–	–	–	–	–	26,769	26,769
Closing balance	24,759	23,459	12,011	960,890	178,808	37,339	1,237,266

17. Net asset value per share

The net asset value per share is based on the net assets attributable to the ordinary shareholders of £1,237,266,000 (2010: £1,035,376,000) and on the 99,035,719 (2010: 101,947,968) shares in issue at the year end.

18. Reconciliation of net return on ordinary activities before finance costs and taxation to net cash inflow from operating activities

	2011 £'000	2010 £'000
Total return on ordinary activities before finance costs and taxation	276,041	389,226
Less capital return on ordinary activities before finance costs and taxation	(245,934)	(359,971)
Scrip dividends received as income	(56)	–
Decrease/(increase) in accrued income	5	(595)
Increase in other debtors	(37)	(16)
Decrease in accrued expenses	(34)	(1,529)
Management fee charged to capital	(3,282)	(1,971)
Overseas withholding tax	(32)	(62)
Distribution on dissolution of subsidiary	–	(37)
Net cash inflow from operating activities	26,671	25,045

Notes to the Accounts – continued

	At 31st January 2010 £'000	Cash flow £'000	Other exchange movement £'000	Non cash movements £'000	At 31st January 2011 £'000
19. Analysis of changes in net debt					
Cash and short term deposits	40,225	49,279	26	–	89,530
Bank loans falling due within one year	–	(15,000)	–	–	(15,000)
Debentures falling due after more than five years	(176,901)	–	–	(96)	(176,997)
Net debt	(136,676)	34,279	26	(96)	(102,467)

20. Contingent liabilities and capital commitments

At the balance sheet date there were no contingent liabilities or capital commitments.

21. Transactions with JPMorgan

Details of the management contract are set out in the Directors' Report on page 20. The management fee payable to JPMorgan Asset Management (UK) Limited ('JPMAM') for the year was £4,689,000 (2010: £3,942,000) of which £nil (2010: £nil) was outstanding at the year end.

During the year £111,000 (2010: £164,000) was payable to JPMAM for the marketing and administration of savings scheme products, of which £nil (2010: £nil) was outstanding at the year end.

Included in other management expenses in note 5 on page 38 are safe custody fees amounting to £16,000 (2010: £26,000) payable to JPMorgan Chase of which £6,000 (2010: £10,000) was outstanding at the year end.

JPMAM may carry out some of its dealing transactions through group subsidiaries. These transactions are carried out at arm's length. The commission payable to JPMorgan Securities for the year was £144,000 (2010: £19,000) of which £nil (2010: £nil) was outstanding at the year end.

During the year, commission on dealing transactions amounting to £465,000 (2010: £537,000) was paid to JPMorgan subsidiaries of which £nil (2010: £nil) was outstanding at the year end.

Handling charges on dealing transactions amounting to £36,000 (2010: £23,000) were payable to JPMorgan Chase during the year of which £14,000 (2010: £8,000) was outstanding at the year end.

At the year end, a bank balance of £89.5 million (2010: £40.2 million) was held with JPMorgan Chase. A net amount of interest of £0.4 million (2010: £0.3 million) was receivable by the Company during the year from JPMorgan Chase of which £7,000 (2010: £7,000) was outstanding at the year end.

22. Disclosures regarding financial instruments measured at fair value

The Company's financial instruments within the scope of FRS 29 that are held at fair value comprise its investment portfolio. The Company currently holds no derivative financial instruments and its liabilities are not held at fair value.

The investments are categorised into a hierarchy consisting of the following three levels:

Level 1 – valued using quoted prices in active markets.

Level 2 – valued by reference to valuation techniques using observable inputs other than quoted market prices included within Level 1.

Level 3 – valued by reference to valuation techniques using inputs that are not based on observable market data.

Categorisation within the hierarchy has been determined on the basis of the lowest level input that is significant to the fair value measurement of the relevant asset.

Details of the valuation techniques used by the Company are given in note 1 on page 35.

The following table sets out the fair value measurements using the FRS 29 hierarchy at 31st January:

	2011			
	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
Financial assets held at fair value through profit or loss at 31st January 2011				
Equity investments	1,338,526	3,071	5,871	1,347,468
Fixed interest investments	–	–	94	94
Total	1,338,526	3,071	5,965	1,347,562

	2010			
	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
Financial assets held at fair value through profit or loss at 31st January 2010				
Equity investments	1,137,933	–	17,961	1,155,894
Fixed interest investments	–	–	2,342	2,342
Total	1,137,933	–	20,303	1,158,236

There have been no transfers between Levels 1 and 2 during the year (2010: nil). A reconciliation of the fair value measurements in Level 3 is set out below.

	2011		
	Equity investments £'000	Fixed interest investments £'000	Total £'000
Level 3 financial assets held at fair value through profit or loss at 31st January 2011			
Opening balance	17,961	2,342	20,303
Sales – proceeds	(14,248)	(2,698)	(16,946)
Transfers into Level 3	1,891	–	1,891
Gains on sales of investments based on the carrying value at the previous balance sheet date	6,030	450	6,480
Net movement in investment holding gains and losses	(5,763)	–	(5,763)
Closing balance	5,871	94	5,965

The transfer into Level 3 relates to one stock which was suspended at the year end, pending delisting from the FTSE Small-Cap Index.

Included in the table above are the sales proceeds from the disposal of JPMorgan Cazenove during the year, amounting to £14,234,000. The cost of this investment amounted to £7,887,000 and the carrying value at the previous balance sheet date was £14,234,000.

Notes to the Accounts – continued

22. Disclosures regarding financial instruments measured at fair value – continued

	2010 Equity investments £'000	2010 Fixed interest investments £'000	2010 Total £'000
Level 3 financial assets held at fair value through profit or loss at 31st January 2010			
Opening balance	16,492	94	16,586
Sales – proceeds	(4,928)	–	(4,928)
Transfers into Level 3	119	2,248	2,367
Gains on sales of investments based on the carrying value at the previous balance sheet date	1,154	–	1,154
Net movement in investment holding gains and losses	5,124	–	5,124
Closing balance	17,961	2,342	20,303

The transfers into Level 3 relate to one stock which has been de-listed from the Alternative Investment Market and a corporate bond which was acquired as part of a company reconstruction.

23. Financial instruments' exposure to risk and risk management policies

As an investment trust, the Company invests in equities for the long term so as to secure its investment objective stated on the 'Features' page. In pursuing this objective, the Company is exposed to a variety of financial risks that could result in a reduction in the Company's net assets or a reduction in the profits available for dividends.

These financial risks include market risk (comprising interest rate risk and market price risk), liquidity risk and credit risk. The Directors' policy for managing these risks is set out below. The Company Secretary, in close cooperation with the Board and the Manager, coordinates the Company's risk management policy. The Company has no significant direct exposure to foreign exchange risk.

The objectives, policies and processes for managing the risks and the methods used to measure the risks that are set out below, have not changed from those applying in the comparative year.

The Company's classes of financial instruments are as follows:

- investments in equity shares and other securities, which are held in accordance with the Company's investment objective;
- short term debtors, creditors and cash arising directly from its operations;
- a sterling loan facility with ING Bank, the purpose of which is to finance the Company's operations; and
- debentures issued by the Company, the purpose of which is to finance the Company's operations.

(a) Market risk

The fair value or future cash flows of a financial instrument held by the Company may fluctuate because of changes in market prices. This market risk comprises two elements – interest rate risk and market price risk. Information to enable an evaluation of the nature and extent of these two elements of market risk is given in parts (i) and (ii) of this note, together with sensitivity analyses where appropriate. The Board reviews and agrees policies for managing these risks and these policies have remained unchanged from those applying in the comparative year. The 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) Interest rate risk

Interest rate movements may affect the level of income receivable on cash deposits and the interest payable on variable rate borrowings when interest rates are re-set.

Management of interest rate risk

Liquidity and borrowings are managed with the aim of increasing returns to shareholders. The Company's gearing policy is to limit gearing within the range 90% to 120% where gearing is defined as investments expressed as a percentage of total net assets.

The possible effects on cash flows that could arise as a result of changes in interest rates are taken into account when the Company borrows on the loan facility. However, amounts drawn down on this facility are for short term periods and therefore exposure to interest rate risk is not significant.

Interest rate exposure

The two series of debentures issued by the Company both carry fixed rates of interest and were issued as a planned level of gearing. This debenture stock is carried in the Company's balance sheet at amortised cost rather than fair value. Hence movement in interest rates will not affect equity but may have an impact on the share price and discount which is not likely to be material.

The Company has no significant holdings of fixed interest rate securities whose fair value would be affected by interest rate movements.

The Company does not normally hold a significantly high level of cash balances and there is an overdraft facility available when required.

The exposure of financial assets and financial liabilities to floating interest rates, giving cash flow interest rate risk when rates are re-set, is shown below:

	2011 £'000	2010 £'000
Exposure to floating interest rates		
Cash at bank and short term deposits	89,530	40,225
Creditors: amounts falling due within one year – borrowings on the loan facility	(15,000)	–
Total exposure	74,530	40,225

Interest receivable on cash balances, or paid on overdrafts, is at a margin below or above LIBOR respectively (2010: same).

During the year, the Company arranged a £45 million one year floating rate loan facility with ING bank, which expires in January 2012. Interest is payable at a rate of LIBOR as quoted in the market for the loan period plus a margin of 1.45% per annum, plus Mandatory Costs, which are the lender's costs of complying with certain regulatory requirements of the Bank of England. At 31st January 2011, the Company had drawn down £15 million on this facility at an interest rate of 2.524% per annum.

The above year end amounts are not representative of the exposure to interest rates during the year as the level of cash balances and drawings on the loan facility have fluctuated. The maximum and minimum net cash balances during the year are as follows:

	2011 £'000	2010 £'000
Maximum interest rate exposure during the year – net cash balances	215,261	149,565
Minimum interest rate exposure during the year – net cash balances	6,986	33,036

Interest rate sensitivity

The following table illustrates the sensitivity of the return after taxation for the year and net assets to a 1% (2010: 1%) increase or decrease in interest rates in regards to the Company's monetary financial assets and financial liabilities. This level of change is considered to be a reasonable illustration based on observation of current market conditions. The sensitivity analysis is based on the Company's monetary financial instruments held at the balance sheet date with all other variables held constant.

Notes to the Accounts – continued

23. Financial instruments' exposure to risk and risk management policies – continued

(a) Market risk – continued

(i) Interest rate risk – continued

	2011		2010	
	1% Increase in rate £'000	1% Decrease in rate £'000	1% Increase in rate £'000	1% Decrease in rate £'000
Income statement – return after taxation				
Revenue return	850	(850)	402	(402)
Capital return	(105)	105	–	–
Total return after taxation	745	(745)	402	(402)
Net assets	745	(745)	402	(402)

In the opinion of the Directors, this sensitivity analysis may not be representative of the Company's future exposure to interest rate changes due to fluctuations in the level of cash balances and drawings on the loan facility.

(ii) Market price risk

Market price risk includes changes in market prices, other than those arising from interest rate risk, which may affect the value of equity investments.

Management of market price risk

The Board meets on at least four occasions each year to consider the asset allocation of the portfolio and the risk associated with particular industry sectors. The investment management team has responsibility for monitoring the portfolio, which is selected in accordance with the Company's investment objective and seeks to ensure that individual stocks meet an acceptable risk/reward profile.

Market price risk exposure

The Company's total exposure to changes in market prices at 31st January comprises its holdings in equity investments as follows:

	2011 £'000	2010 £'000
Equity investments held at fair value through profit or loss	1,347,468	1,155,894

The above data is broadly representative of the exposure to market price risk during the year.

Concentration of exposure to market price risk

An analysis of the Company's investments is given on pages 15 to 16 This shows that the majority of the investments' value is in the UK. Accordingly there is a concentration of exposure to that country. However it should be noted that an investment may not be entirely exposed to the economic conditions in its country of domicile or of listing.

Market price risk sensitivity

The following table illustrates the sensitivity of the return after taxation for the year and net assets to an increase or decrease of 10% (2010: 20%) in the fair values of the Company's equities. This level of change is considered to be a reasonable illustration based on observation of current market conditions. The sensitivity analysis is based on the Company's equities, adjusting for changes in the management fee but with all other variables held constant.

	2011 10% Increase in fair value £'000	2011 10% Decrease in fair value £'000	2010 20% Increase in fair value £'000	2010 20% Decrease in fair value £'000
Income statement – return after taxation				
Revenue return	(202)	202	(289)	289
Capital return	134,276	(134,276)	115,300	(115,300)
Total return after taxation	134,074	(134,074)	115,011	(115,011)
Net assets	134,074	(134,074)	115,011	(115,011)

(b) **Liquidity risk**

This is the risk that the Company will encounter difficulty in meeting its obligations associated with financial liabilities that are settled by delivering cash or another financial asset.

Management of the risk

Liquidity risk is not significant as the Company's assets comprise mainly readily realisable securities, which can be sold to meet funding requirements if necessary. Short term flexibility is achieved through the use of overdraft facilities.

The Board's policy is for the Company to remain fully invested in normal market conditions and that short term borrowings be used to manage short term liabilities and working capital requirements and to gear the Company as appropriate.

Liquidity risk exposure

Contractual maturities of the financial liabilities, based on the earliest date on which payment can be required are as follows:

	2011 Three months or less £'000	2011 More than three months but not more than one year £'000	2011 More than one year £'000	2011 Total £'000	2010 Three months or less £'000	2010 More than three months but not more than one year £'000	2010 More than one year £'000	2010 Total £'000
Creditors: amounts falling due within one year								
Securities purchased awaiting settlement	6,990	–	–	6,990	–	–	–	–
Repurchase of the Company's shares awaiting settlement	–	–	–	–	949	–	–	949
Bank loan	–	15,000	–	15,000	–	–	–	–
Other creditors and accruals	4,869	–	–	4,869	4,882	–	–	4,882
Creditors: amounts falling due after more than one year								
Debenture stock – principal	–	–	178,850	178,850	–	–	178,850	178,850
Debenture stock – interest	5,441	5,441	201,598	212,480	5,441	5,441	212,480	223,362
	17,300	20,441	380,448	418,189	11,272	5,441	391,330	408,043

The outflow of cash in connection with the debenture stock could occur earlier if the Company were to repurchase debentures for cancellation or if the Company goes into default and the security is enforced.

Notes to the Accounts – continued

23. Financial instruments' exposure to risk and risk management policies – continued

(c) Credit risk

Credit risk is the risk that the failure of the counterparty to a transaction to discharge its obligations under that transaction could result in loss to the Company.

Management of credit risk

Portfolio dealing

The Company invests in markets that operate DVP (Delivery Versus Payment) settlement. The process of DVP mitigates the risk of losing the principal of a trade during the settlement process. The Manager continuously monitors dealing activity to ensure best execution, a process that involves measuring various indicators including the quality of trade settlement and incidence of failed trades. Counterparty lists are maintained and adjusted accordingly.

Cash

Counterparties are subject to daily credit analysis by the Manager and trades can only be placed with counterparties that have a minimum credit rating of A1/P1 from Standard & Poor's and Moody's respectively.

Exposure to JPMorgan Chase

The Company's assets are ring-fenced in client designated accounts. Therefore these assets are designed to be protected from creditors in the event that JPMorgan Chase were to cease trading. However, no absolute guarantee can be given to investors on the protection of all of the assets of the Company.

Credit risk exposure

The following amounts shown in the Balance Sheet, represent the maximum exposure to credit risk at the current and comparative year end.

	2011		2010	
	Balance sheet £'000	Maximum exposure £'000	Balance sheet £'000	Maximum exposure £'000
Fixed assets – investments held at fair value through profit or loss	1,347,562	–	1,158,236	2,248
Current assets				
Debtors – securities sold awaiting settlement, dividends and interest receivable and other debtors	4,030	4,030	19,647	19,647
Cash and short term deposits	89,530	89,530	40,225	40,225
	1,441,122	93,560	1,218,108	62,120

The maximum credit risk exposure of fixed asset investments at 31st January 2010 comprised a holding in an unrated corporate bond.

No debtors are past their due date and none have been provided for.

Cash and short term deposits comprises balances held at banks that have a minimum credit rating of A1/P1 (2010: A1/P1) from Standard & Poor's and Moody's respectively.

(d) Fair values of financial assets and financial liabilities

All financial assets and liabilities are either carried in the balance sheet at fair value or the balance sheet amount is a reasonable approximation of fair value except for the debenture stock which the Company has in issue. The fair value of this debenture stock has been calculated using discounted cash flow techniques, using the yield from a similar dated gilt plus a margin based on the 5 year average for the AA Barclays Sterling Corporate Bond spread.

	Carrying value		Fair value	
	2011 £'m	2010 £'m	2011 £'m	2010 £'m
£175 million 6.125% debenture stock 25th February 2030	173.1	173.1	188.1	184.5
£3.85 million 4.25% perpetual debenture stock	3.9	3.9	3.2	2.7
	177.0	177.0	191.3	187.2

24. Capital management policies and procedures

The Company's capital comprises the following:

	2011 £'000	2010 £'000
Debt		
£175 million 6.125% debenture stock 25th February 2030	173,147	173,051
£3.85 million 4.25% perpetual debenture stock	3,850	3,850
Bank loan	15,000	–
	191,997	176,901
Equity		
Called up share capital	24,759	25,487
Reserves	1,212,507	1,009,889
	1,237,266	1,035,376
Total capital	1,429,263	1,212,277

The Company's capital management objectives are to ensure that it will continue as a going concern and to maximise the income and capital return to its equity shareholders through an appropriate level of gearing.

The Board's policy is to limit gearing within the range 90% to 120%. Gearing for this purpose is defined as investments expressed as a percentage of a total net assets.

	2011 £'000	2010 £'000
Investments at fair value	1,347,562	1,158,236
Net assets	1,237,266	1,035,376
Gearing	108.9%	111.9%

The Board, with the assistance of the Manager, monitors and reviews the broad structure of the Company's capital on an ongoing basis. This review includes:

- the planned level of gearing, which takes into account the Manager's views on the market;
- the need to buy back equity shares, either for cancellation or to hold in Treasury, which takes into account the share price discount or premium;
- the need for issues of new shares, including issues from Treasury; and
- the extent to which revenue in excess of that which is required to be distributed should be retained.

Notice of Meeting

Notice is hereby given that the one hundred and twenty fifth Annual General Meeting of The Mercantile Investment Trust plc will be held at Trinity House, Tower Hill, London EC3N 4DH on 18th May 2011 at 12 noon for the following purposes:

1. To receive the Directors' Report, the Annual Accounts and the Auditors' Report for the year ended 31st January 2011.
2. To approve the Directors' Remuneration Report for the year ended 31st January 2011.
3. To re-elect Hamish Leslie Melville as a Director of the Company.
4. To re-elect Sir Richard Beckett as a Director of the Company.
5. To re-elect The Right Hon. The Earl of Halifax as a Director of the Company.
6. To re-elect Sandy Nairn as a Director of the Company.
7. To re-elect Charles Peel as a Director of the Company.
8. To re-elect Ian Russell as a Director of the Company.
9. To re-appoint PricewaterhouseCoopers LLP as auditors to the Company and to authorise the Directors to determine their remuneration.

Special Business:
To consider the following resolution:

Authority to allot new shares – Ordinary Resolution

10. THAT the Directors of the Company be and they are hereby generally and unconditionally authorised, (in substitution of any authorities previously granted to the Directors), pursuant to and in accordance with Section 551 of the Companies Act 2006 (the 'Act') to exercise all the powers of the Company to allot shares in the Company and to grant rights to subscribe for, or to convert any security into, shares in the Company ('rights') up to an aggregate nominal amount of £1,237,946, representing approximately 5% of the Company's issued share capital as at the date of the passing of this resolution, provided that this authority shall expire at the conclusion of the Annual General Meeting of the Company held in 2012 unless renewed at a general meeting prior to such time, save that the Company may before such expiry make offers or agreements which would or might require shares to be allotted or Rights to be granted after such expiry and so that the Directors of the Company may allot shares and grant Rights in pursuance of such offers or agreements as if the authority conferred hereby had not expired.

Authority to disapply pre-emption rights on allotment of relevant securities – Special Resolution

11. THAT subject to the passing of Resolution 10 set out above, the Directors of the Company be and they are hereby empowered pursuant to Sections 570 and 573 of the Act to allot equity securities (within the meaning of Section 560 of the Act) for cash pursuant to the authority conferred by Resolution 10 as if Section 561(1) of the Act did not apply to any such allotment, provided that this power shall be limited to the allotment of equity securities for cash up to an aggregate nominal amount of £1,237,946 representing approximately 5% of the issued share capital as at the date of the passing of this resolution at a price of not less than the net asset value per share and shall expire upon the expiry of the general authority conferred by Resolution 10 above, save that the Company may before such expiry make offers or agreements which would or might require equity securities to be allotted after such expiry and so that the Directors of the Company may allot equity securities in pursuant of such offers or agreements as if the power conferred hereby had not expired.

Authority to repurchase the Company's shares – Special Resolution

12. THAT the Company be generally and subject as hereinafter appears unconditionally authorised in accordance with Section 701 of the Act to make market purchases (within the meaning of Section 693 of the Act) of its issued shares on such terms and in such manner as the Directors may from time to time determine.

    PROVIDED ALWAYS THAT

    (i) the maximum number of ordinary shares hereby authorised to be purchased shall be 14,845,454 or if less, that number of ordinary shares which is equal to 14.99% of the

Company's issued share capital as at the date of the passing of this Resolution;

(ii) the minimum price which may be paid for an ordinary share shall be 25p;

(iii) the maximum price which may be paid for an ordinary share or unit shall be an amount equal to the highest of: (a) 105% of the average of the middle market quotations for an ordinary share taken from and calculated by reference to the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the ordinary share is contracted to be purchased; or (b) the price of the last independent trade; or (c) the highest current independent bid;

(iv) any purchase of ordinary shares will be made in the market for cash at prices below the prevailing net asset value per ordinary share (as determined by the Directors);

(v) the authority hereby conferred shall expire on 17th November 2012 unless the authority is renewed at the Company's Annual General Meeting in 2012 or at any other general meeting prior to such time; and

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

By order of the Board
JPMorgan Asset Management (UK) Limited,
Secretary
31st March 2011

Notes

These notes should be read in conjunction with the notes on the reverse of the proxy form.

1. A member entitled to attend and vote at the Meeting may appoint another person(s) (who need not be a member of the Company) to exercise all or any of his rights to attend, speak and vote at the Meeting. A member can appoint more than one proxy in relation to the Meeting, provided that each proxy is appointed to exercise the rights attaching to different shares held by him.
2. A proxy does not need to be a member of the Company but must attend the Meeting to represent you. Your proxy could be the Chairman, another director of the Company or another person who has agreed to attend to represent you. Details of how to appoint the Chairman or another person(s) as your proxy or proxies using the proxy form are set out in the notes to the proxy form. If a voting box on the proxy form is left blank, the proxy or proxies will exercise his/their discretion both as to how to vote and whether he/they abstain(s) from voting. Your proxy must attend the Meeting for your vote to count. Appointing a proxy or proxies does not preclude you from attending the Meeting and voting in person. If you attend the Meeting in person, your proxy appointment will automatically be terminated.
3. Any instrument appointing a proxy, to be valid, must be lodged in accordance with the instructions given on the proxy form.
4. You may change your proxy instructions by returning a new proxy appointment. The deadline for receipt of proxy appointments also applies in relation to amended instructions. Any attempt to terminate or amend a proxy appointment received after the relevant deadline will be disregarded. Where two or more valid separate appointments of proxy are received in respect of the same share in respect of the same Meeting, the one which is last received (regardless of its date or the date of its signature) shall be treated as replacing and revoking the other or others as regards that share; if the Company is unable to determine which was last received, none of them shall be treated as valid in respect of that share.
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 as at 6.00 p.m. two business days prior to the Meeting (the 'specified time'). If the Meeting is adjourned to a time not more than 48 hours after the specified time applicable to the original Meeting, that time will also apply for the purpose of determining the entitlement of members to attend and vote (and for the purpose of determining the number of votes they may cast) at the adjourned Meeting. If however the Meeting is adjourned for a longer period then, to be so entitled, members must be entered on the Company's register of members as at 6.00 p.m. two business days prior to the adjourned Meeting or, if the Company gives notice of the adjourned Meeting, at the time specified in that notice. Changes to entries on the register after this time shall be disregarded in determining the rights of persons to attend or vote at the meeting or adjourned meeting.
6. Entry to the Meeting will be restricted to shareholders and their proxy or proxies, with guests admitted only by prior arrangement.

Notice of Meeting – continued

7. A corporation, which is a shareholder, may appoint an individual(s) to act as its representative(s) and to vote in person at the Meeting (see instructions given on the proxy form). In accordance with the provisions of the Companies Act 2006, each such representative(s) may exercise (on behalf of the corporation) the same powers as the corporation could exercise if it were an individual member of the Company, provided that they do not do so in relation to the same shares. It is therefore no longer necessary to nominate a designated corporate representative. Representatives should bring to the meeting evidence of their appointment, including any authority under which it is signed.
8. Members that satisfy the thresholds in Section 527 of the Companies Act 2006 can require the Company to publish a statement on its website setting out any matter relating to: (a) the audit of the Company's accounts (including the Auditor's report and the conduct of the audit) that are to be laid before the AGM; or (b) any circumstances connected with an Auditor of the Company ceasing to hold office since the previous AGM; which the members propose to raise at the meeting. The Company cannot require the members requesting the publication to pay its expenses. Any statement placed on the website must also be sent to the Company's Auditors no later than the time it makes its statement available on the website. The business which may be dealt with at the AGM includes any statement that the Company has been required to publish on its website pursuant to this right.
9. Pursuant to Section 319A of the Companies Act 2006, the Company must cause to be answered at the AGM any question relating to the business being dealt with at the AGM which is put by a member attending the meeting except in certain circumstances, including if it is undesirable in the interests of the Company or the good order of the meeting or if it would involve the disclosure of confidential information.
10. Under sections 338 and 338A of the 2006 Act, members meeting the threshold requirements in those sections have the right to require the Company: (i) to give, to members of the Company entitled to receive notice of the Meeting, notice of a resolution which those members intend to move (and which may properly be moved) at the Meeting; and/or (ii) to include in the business to be dealt with at the Meeting any matter (other than a proposed resolution) which may properly be included in the business at the Meeting. A resolution may properly be moved, or a matter properly included in the business unless: (a) (in the case of a resolution only) it would, if passed, be ineffective (whether by reason of any inconsistency with any enactment or the Company's constitution or otherwise); (b) it is defamatory of any person; or (c) it is frivolous or vexatious. A request made pursuant to this right may be in hard copy or electronic form, must identify the resolution of which notice is to be given or the matter to be included in the business, must be accompanied by a statement setting out the grounds for the request, must be authenticated by the person(s) making it and must be received by the Company not later than the date that is six clear weeks before the Meeting, and (in the case of a matter to be included in the business only) must be accompanied by a statement setting out the grounds for the request.
11. A copy of this notice has been sent for information only to persons who have been nominated by a member to enjoy information rights under Section 146 of the Companies Act 2006 (a 'Nominated Person'). The rights to appoint a proxy can not be exercised by a Nominated Person: they can only be exercised by the member. However, a Nominated Person may have a right under an agreement between him and the member by whom he was nominated to be appointed as a proxy for the Meeting or to have someone else so appointed. If a Nominated Person does not have such a right or does not wish to exercise it, he may have a right under such an agreement to give instructions to the member as to the exercise of voting rights.
12. In accordance with Section 311A of the Companies Act 2006, the contents of this notice of meeting, details of the total number of shares in respect of which members are entitled to exercise voting rights at the AGM, the total voting rights members are entitled to exercise at the AGM and, if applicable, any members' statements, members' resolutions or members' matters of business received by the Company after the date of this notice will be available on the Company's website www.mercantileit.co.uk.
13. The register of interests of the Directors and connected persons in the share capital of the Company and the Directors' letters of appointment are available for inspection at the Company's registered office during usual business hours on any weekday (Saturdays, Sundays and public holidays excepted). It will also be available for inspection at the Annual General Meeting. No Director has any contract of service with the Company.
14. You may not use any electronic address provided in this Notice of meeting to communicate with the Company for any purposes other than those expressly stated.
15. As an alternative to completing a hard copy Form of Proxy/ Voting Instruction Form, you can appoint a proxy or proxies electronically by visiting www.sharevote.co.uk. You will need your Voting ID, Task ID and Shareholder Reference Number (this is the series of numbers printed under your name on the Form of Proxy/Voting Instruction Form). Alternatively, if you have already registered with Equiniti Limited's online portfolio service, Shareview, you can submit your Form of Proxy at www.shareview.co.uk. Full instructions are given on both websites.
16. As at 31st March 2011 (being the latest business day prior to the publication of this Notice), the Company's issued share capital consists of 99,035,719 Ordinary shares, carrying one vote each. Therefore the total voting rights in the Company are 99,035,719.

Electronic appointment – CREST members

CREST members who wish to appoint a proxy or proxies by utilising the CREST electronic proxy appointment service may do so for the Meeting and any adjournment(s) thereof by using the procedures described in the CREST Manual. See further instructions on the proxy form.

Glossary of Terms and Definitions

Return on Net Assets
Total return on net asset value ('NAV') per share, on a bid value to bid value basis, assuming that all dividends paid out by the Company were reinvested in the shares of the Company at the NAV per share at the time the shares were quoted ex-dividend.

In accordance with industry practice, dividends payable which have been declared but which are unpaid at the balance sheet date are deducted from the NAV when calculating the total return on net assets.

Return to Shareholders
Total return to the investor, on a mid-market price to mid-market price basis, assuming that all dividends received were reinvested, without transaction costs, in the shares of the Company at the time the shares were quoted ex-dividend.

Benchmark Return
Total return on the benchmark, on a mid-market value to mid-market value basis, assuming that all dividends received were reinvested, without transaction costs, in the shares of the underlying companies at time the shares were quoted ex-dividend.

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

Total Expense Ratio (TER)
Management fees and all other operating expenses excluding interest, expressed as a percentage of the average of the month end net assets during the year. The method of calculating the TER has changed this year and the prior year figure restated. In previous years the TER represented management fees and all other operating expenses excluding interest, calculated as above expressed as a percentage of the average of the opening and closing net assets. The new methodology more accurately reflects the way the management fee is calculated, which is based on the Company's month end market capitalisation.

Actual Gearing Factor
Investments expressed as a percentage of shareholders' funds. This shows the effect of gearing on the net asset value if the market value of the portfolio were to increase by 100%.

Share Price Discount/Premium to Net Asset Value
If the share price of an investment trust is lower than the net asset value ('NAV') per share, the shares are said to be trading at a discount. The discount is shown as a percentage of the NAV. The opposite of a discount is a premium. It is more common for an investment trust's shares to trade at a discount than at a premium.

Performance Attribution
Analysis of how the Company achieved its recorded performance relative to its benchmark.

Performance Attribution Definitions:
Allocation Effect
Measures the impact of allocating assets differently to those in the benchmark, via the portfolio's weighting in different countries, sectors or asset types.

Selection Effect
Measures the effect of investing in securities to a greater or lesser extent than their weighting in the benchmark, or of investing in securities which are not included in the benchmark.

Gearing/Cash Effect
Measures the impact on returns of borrowings or cash balances on the Company's relative performance.

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

Share Buybacks
Measures the effect on relative performance of repurchasing and cancelling the Company's own shares at a price which is less than the net asset value per share.

Information about the Company

Financial Calendar

Financial year end	31st January
Final results announced	April
Half year end	31st July
Half year results announced	September
Interim Management Statements announced	May/November
Dividends on ordinary shares paid to shareholders	*1st August, 1st November, 1st February, 1st May
Interest on 4.25% perpetual debenture stock paid	1st June, 1st December
Annual General Meeting	April/May

*or nearest following business day.

History

The Mercantile Investment & General Trust Company Limited was formed in December 1884 with issued capital of £500,000. The Company merged with three other investment trusts in 1960 under a scheme of arrangement and changed its name to The Mercantile Investment Trust Limited. In 1982 the Company became The Fleming Mercantile Investment Trust plc. JPMorgan has been the Company's manager and secretary since its appointment in 1976. In April 2008, the Company adopted its present name, The Mercantile Investment Trust plc.

A publication entitled 'The Mercantile Investment Trust plc 125 years' is available from the Secretary.

Directors

Hamish Leslie Melville (Chairman)
Sir Richard Beckett
The Right Hon. The Earl of Halifax
Sandy Nairn
Charles Peel
Ian Russell

Company Numbers

Company Registration number: 20537
London Stock Exchange number: 0579403
ISIN: GB0005794036
Bloomberg ticker: MRC LN

Market Information

The Company's shares are listed on the London Stock Exchange. The market price is shown daily in the Financial Times, The Guardian, The Times, The Daily Telegraph, The Independent, The Scotsman, and on the internet site at www.mercantileit.co.uk, where the share price is updated every fifteen minutes during trading hours.

Website

www.mercantileit.co.uk

Share Transactions

The Company's shares may be dealt in directly through a stockbroker or professional adviser acting on an investor's behalf. They may also be purchased and held through the J.P. Morgan Investment Account, J.P. Morgan ISA and J.P. Morgan SIPP. These products are all available on the online wealth manager service, J.P. Morgan WealthManager+ available at www.jpmorganwealthmanagerplus.co.uk.

aic The Association of Investment Companies A member of the AIC

Manager and Secretary

JPMorgan Asset Management (UK) Limited

Company's Registered Office

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

Please contact Juliet Dearlove for company secretarial and administrative matters.

Registrars

Equiniti Limited
Reference 1101
Aspect House
Spencer Way
Lancing
West Sussex BN99 6DA
Telephone number: 0871 384 2329

Calls to this number cost 8p per minute from a BT landline. Other providers' costs may vary. Lines open 8.30 am to 5.30 pm, Monday to Friday. The overseas helpline number is +44 (0)121 415 7047.

Notifications of changes of address and enquiries regarding share certificates or dividend cheques should be made in writing to the Registrar quoting reference 1101. Registered shareholders can obtain further details on their holdings on the internet by visiting www.shareview.co.uk.

Independent Auditors

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Hay's Galleria
1 Hay's Lane
London SE1 2RD

Brokers

Cenkos Securities plc
6, 7, 8 Tokenhouse Yard
London EC2R 7AS

Oriel Securities Limited
125 Wood Street
London EC2V 7AN

Savings Product Administrators

For queries on the J.P. Morgan Investment Account, J.P. Morgan ISA and J.P. Morgan SIPP, see contact details on the back cover of this report.

J.P. Morgan Helpline
Freephone 0800 20 40 20 or +44 (0)20 7742 9995

Your telephone call may be recorded for your security

www.mercantileit.co.uk