The Mercantile Investment Trust plc

(formerly JPMorgan Fleming Mercantile Investment Trust plc)

Annual Report & Accounts for the year ended 31st January 2009

JPMorgan
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

The Company has an authorised share capital of 163,875,000 ordinary shares of 25p each, of which 102,321,968 were in issue at the year end.

In addition, the Company had at the year end £3,850,000 perpetual debenture stock and a £175 million debenture.

Management Company

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

Financial Highlights

Total Returns (capital plus income)

-39.3%
Return on net assets
(2008: -16.2%)

-39.2%
Return to shareholders[1]
(2008: -16.7%)

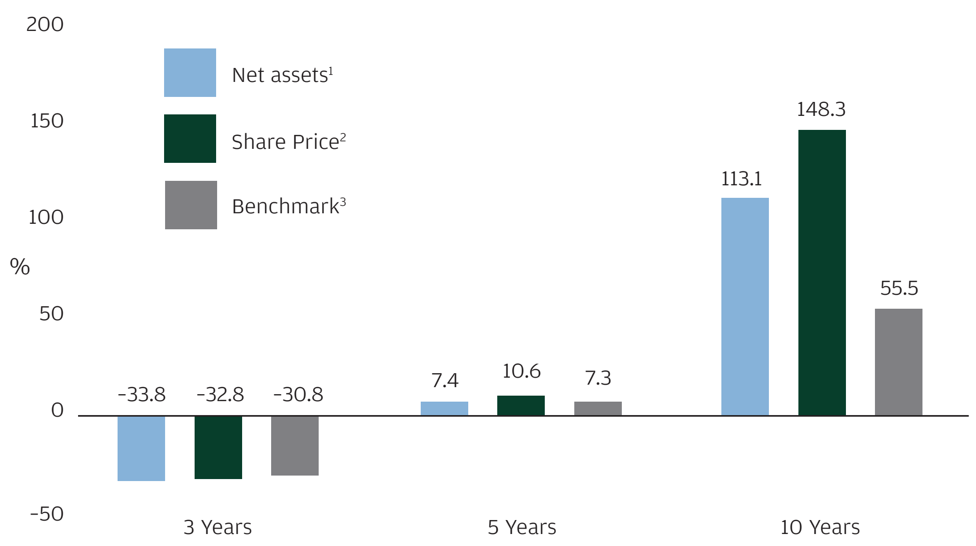
-36.2%
Benchmark return[2]
(2008: -12.7%)

36.0p
Ordinary - dividend
(2008: 34.0p ordinary
and a special of 4.0p)

[1]Source: Standard & Poor's - www.funds.morningstar.com

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

Long Term Performance
for periods ended 31st January 2009



A glossary of terms and definitions is provided on page 52.

[1]Source: Fundamental Data Ltd, a Morningstar company - www.funddata.com

[2]Source: Standard & Poor's - www.funds.morningstar.com

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

Chairman's Statement

Over the year to 31st January 2009, the 124th year since the Company was founded, the Company's total return on net assets (i.e. with net income reinvested) was -39.3%, which compares with a return of -36.2% on the same basis from the Company's benchmark index, the FTSE All-Share (excluding FTSE 100 constituents and investment trusts). Conditions in the financial markets globally and particularly in the UK economy were the worst for decades and the Company's performance was very adversely affected despite the fact that the Company was in a net cash position for substantial periods throughout the year.

Earnings and Dividends

Earnings per share increased by 4.9% for the year, from 39.79p to 41.73p partly due to the receipt of a number of special dividends, a higher level of deposit interest income and the receipt of further VAT recoveries and interest thereon.

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, an increase of 5.9% on last year's baseline dividend of 34.0p. The Board recognises that it is essential to make an appropriate distribution, which both meets shareholders' legitimate expectations, and is prudent in light of what may be continued difficult times ahead. With this in mind, the Board feels it appropriate not to declare a special dividend in order to distribute the VAT and related interest recovered during the year, the additional amount, of 3p per share, being included in the baseline dividend.

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 2010. 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 very strong residual revenue reserve of 40.0p per share.

Share Price Discount

The share price fell by 41.9% during the year and, including dividends paid, the total return to shareholders was -39.2%. The discount to net asset value was 9.2% compared to 10.5% (with debt at fair value) a year ago. The average daily discount, with debt at fair value, during the year was 10.5%.

Share Repurchases

During the year under review a total of 1.98m shares were repurchased for cancellation, amounting to 1.9% of issued share capital at the beginning of the year, at a total cost of £17.59 million. Share repurchases during the year under review have added approximately 2.4 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. To date the Board believes 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 a gearing factor of 102.8% geared. During the year the gearing varied between 89% and 103%. It is the Board's intention to continue to operate within the range of 90% to 120% invested, under normal market conditions, although at the present time, the Board is maintaining gearing at the lower end of the range.

The Board elected not to renew the £70 million 364 day revolving credit facility in place with Lloyds TSB, which was never drawn down and expired on 4th March 2008.

VAT case

Following the successful outcome, in November 2007, of the action brought by the AIC and JPMorgan Claverhouse Investment Trust plc challenging the imposition of VAT on management fees for investment trust companies, in December 2008 the Board reached agreement with the Company's Manager, JPMorgan Asset Management (UK) Limited ('JPMAM'), on the recovery of past VAT. The total recovery by the Company from HM Revenue & Customs and JPMAM, including interest, was £10,132,000 and this was all reflected in the Company's net asset value by 23rd December 2008. As reported in last year's Annual Report, the Board retained Noble Grossart to act on behalf of the Company in this matter.

Board

There have been no Board changes during the year under review. The Board takes into account the ongoing requirements of the Combined Code, including the need to refresh the Board and its Committees. Directors conduct a self-assessment of their performance each year. A report is made to the Nomination Committee which meets annually to evaluate the performance of the Board, its Committees and the individual Directors. The Chairman reports the findings of the Nomination Committee to the Board.

No re-election of Directors is required this year other than myself. Having been a Director for more than nine years, in accordance with the Board's policy, I offer myself for re-election on an annual basis only.

Investment Managers

The Company's investment management team comprises Martin Hudson, who was appointed in 1993, and Jane Lennard, who was appointed in 2006. Emel Akan left the team, and will be replaced by a graduate recruit later in 2009.

The Board continues to monitor the performance of the Manager on a regular basis. The notice period with respect to the Management Contract has been shortened to six months from one year, in line with market practice.

Annual General Meeting

The Company's one hundred and twenty third Annual General Meeting will be held at Trinity House, Tower Hill, London EC3N 4DH on Wednesday 29th April 2009 at 12.00 noon. 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.

Chairman's Statement – continued

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 in writing any detailed questions that you wish to raise at the AGM to the Company Secretary at Finsbury Dials, 20 Finsbury Street, London EC2Y 9AQ or via the website at www.mercantileit.co.uk (then click on "AGM calendar"). Shareholders who are unable to attend the AGM in person are encouraged to use their proxy votes, and attention is drawn to the changes to the proxy voting regime following the introduction of the Companies Act 2006.

8th December 2009 will mark the 125th anniversary of the founding of the Company.

Outlook

The UK stock market has been severely depressed by the extremely difficult trading conditions affecting financial markets globally. The uncertainty to business that this has caused has brought the United Kingdom into the recession which it is currently experiencing. The Board continues to work with the Investment Managers to seek improved performance, and believes that, over time, this can be achieved. However, despite the fact that, on a historic basis, valuations in the sectors in which we are engaged are becoming more attractive, it is unlikely that markets will progress until clarity and stability return to the global financial system.

Hamish Leslie Melville
Chairman 24th March 2009

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 to 31st January 2009

	%	1 Year %
Contributions to Total Returns		
Benchmark total return		-36.2
Allocation effect	-1.9	
Selection effect	-0.8	
Gearing/cash effect	0.5	
Portfolio total return		-38.4
Fees/Expenses	-0.6	
Share buybacks	0.2	
VAT recovery	0.2	
Residual	-0.7	
Net asset value total return		-39.3
Effect of decrease/ (increase) in discount	0.1	
Share price total return		-39.2

Source: Xamin/JPMAM/AIC/Fundamental Data Ltd, a Morningstar company – www.funddata.com

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 52.

Market Background

Last year was one of the worst ever for equity markets and indeed for all risk assets. There was an ominous fragility about the world in 2008 and in September the financial system came close to collapse. Investment banks and High Street banks failed as funds were withdrawn, cash was hoarded and they were unable to fund their operations. There was a co-ordinated global response from Central banks to the crisis and the size of the US Government's rescue packages has now risen to $2 trillion.

In the UK the run of more than 15 years of economic growth, which had been fuelled by ever increasing levels of debt, came to dramatic end; most of the UK banking system had to be rescued by the Government; the housebuilding industry practically came to a halt; UK manufacturing suffered its sharpest quarterly contraction since at least 1974 with manufacturing output falling by 5.1% and company failures rose by more than 250% in the fourth quarter; one in every 150 active companies went into liquidation in 2008; unemployment rose sharply, consumer confidence evaporated and both companies and individuals cut back their spending substantially. Despite the base rate being cut to 0.5%, its lowest level ever, the actual cost of debt remained high and its availability scarce.

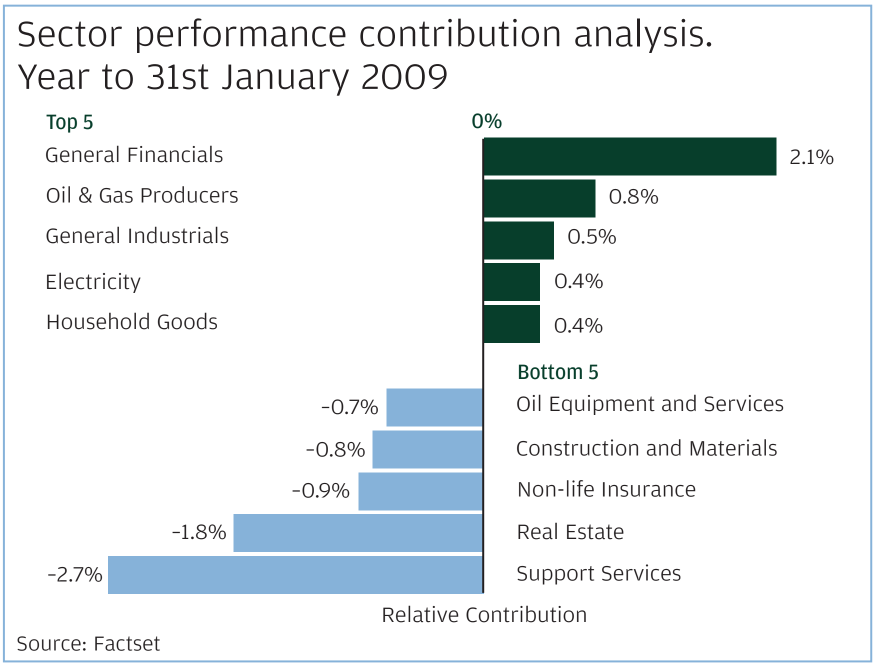
That said, the stockmarket did not seize up; it was open for business and, although volatility was extraordinarily high, a logical thread remained with those companies which had very high borrowings, cyclical earnings coupled with high operational gearing, or were exposed to falling commodity prices being hit the hardest. The events of the last 18 months have followed a familiar pattern; falling asset prices prompted the banks to withdraw capital which in turn slowed economic activity and caused a further decline in asset values. By October 2008 this downward spiral had taken hold and despite seemingly sophisticated risk controls it seems that basic human behaviour does not change that much.

Performance

It was a tough year for small and mid sized UK equities and disappointingly we have not been able to outperform, with the Company's net asset value total return of -39.3% for the year ended 31st January 2009 being 3.1% behind the Company's benchmark index, the FTSE All-Share excluding FTSE 100 constituents and investment companies, which returned -36.2%. However the ten year record remains ahead of the benchmark with a net asset value return of 113.1%. This remains substantially ahead of the broader All Share index performance and we believe that, structurally, small and mid sized companies will again deliver superior outperformance over the longer term, given their broader exposure to different sectors and to new growth companies.

The total return to shareholders for the year was -39.2% as the share price discount to net asset value narrowed from 10.5% to 9.2%. The relative performance is analysed in the table on the left. The bar chart on page 6 shows the relative contributions to performance for the year for the five best and the five worst sectors within the portfolio. The dark green bars to the right show the positive contributions to performance relative to the benchmark index and reflect a contribution of both sector weightings and stock selection. The light blue bars to the left show the negative relative contributors.

Investment Managers' Report – continued



This shows that the biggest contributor to underperformance was the Company's underweight stance in the Support Services sector. Support Services is the biggest sector in our benchmark index, representing about 15% of the index on average last year but we held only 10% of the portfolio in the sector, believing that these companies will not be immune from the economic downturn. The stockmarket, however, continues to believe that they will be more resilient because of their earnings visibility, long order books, framework agreements and public sector workloads. The sector outperformed during the year but we continue to remain underweight in Support Services believing that the profits to be reported by many of the companies will disappoint. Real Estate was the Company's next worst sector as the difficulty in financing new projects weighed particularly heavily on developers such as Real Estate Opportunities. The underperformance from Non-Life Insurers reflected an underweight position in Catlin and an early disposal of Amlin as it moved towards FTSE 100 promotion. This was offset by a positive performance from General Financials where IG Group contributed particularly strongly. The Oil and Gas Producers sector contributed strongly, particularly benefiting from the cash bid for Imperial Energy, but was offset by underperformance in the Oil Equipment and Services sector where we did not hold Expro, which also received a cash bid.

With market conditions so difficult throughout the year, the portfolio held a net cash position. This helped relative performance and we also bought a small position in a put option on the FTSE 100 index enabling us to take a profit of £1 million when the stockmarket fell substantially in the second half of the year.

Activity

Gearing was managed actively throughout the year. Having started the year with more than 5% net cash on deposit in order to preserve value in a falling market. This was increased to 10% cash by March as the outlook worsened. From September onwards, as the stockmarket fell substantially, cash was reinvested in the stockmarket and we ended the year with gearing of 102.8%. The investment managers have the flexibility to operate within a gearing range of 90% – 120% invested and a more specific tactical range is agreed regularly with the Board.

On 1st October 2008 Standard and Poor's reviewed the Company's credit rating and it remained unchanged at AA with a stable outlook reflecting the well-diversified portfolio and the expectation that Mercantile will continue to follow a conservative strategy.

The portfolio retains its style of broad diversification across all sectors, holding about 130 stocks of which 70 are mid sized and 60 are smaller companies. By value, around 80% of the portfolio is invested in mid sized stocks. The table below shows that the holding of companies larger than £1.5 billion market capitalisation is larger than the benchmark index weighting. This reflects an overweight holding in those successful larger mid sized companies which are progressing towards the FTSE 100 index. The portfolio is also overweight in the very smallest companies. These are currently offering outstanding value and good growth opportunities.

Portfolio Size Distribution

Market capitalisation	Benchmark index weighting %	Fund weighting %	Relative weighting %
More than £1.5bn	1.6	4.1	+2.5
£1.0bn to £1.5bn	17.8	14.1	–3.7
£500m to £1.0bn	41.1	40.3	–0.8
£300m to £500m	15.8	11.3	–4.5
£100m to £300m	18.7	15.5	–3.2
£50m to £100m	3.6	6.3	+2.7
Less than £50m	1.4	8.4	+7.0
Total	**100.0**	**100.0**	**–**

As at 31st January 2009

In the second half of the year we positioned the portfolio, within our diversified approach, to take advantage of falling interest rates by buying housebuilders, general financials, leisure and media stocks. We felt that the reduction in demand for commodities as global economies slowed would result in a fall in inflation which would, in turn, allow Central banks to reduce interest rates; the oil price has fallen from a peak of $147 a barrel to about $44 now and base rates in the UK have been reduced to 1.0%, their lowest ever. Although in practice the cost of debt remains relatively high and securing new borrowing facilities is difficult, those who do not have to renew their borrowings and who are not breaking their banking covenants will find the cost of borrowing reducing.

Our ten largest holdings reflect this positioning. Of the ten largest holdings as at 31st January 2009 (which are shown on page 12) only four were in the top ten last year: IG Group, United Business Media, Ladbrokes and Investec. The new additions are two housebuilders,

Investment Managers' Report – continued

Bellway and Persimmon; a leisure company, William Hill; a media company, ITV, an oil and gas producer, Venture Production and a support services supplier, Babcock International.

During the year we met or visited about 250 companies and this remains a key component in our process of evaluating companies. We believe that properly targeted company meetings can help us analyse smaller companies that are often overlooked by the mainstream, evaluate management 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.

Takeover activity was relatively low last year and in the coming year we expect corporate activity to centre on recapitalisation, debt for equity swaps and rescue rights issues rather than corporate acquisitions, management buyouts, private equity takeovers and initial public offerings.

Outlook

These are dramatic times and they are unlike any which have been experienced in recent history. It is clear that there is a collective global determination to maintain a supply of credit and to ensure the capital strength of the banks to avert the risk of a prolonged slump. Confidence, however, remains low and fragile and will not be helped by deteriorating news on unemployment, economic output and corporate earnings. Although still in the maelstrom, we are now working towards recovery, which will require private sector de-gearing, asset prices falling to sensible levels, the recognition of the resulting financial sector losses and recapitalisation of the financial system. No easy task. Capital preservation is thus still important. The risk of high levels of debt in individual companies is now well understood by the stockmarket but specific debt covenant risks and working capital risks are less well understood. However, the unprecedented fiscal and monetary easing which is being applied, together with the collapse in the oil price, will mean that many people will feel a benefit in 2009 and perhaps create confidence that 2010 will be a better year. We are seeking out strong companies which do have a viable future but where the stockmarket has become too negative. Substantial falls in corporate earnings of perhaps 40% are already being discounted by the market although analysts' profit forecasts for individual companies are still too high.

We now face the substantial risk that by printing money to reduce the value of the existing debt burden the Government could reignite fears of inflation. In that case, real assets such as property, equities and index linked gilts will offer higher returns than government bonds and cash.

Because analysts' forecasts for companies are still too high, we have omitted our usual table of forward market aggregate estimates. However, for the record, they show that the Mercantile portfolio currently stands on a 12 month forward price to earnings ratio of 7.2X and dividend yield of 5.1%. On a historic valuation basis the stockmarket is clearly cheap and long term value is present. We plan to increase gearing, by investing more of the cash available to us, either if volatility drives the stockmarket lower or if the prospects for growth improve.

Martin Hudson
Jane Lennard
Investment Managers 24th March 2009

Summary of Results

	2009	2008	
Total Returns (capital plus income) for the year ended 31st January			
Return on net assets	-39.3%	-16.2%	
Return to shareholders[1]	-39.2%	-16.7%	
Benchmark[2]	-36.2%	-12.7%	
Net Asset Value and Discount at 31st January			% change
Shareholders' funds (£'000)	697,298	1,208,150	-42.3
Net asset value per share with debt at par	681.5p	1,158.3p	-41.2
Net asset value per share with debt at fair value[3]	652.4p	1,139.6p	-42.8
Discount of net asset value to share price with debt at par	13.0%	11.9%	
Discount of net asset value to share price with debt at fair value[3]	9.2%	10.5%	
Market Data			
FTSE All-Share Index[4] (capital only) (excluding FTSE 100 constituents and investment trusts)	1,229.5	2,012.4	-38.9
Share price	592.5p	1,020.0p	-41.9
Revenue for the year ended 31st January			
Net revenue available for shareholders (£'000)	43,028	44,345	-3.0
Return per share	41.73p	39.79p	+4.9
Dividend per share: Ordinary dividends	36.0p	34.0p	+5.9
Special dividend	–	4.0p	
Total dividends per share	36.0p	38.0p	
Total Expense Ratio (TER)[5]	0.56%	0.59%	
Actual Gearing Factor[6]	102.8%	94.8%	

A glossary of terms and definitions is provided on page 52.

[1]Source: Standard & Poor's - www.funds.morningstar.com

[2]Source: Russell/Mellon Caps.

[3]Market values have been used to determine the fair value of the debenture stock.

[4]Source: Datastream.

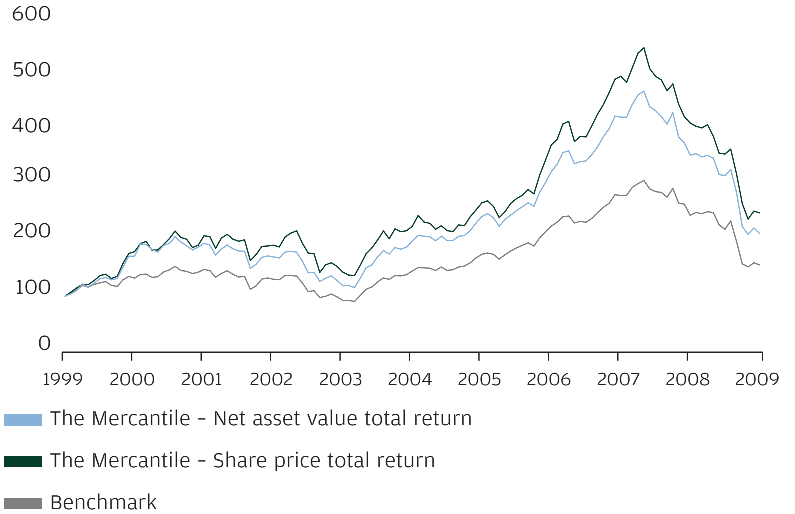
[5]Management fees and all other operating expenses, excluding interest and professional fees incurred in connection with VAT recoveries, expressed as a percentage of the average of the opening and closing net assets.

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

Performance

Ten Year Performance

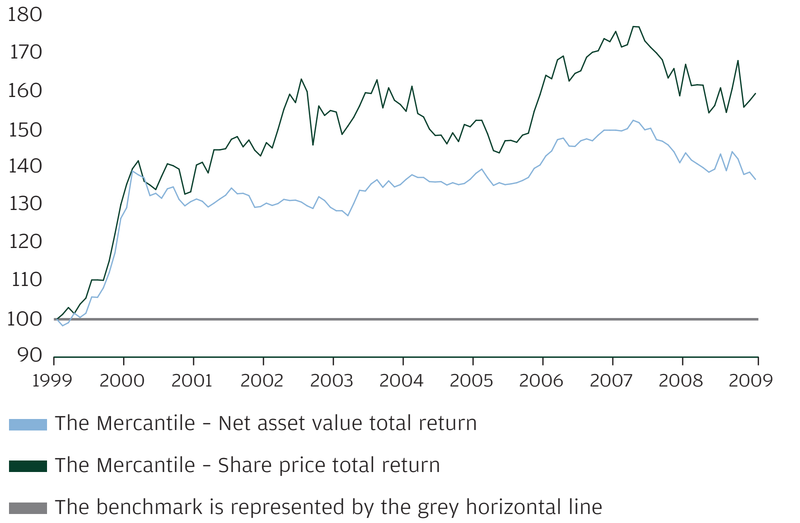
Figures have been rebased to 100 at 31st January 1999



Source: Fundamental Data Ltd, a Morningstar company – www.funddata.com
Standard & Poor's – www.funds.morningstar.com/Russell/Mellon Caps.

Performance relative to Benchmark

Figures have been rebased to 100 at 31st January 1999



Source: Fundamental Data Ltd, a Morningstar company – www.funddata.com
Standard & Poor's – www.funds.morningstar.com/Russell/Mellon Caps.

Ten Year Financial Record

As at 31st January	1999	2000	2001	2002	2003	2004	2005[1]	2006	2007	2008	2009
Total assets less current liabilities (£'m)	664.7	1,068.3	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
Net asset value per share (p)	405.4	679.5	755.8	644.7	434.6	703.5	842.6	1,090.6	1,394.4	1,158.3	681.5
Share price (p)	321.5	560.5	635.5	567.0	408.5	620.0	713.5	965.0	1,258.0	1,020.0	592.5
Year to 31st January											
Gross revenue (£'000)	26,068	26,556	34,391	39,435	34,584	34,050	34,970	39,899	45,493	51,684	51,750
Revenue available for shareholders (£'000)	16,541	19,177	24,124	28,364	24,169	24,555	24,820	29,373	35,043	44,345	43,028
Earnings per share (p)	11.5	13.4	17.6	20.9	17.8	18.1	18.3	21.8	27.5	39.8	41.7
Dividend per share (net) (p)[2]	11.0	12.3	14.8	17.5	18.0	18.8	19.8	21.8	25.0	38.0	36.0
Discount	20.7	17.5	15.9	12.1	6.0	11.9	15.3	11.5	9.8	11.9	13.0
Actual gearing	115.9	113.6	114.0	110.0	113.1	112.6	115.5	111.2	102.0	94.8	102.8
Total expense ratio[3]	0.66	0.63	0.65	0.63	0.73	0.69	0.60	0.56	0.55	0.59	0.56
Rebased to 100 at 31st January 1999											
Net asset value per share	100.0	167.6	186.4	159.0	107.2	173.5	207.8	269.0	344.0	285.7	168.1
Net asset value per share – total return[4]	100.0	171.0	194.2	169.8	118.5	198.5	241.8	321.7	418.9	351.1	213.1
Share price	100.0	174.3	197.7	176.4	127.1	192.8	221.9	300.2	391.3	317.3	184.3
Share price – total return[4]	100.0	179.1	207.5	190.6	142.6	224.6	266.2	369.5	491.8	408.4	248.3
Benchmark[4]	100.0	132.0	147.4	129.9	92.1	144.9	174.5	224.6	279.3	243.9	155.5
Earnings per share	100.0	116.5	153.0	181.7	154.8	157.4	159.1	189.6	239.1	345.6	362.6
Dividend[2]	100.0	123.0	148.0	175.0	180.0	188.0	198.0	218.0	250.0	380.0	360.0

[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 and professional fees incurred in connection with VAT recoveries, expressed as a percentage of the average of the opening and closing net assets.

[4]Source: Standard & Poor's – www.funds.morningstar.com/Fundamental Data – www.funddata.com/Russell/Mellon Caps.

Ten Largest Investments

Company	As at 31st January 2009 Valuation £'000	%[1]	As at 31st January 2008 Valuation £'000	%
IG Group Offers global financial derivatives trading. Its products include spread betting, contracts for difference and foreign exchange. The group also offers spread betting on sports, entertainment and political events	24,775	2.8	31,390	2.3
United Business Media Provides business information services. The company's market research, news distribution, publishing, and events organising services are provided to the technology, healthcare, media, automotive, and financial services industries.	17,161	2.0	21,810	1.6
Bellway[2] Designs, builds and develops residential housing throughout England, Wales and Scotland.	15,227	1.7	14,016	1.0
Persimmon[3] Designs, builds and develops residential housing throughout England, Wales and Scotland.	14,843	1.7	–	–
William Hill[2] Provides bookmaking services in the United Kingdom. The group, which operates licenced betting offices, telephone based-betting operations, and online betting, offers odds and takes bets on an assortment of sporting and other events.	14,123	1.6	15,078	1.1
Ladbrokes Has diversified interests in betting ventures. The company operates betting shops and call centres in the UK, Ireland, and Belgium.	13,136	1.5	26,255	1.9
Investec Is an international investment and private banking group. The group provides corporate and investment banking, private banking, securities trading, asset management, property trading and management and trade finance services.	13,061	1.5	19,531	1.4
Venture Production[2] Produces oil and gas. The company acquires rights to oil fields with proven reserves that have not been fully exploited, and revitalises the fields to produce the oil and gas. The company operates in the North Sea and onshore and offshore in Trinidad.	12,597	1.4	1,280	0.1
ITV[3] 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, a commercial television channel, as well as ITV2.	12,206	1.4	–	–
Babcock International[3] A supplier of support services to UK armed forces and other non-military customers.	11,901	1.4	11,466	0.8
Total	**149,030**	**17.0**		

All of the above investments are listed in UK.

[1]Based on total assets less current liabilities of £874m.

[2]Not included in the ten largest investments at 31st January 2008.

[3]Not held in the portfolio at 31st January 2008.

As at 31st January 2008, the value of the ten largest investments amounted to £230.8m representing 16.7% of total assets less current liabilities.

Portfolio Analyses

Listed Equity Market Capitalisation
at 31st January

	2009 %	2008 %
UK FTSE Mid 250 Companies	62.5	62.1
UK Smaller Companies	16.3	17.7
UK FTSE 100	1.4	0.7
UK Unquoted	1.7	1.4
Overseas Company	0.1	0.8
Net Current Assets	18.0	17.3
Total	100.0	100.0

Based on total assets less current liabilities of £874m (2008: £1,385m).

Sector Analysis
at 31st January

	Portfolio 2009 %	Benchmark 2009 %	Portfolio 2008 %	Benchmark 2008 %
Financials	22.6	17.3	25.8	18.1
Consumer Services	18.4	20.4	17.1	20.4
Industrials	18.2	31.1	19.3	29.9
Consumer Goods	9.2	8.6	10.8	8.0
Oil & Gas	9.2	6.7	3.2	6.4
Technology	1.6	6.1	1.4	6.0
Basic Materials	1.4	5.6	2.7	4.7
Utilities	0.8	0.8	2.4	2.4
Telecommunications	0.6	0.4	–	1.4
Healthcare	–	3.0	–	2.7
Net Current Assets	18.0	–	17.3	–
Total	100.0	100.0	100.0	100.0

Based on total assets less current liabilities of £874m (2008: £1,385m).

List of Investments

at 31st January 2009

Company	£'000
United Kingdom	
Financials	
IG Group	24,775
Investec	13,061
Cazenove[1]	11,738
Aberdeen Asset Management	9,643
Segro	9,275
Close Brothers	9,254
Derwent London	8,902
Provident	8,584
F&C Asset Management	6,739
Brixton	6,302
Chaucer	6,265
Catlin	5,811
TR Property Investment Trust	5,303
Great Portland Estates	5,167
Puma Brandenburg[2]	4,977
Hiscox	4,253
St Peter Port[2]	4,224
Tenon[2]	3,982
Paragon Group of Companies	3,741
Brewin Dolphin	3,735
Shore Capital	3,484
Mapeley[3]	3,228
Daejan Holdings	3,188
Rensburg Sheppards	3,116
Helical Bar	3,105
Orchid Development[2]	2,973
Songbird Estates[2]	2,948
Development Securities	2,648
Rathbone Brothers	2,479
Novae	2,377
Real Estate Opportunities	2,025
Cenkos Securities[2]	1,587
Mountview Estates	1,524
Vantis[2]	1,432
Invista Real Estate Investment Management[2]	1,324
JPMorgan Cazenove Holdings[1]	1,155
Capital Management & Investment[2]	962
Quintain Estates & Development	940
Jardine Lloyd Thompson	911
Sovereign Reversions[2]	377
Mucklow (A & J)	193
Advance Aim Value Realisation[2]	156
	197,862

Company	£'000
Consumer Services	
United Business Media	17,161
William Hill	14,123
Ladbrokes	13,136
ITV	12,206
Daily Mail & General Trust	11,798
Carphone Warehouse	9,121
Mitchells & Butlers	8,958
Stagecoach	8,897
Go-Ahead	8,593
Bloomsbury Publishing	6,792
Arriva	6,709
Pinewood Shepperton	5,267
Young & Co's Brewery[2]	4,594
Trinity Mirror	4,535
Home Retail	4,534
The Hotel Corporation[2]	4,492
Greene King	3,366
National Express	2,985
Cineworld	2,944
Millennium & Copthorne Hotels	2,871
Arena Leisure	2,747
Chrysalis	1,474
Peel Hotels[2]	1,240
Skywest Airlines[2]	600
Avesco[2]	597
Prezzo[2]	432
JD Sports Fashion	367
Expomedia[2]	9
	160,549
Industrials	
Babcock International	11,901
Tomkins	11,471
Rentokil Initial	9,283
Hays	9,059
Carillion	8,248
BSS	8,034
Balfour Beatty	7,321
BBA Aviation	6,996
Interserve	6,946
Morgan Crucible	6,679
Homeserve	6,634
Ultra Electronics	6,456
SIG	5,790
Marshalls	5,280
VP	5,028

Company	£'000
Filtrona	4,760
Chloride	4,035
Halma	3,964
Smiths News	3,923
Xchanging	3,419
QinetiQ	3,303
Fiberweb	3,281
Henry Boot	3,179
Fenner	2,579
Premier Farnell	2,566
Electrocomponents	2,102
Spirax Sarco	1,419
Travis Perkins	1,347
E2V Technologies	1,328
Readymix[4]	1,058
TT electronics	955
Norcros	692
	159,036
Consumer Goods	
Bellway	15,227
Persimmon	14,843
Bovis Homes	10,213
Redrow	7,863
M P Evans[2]	7,043
GKN	5,411
Taylor Wimpey	4,501
Dairy Crest	4,199
New Britain Palm Oil	3,479
Premier Foods	3,209
AGA Rangemaster	1,994
SSL International	1,619
UNIQ	657
	80,242
Oil & Gas	
Venture Production	12,597
Premier Oil	9,945
Dana Petroleum	8,911
John Wood	8,778
Wellstream	7,882
Hunting	7,683
Petrofac	7,448
Addax Petroleum	5,312
Soco International	4,193
JKX Oil & Gas	3,998
Serica Energy[2]	2,260
Resaca Exploitation[2]	1,134
	80,141

Company	£'000
Technology	
Logica CMG	5,429
Psion	3,035
Blinkx[2]	2,753
Vislink	1,676
Kewill Systems	1,492
	14,385
Basic Materials	
Mondi	9,675
Tennants Consolidated[1]	2,180
	11,855
Utilities	
Northumbrian Water	7,286
	7,286
Telecommunications	
Colt Telecom	5,519
	5,519
Total Portfolio[5]	**716,891**

[1]Unquoted investment.

[2]AIM listed investment.

[3]Includes convertible bond.

[4]Listed in Ireland.

[5]The portfolio comprises investments in equity shares and a convertible bond.

Board of Directors

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

He is a Managing Director and Chairman of the European Investment Banking Committee at Credit Suisse Securities (Europe) Limited and a director of Persimmon plc.

Lord 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.

Richard Hambro
A Director since October 2006.

He is Chairman of JO Hambro Investment Management Limited, a subsidiary of Credit Suisse Private Bank. He is also Chairman of I Hennig & Co, Newmarket Racecourses Trust, Smiths Holdings Limited, Wilton's (St. James's) Limited and The Joint British Cancer Charities.

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 a non-executive director of Artemis Alpha Trust plc and 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 17th May 2007. He is Chairman of Johnston Press plc, Advanced Power AG, Remploy 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, who stood down from membership of the Audit Committee on 19th March 2008.

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 for the year ended 31st January 2009.

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 842 of the Income and Corporation Taxes Act 1988 for the year ended 31st January 2008. In the opinion of the Directors, the Company has subsequently conducted its affairs so that it should continue to qualify. The Company will continue to seek approval under Section 842 of the Income and Corporation Taxes Act 1988 each year.

Approval for the year ended 31st January 2008 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 8.

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 2009, the Company produced a total return to shareholders of –39.2% and a total return on net assets of –39.3%. This compares with the return on the Company's benchmark index of –36.2%. As at 31st January 2009, the value of the Company's investment portfolio was £716.9 million. The Investment Managers' Report on pages 5 to 8 includes a review of developments during the year as well as information on investment activity within the Company's portfolio.

Total Return, Revenue and Dividends

Gross total loss for the year amounted to £437.0 million (2008: £219.4 million) and net total loss after deducting interest, management expenses and taxation amounted to £452.4 million (2008: £233.2 million). Distributable income for the year amounted to £43.0 million (2008: £44.3 million). The Directors have declared quarterly interim dividends totalling 36.0p per ordinary share (2008: 34.0p ordinary dividend and 4.0p special dividend) for the year which totalled £36.9 million (2008: £40.1 million). The year end revenue reserve after allowing for these dividends will amount to £41.0 million (2008: £34.9 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.

Directors' Report – continued

Performance relative to Benchmark Index

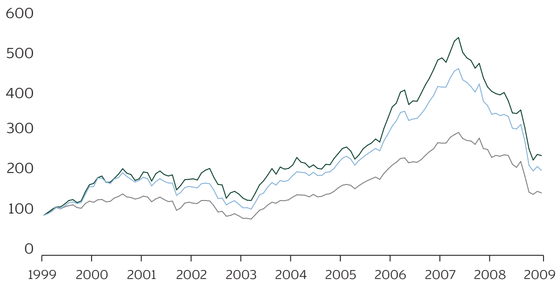
Figures have been rebased to 100 at 31st January 1999

- The Mercantile – Net asset value total return
- The Mercantile – Share price total return
- Benchmark

Source: Standard & Poor's – www.funds.morningstar.com/Fundamental Data – www.funddata.com/Russell Mellon caps

Ten Year Performance

Figures have been rebased to 100 at 31st January 1999



- The Mercantile – Net asset value total return
- The Mercantile – Share price total return
- Benchmark

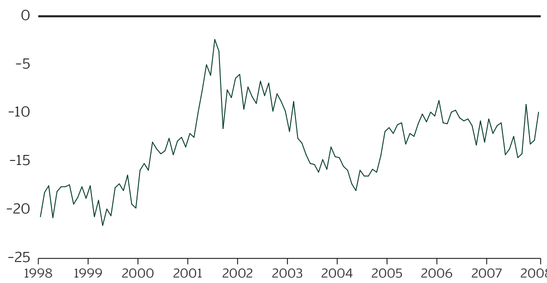
Source: Standard & Poor's – www.funds.morningstar.com/Fundamental Data – www.funddata.com/Russell Mellon caps

- 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 2009 are given in the Investment Managers' Report on page 5.

- 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 minimise 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 and fees incurred in connection with VAT recoveries, expressed as a percentage of the average of the opening and closing net assets. The TER for the year ended 31st January 2009 was 0.56% (2008: 0.59%). 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 1,981,198 ordinary shares for cancellation. This amount represented 1.9% 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 not repurchased any 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.

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 842 of the Income and Corporation Taxes Act 1988 ('Section 842'). Details of the Company's approval are given under 'Business of the Company' above. Were the Company to breach Section 842, 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 842 qualification criteria are continually monitored by JPMAM and the results reported to the Board each month. The Company must also comply with the provisions of the Companies Act 1985 and 2006 and, since its shares are listed on the London Stock Exchange, the UKLA Listing Rules. A breach of the Companies Act 1985 or 2006 could result in the Company and/or the Directors being fined or the subject of criminal proceedings. Breach of the UKLA Listing Rules could result in the Company's shares being suspended from listing which in turn would breach Section 842. The Board relies on the services of its Company Secretary, JPMAM, to ensure compliance with The Companies Act 1985 and 2006 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 22 to 24.
- 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 24.
- 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 22 on pages 43 to 46.

Future Developments

Clearly, the future development of the Company is much dependent upon the success of the Company's investment strategy in the light of economic and equity market developments. 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 consistent outperformance of the benchmark over the long term and the support that the Company receives from JPMAM.

Directors' Report – continued

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 17), risk management policies (see page 43), capital management policies and procedures (see page 47), 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 2009, 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 2009	1st February 2008 or at date of appointment
Hamish Leslie Melville	30,000	30,000
Lord Halifax	2,000	2,000
Richard Hambro	30,000	30,000
Sandy Nairn	5,000	5,000
Charles Peel	33,100	20,000
Ian Russell	5,000	5,000

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

In accordance with the Company's Articles of Association, none of the Directors are required to offer themselves for re-election. Pursuant to the Financial Reporting Council Combined Code, having served as a Director for more than nine years, Hamish Leslie Melville is subject to annual re-election.

During the year an insurance policy has been maintained by the Company which indemnifies the Directors of the Company against certain liabilities arising in the conduct of their duties.

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 234Z of the Companies Act 1985.

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

Details of the voting rights in the Company's shares as at the date of this report are given in note 11 to the Notice of AGM on page 51.

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	11,841,361	11.57
Chase Nominees Ltd[1]	6,971,318	6.81
JPMorgan Asset Management (UK) Ltd	5,479,153	5.35
Rathbone Investment Management Ltd	5,409,835	5.29
Brewin Dolphin Ltd	4,674,317	4.57
Legal & General Group plc	4,053,293	3.96
Rensburg Sheppards Investment Management Ltd	3,829,165	3.74
Citigroup Quilter	3,295,941	3.22

[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 Act 1985 and 2006.

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

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.

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:

Repurchase of the Company's shares (resolution 5)

At the Annual General Meeting held in April 2008, 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 29th October 2009 unless renewed by shareholders. The repurchase of shares at a discount to the underlying net asset value ('NAV') would enhance the NAV of the remaining shares.

Recommendation

The Board considers resolution 5 is likely to promote the success of the Company and is in the best interests of the Company and its shareholders as a whole. The Directors unanimously recommend that you vote in favour of the resolution as they intend to do in respect of their own beneficial holdings which amount in aggregate to 105,100 shares representing approximately 0.1% of the existing issued ordinary share capital of the Company. The full text of the resolution is set out in the Notice of Meeting on page 50.

By order of the Board
Juliet Dearlove, for and on behalf of
JPMorgan Asset Management (UK) Limited,
Secretary
24th March 2009

Corporate Governance

Compliance

The Company is committed to high standards of corporate governance. This statement, together with the Statement of Directors' Responsibilities on page 26, indicates how the Company has applied the principles of good governance of the Financial Reporting Council Combined Code (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, other than in respect of the provision relating to the appointment of a senior independent director, and the AIC Code throughout the year under review.

Role of the Board

A management agreement between the Company and JPMAM sets out the matters over which the Manager has authority. This includes management of the Company's assets and the provision of accounting, company secretarial, administration, and some marketing services. The Company delegates responsibility for voting investee shares to JPMAM. Details of JPMAM's Voting Policy and Corporate Governance Guidelines are available from JPMAM on request or can be accessed at www.jpmorganassetmanagement.co.uk/institutional. Within the "Commentary & Analysis" tab there is a section on Corporate Governance.

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 16.

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

Directors are initially appointed until the following Annual General Meeting when, under the Company's Articles of Association, it is required that they be elected by shareholders. Thereafter, a Director's appointment will run for a term of three years. Subject to the performance evaluation carried out each year, the Board will agree whether it is appropriate for the Director to seek an additional term. Any Director who has served for a period of more than nine years will submit himself for annual re-election thereafter.

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

The Board recommends the re-election of Hamish Leslie Melville, who retires by rotation 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 16. Directors who are not members of Committees may attend at the invitation of the Chairman.

In line with corporate governance guidance, the Chairman decided to stand down from the Audit Committee with effect from 19th March 2008.

The table below details the number of Board, Audit Committee and Nomination Committee meetings attended by each Director. During the year there were seven 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	6	2*	0
Lord Halifax	6	2	1
Richard Hambro	6	2	1
Sandy Nairn	6	2	1
Charles Peel	7	2	1
Ian Russell	7	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 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 duties and to select and propose suitable candidates when necessary for appointment.

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.

Audit Committee

The Audit Committee, chaired by Ian Russell, consists of all the Directors other than the Chairman (from 19th March 2008) 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 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. 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 24.

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

Corporate Governance – continued

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 48.

The Company's Annual Report and Accounts is published in time to give shareholders at least 20 working days' notice of the Annual General Meeting. Shareholders wishing to raise questions in advance of the meeting are encouraged to write to the Company Secretary at the address shown on page 48 or via the website.

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

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. 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, 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 2009, 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.

Directors' Remuneration Report

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

The law requires the Company's auditors to audit certain of the disclosures provided. Where disclosures have been audited they are indicated as such. The auditors' opinion is included in their report on page 27.

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.

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 22.

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: Russell/Mellon Caps/Standard & poor's – www.funds.morningstar.com

Directors' Remuneration

(Audited Information) Director's Name	2009 £	2008 £
Hamish Leslie Melville (Chairman)	45,000	40,969
Nicholas Berry[1]	–	7,635
Richard Hambro	30,000	28,750
Simon Keswick[1]	–	7,635
Sandy Nairn	30,000	28,750
Charles Peel	30,000	28,750
Lord Rothermere[1]	–	7,635
Ian Russell[2]	35,000	34,532
Lord Halifax[3]	30,000	4,692
Total	**200,000**	**189,348**

[1]Retired as a Director on 16th May 2007.

[2]Appointed as a Director on 1st January 2007.

[3]Appointed as a Director on 5th December 2007.

By order of the Board
Juliet Dearlove, for and on behalf of
JPMorgan Asset Management (UK) Limited,
Secretary
24th March 2009

Directors' Responsibilities in Respect of the Accounts

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

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

The Directors confirm that the accounts comply with the above requirements.

The Directors are responsible for ensuring that proper accounting records are kept which disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the accounts comply with the Companies Act 1985 and the Companies Act 2006 as in force from time to time. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The accounts are published on the www.jpmorganassetmanagement.com website, which is maintained by the Company's investment Manager, JPMorgan Asset Management (UK) Limited ('JPMAM'). The maintenance and integrity of the website maintained by JPMAM is, so far as it relates to the Company, the responsibility of JPMAM.

Statement under the Disclosure & Transparency Rules 4.1.12

The Directors each confirm to the best of their knowledge that:

a) the accounts, prepared in accordance with applicable accounting standards, give a true and fair view of the assets, liabilities, financial position and return or loss of the Company; and

b) this Annual Report includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that they face.

For and on behalf of the Board
Hamish Leslie Melville
24th March 2009

Independent Auditors' Report[1]

To the shareholders of The Mercantile Investment Trust plc

We have audited the accounts of The Mercantile Investment Trust plc for the year ended 31st January 2009 which comprise the Income Statement, the Reconciliation of Movements in Shareholders' Funds, the Balance Sheet, the Cash Flow Statement and the related notes. These accounts have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

Respective Responsibilities of Directors and Auditors

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

Our responsibility is to audit the accounts and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the accounts give a true and fair view and whether the accounts and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the accounts. The information given in the Directors' Report includes that specific information presented in the Chairman's Statement and the Investment Managers' Report that is cross referenced from the Business Review section of the Directors' Report.

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

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

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

Basis of Audit Opinion

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

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

Independent Auditors' Report – continued

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

Opinion

In our opinion:

- the accounts give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 31st January 2009 and of its net loss and cash flows for the year then ended;
- the accounts and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the accounts.

PRICEWATERHOUSECOOPERS LLP
Chartered Accountants and Registered Auditors
London,

24th March 2009

Income Statement

for the year ended 31st January 2009

	Notes	2009 Revenue £'000	2009 Capital £'000	2009 Total £'000	2008 Revenue £'000	2008 Capital £'000	2008 Total £'000
Losses on investments held at fair value through profit or loss	2	–	(488,753)	(488,753)	–	(271,045)	(271,045)
Net foreign currency losses		–	(26)	(26)	–	(42)	(42)
Income from investments	3	39,601	–	39,601	43,948	–	43,948
Other interest receivable and similar income	3	12,149	–	12,149	7,736	–	7,736
Gross return/(loss)		51,750	(488,779)	(437,029)	51,684	(271,087)	(219,403)
Management fee	4	(2,187)	(2,187)	(4,374)	(3,900)	(3,900)	(7,800)
VAT recoverable	4	1,130	1,069	2,199	2,921	2,922	5,843
Other administrative expenses	5	(2,144)	–	(2,144)	(842)	–	(842)
Net return/(loss) on ordinary activities before finance costs and taxation		48,549	(489,897)	(441,348)	49,863	(272,065)	(222,202)
Finance costs	6	(5,502)	(5,502)	(11,004)	(5,518)	(5,518)	(11,036)
Net return/(loss) on ordinary activities before taxation		43,047	(495,399)	(452,352)	44,345	(277,583)	(233,238)
Taxation	7	(19)	–	(19)	–	–	–
Net return/(loss) on ordinary activities after taxation		43,028	(495,399)	(452,371)	44,345	(277,583)	(233,238)
Return/(loss) per share	9	41.73p	(480.45)p	(438.72)p	39.79p	(249.10)p	(209.31)p

Dividends declared in respect of the financial year ended 31st January 2009 total 36.0p per share (2008: 34.0p ordinary dividend and 4.0p special dividend per share) costing £36,898,000 (2008: £40,113,000). Further information on dividends is given in note 8 on page 38.

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 33 to 47 form an integral part of these accounts.

Reconciliation of Movements in Shareholders' Funds

for the year ended 31st January 2009

	Called up share capital £'000	Share premium £'000	Capital redemption reserve £'000	Capital reserves £'000	Revenue reserve £'000	Total £'000
At 31st January 2007	31,264	23,459	5,506	1,639,238	44,381	1,743,848
Shares bought back and cancelled	(5,189)	–	5,189	(271,068)	–	(271,068)
Net (loss)/return from ordinary activities	–	–	–	(277,583)	44,345	(233,238)
Dividends appropriated in the year	–	–	–	–	(31,392)	(31,392)
At 31st January 2008	26,075	23,459	10,695	1,090,587	57,334	1,208,150
Shares bought back and cancelled	(495)	–	495	(17,586)	–	(17,586)
Net (loss)/return from ordinary activities	–	–	–	(495,399)	43,028	(452,371)
Dividends appropriated in the year	–	–	–	–	(40,895)	(40,895)
At 31st January 2009	25,580	23,459	11,190	577,602	59,467	697,298

The notes on pages 33 to 47 form an integral part of these accounts.

Balance Sheet

at 31st January 2009

	Notes	2009 £'000	2008 £'000
Fixed assets			
Investments at fair value through profit or loss	10	716,891	1,145,680
Current assets	12		
Debtors		1,786	7,798
Cash and short term deposits		171,392	287,985
		173,178	295,783
Creditors: amounts falling due within one year	13	(15,966)	(56,604)
Net current assets		157,212	239,179
Total assets less current liabilities		874,103	1,384,859
Creditors: amounts falling due after more than one year	14	(176,805)	(176,709)
Total net assets		697,298	1,208,150
Capital and reserves			
Called up share capital	15	25,580	26,075
Share premium	16	23,459	23,459
Capital redemption reserve	16	11,190	10,695
Capital reserves	16	577,602	1,090,587
Revenue reserve	16	59,467	57,334
Shareholders' funds		697,298	1,208,150
Net asset value per share	17	681.5p	1,158.3p

The accounts on pages 29 to 47 were approved and authorised for issue by the Directors on 24th March 2009 and are signed on their behalf by:

Hamish Leslie Melville
Chairman

The notes on pages 33 to 47 form an integral part of these accounts.

Cash Flow Statement

for the year ended 31st January 2009

	Notes	2009 £'000	2008 £'000
Net cash inflow from operating activities	18	54,483	45,371
Servicing of finance			
Interest paid		(10,898)	(10,927)
Net cash outflow from servicing of finance		(10,898)	(10,927)
Taxation			
Overseas tax recovered		16	–
Financial investment			
Purchases of investments		(1,320,325)	(1,079,216)
Sales of investments		1,217,694	1,509,476
Settlement of option contracts		975	–
Other capital charges		(31)	(61)
Net cash (outflow)/inflow from financial investment		(101,687)	430,199
Total dividends paid		(40,895)	(31,392)
Net cash (outflow)/inflow before financing		(98,981)	433,251
Financing			
Repurchase of ordinary shares		(17,586)	(274,953)
Net cash outflow from financing		(17,586)	(274,953)
(Decrease)/increase in cash in the year	19	(116,567)	158,298

The notes on pages 33 to 47 form an integral part of these accounts.

Notes to the Accounts

for the year ended 31st January 2009

1. Accounting Policies

(a) Basis of accounting

The accounts are prepared in accordance with the Companies Act 1985. United Kingdom Generally Accepted Accounting Practice ('UK GAAP') and with the Statement of Recommended Practice 'Financial Statements of Investment Trust Companies' (the 'SORP') issued by the Association of Investment Companies ('AIC') 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 Company has a dormant, wholly owned subsidiary 'Mercantile Management Limited'. Consolidated accounts have not been prepared as exemption under S229 of the Companies Act 1985 has been exercised due to the immateriality of the subsidiary.

(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 '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 is bid market price for listed investments. Unlisted and restricted investments are valued at fair value by the Board. In making its valuations, the Board takes into account, where appropriate, latest dealing prices, valuations from reliable sources, asset values and other relevant factors.

Changes in the fair value of investments held at fair value through profit or loss and gains and losses on sales are included in capital within 'Losses on investments held at fair value through profit or loss'. Gains and losses on sales of investments and exchange differences of a capital nature are accounted in capital reserves within 'Gains on sales of investments'. Increases and decreases in the valuation of investments held at the year end are accounted for in capital reserves within 'Investment holding losses'.

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

(c) Income

Dividends receivable from equity shares are included in the revenue column of the income statement 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 the capital column.

UK dividends are included net of any 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 the revenue column of the income statement. Any excess in the value of the shares received over the amount of the cash dividend is recognised in the capital column.

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

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

Stock lending income and underwriting commission are taken to the revenue column on a receipts basis.

(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:

- management fees are allocated 50% to the revenue column and 50% to the capital column in line with the Board's expected long term split of revenue and capital return from the Company's investment portfolio.
- expenses incidental to the purchase and sale of an investment are charged to the capital column. 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 39.

Notes to the Accounts – continued

1. Accounting Policies – 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'.

Finance costs are allocated 50% to the revenue column of the income statement and 50% to the capital column in line with the Board's expected long term split of revenue and capital return from the Company's investment portfolio.

Breakage costs incurred on the early repayment of loans are charged 100% to the capital column in accordance with the SORP.

(f) Financial instruments

Cash at bank and in hand 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 receivables and payables do not carry any interest, are short term in nature and are accordingly stated at nominal value as 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.

(h) VAT

Irrecoverable VAT is expensed to capital or income in the proportions in which it has been suffered. The basis on which it has been calculated is the partial exemption method using the proportion of taxable supplies to non taxable supplies. Further information regarding VAT on management fees is given in note 4 on page 36.

(i) Foreign currency

In accordance with FRS23: '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.

Any gain or loss arising on monetary assets from a change in exchange rates subsequent to the date of the transaction is included as an exchange gain or loss in revenue or capital, depending on whether the gain or loss is of a revenue or capital nature. Gains and losses on investments arising from a change in exchange rates are included in gains from investments held at fair value through profit or loss.

(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.

	2009 £'000	2008 £'000
2. Losses on investments held at fair value through profit or loss		
(Losses)/gains on investments held at fair value through profit or loss based on historical cost	(206,024)	268,358
Amounts recognised in investment holding losses/(gains) in the previous year in respect of investments sold during the year	61,592	(271,828)
Losses on sales of investments based on carrying value at previous balance sheet date	(144,432)	(3,470)
Net movement in investment holding losses	(345,265)	(267,529)
Gains on option contracts	975	–
Other capital charges	(31)	(46)
Total capital losses on investments held at fair value through profit or loss	(488,753)	(271,045)

	2009 £'000	2008 £'000
3. Income		
Income from investments		
UK dividends	36,918	42,443
Property income distribution	910	21
Overseas dividends	1,773	1,484
	39,601	43,948
Other interest receivable and similar income		
Deposit interest	9,853	7,703
Interest on VAT recovered[1]	2,090	–
Underwriting commission	206	33
	12,149	7,736
Total income	51,750	51,684
Analysis of income from investments:		
Listed in the UK	36,177	38,151
Unlisted	1,651	4,313
Listed overseas	1,773	1,484
	39,601	43,948

[1]This represents interest on VAT recovered relating to management fees paid in the past. Further details are given in note 4 on page 36.

Notes to the Accounts – continued

	2009 Revenue £'000	2009 Capital £'000	2009 Total £'000	2008 Revenue £'000	2008 Capital £'000	2008 Total £'000
4. Management fee						
Management fee[1]	2,187	2,187	4,374	3,468	3,468	6,936
VAT thereon	–	–	–	432	432	864
	2,187	2,187	4,374	3,900	3,900	7,800
VAT recoverable[2]	(1,130)	(1,069)	(2,199)	(2,921)	(2,922)	(5,843)
	1,057	1,118	2,175	979	978	1,957

[1] Details of the management fee are given in the Directors' Report on page 20.

[2] No VAT has been charged on management fees since November 2007 when HM Revenue & Customs announced acceptance that VAT was not chargeable on investment trust management fees. The Company has since recovered VAT amounting to £8,042,000 in respect of VAT paid in the past. Of this amount £5,843,000 was included in the accounts for the year ended 31st January 2008. The balance of £2,199,000 is included in the accounts this year. The amounts have been allocated between revenue and capital in the same proportions as they were originally expensed to revenue and capital. Interest amounting to £2,090,000 has also been received and allocated wholly to revenue in this year and is included within 'other interest receivable and similar income' in note 3 on page 35.

	2009 £'000	2008 £'000
5. Other administrative expenses		
Other management expenses[1]	1,796	568
Directors' fees[2]	200	189
Savings products[3]	113	49
Auditors' remuneration for audit services[4]	34	35
Auditors' remuneration for all other services	1	1
	2,144	842

[1] Includes £1,165,000 (2008: nil) of professional fees in connection with VAT recoveries, including interest, amounting to £10,132,000.

[2] Full disclosure is given in the Directors' Remuneration Report on page 25.

[3] These fees were paid to JPMAM for the marketing of 'Wrapper products'.

[4] Includes £5,000 (2008: £5,000) irrecoverable VAT.

	2009 Revenue £'000	2009 Capital £'000	2009 Total £'000	2008 Revenue £'000	2008 Capital £'000	2008 Total £'000
6. Finance costs						
Bank loans and overdrafts	13	13	26	29	29	58
Debentures	5,489	5,489	10,978	5,489	5,489	10,978
	5,502	5,502	11,004	5,518	5,518	11,036

	2009 £'000	2008 £'000
7. Taxation		
(a) Analysis of tax charge in the year		
UK Corporation tax at 28.32% (2008: 30%)	–	–
Prior year adjustment	19	–
Current tax charge for the year	19	–

	2009 Revenue £'000	2009 Capital £'000	2009 Total £'000	2008 Revenue £'000	2008 Capital £'000	2008 Total £'000
(b) Factors affecting current tax charge for the year						
Net return/(loss) on ordinary activities before taxation	43,047	(495,399)	(452,352)	44,345	(277,583)	(233,238)
Net return/(loss) on ordinary activities before taxation multiplied by the Company's applicable rate of corporation tax of 28.32% (2008: 30%)	12,191	(140,297)	(128,106)	13,304	(83,275)	(69,971)
Effect of:						
Non taxable UK dividend income	(10,455)	–	(10,455)	(12,739)	–	(12,739)
Non taxable capital losses	–	138,422	138,422	–	81,326	81,326
Excess capital expense arising in the year	–	1,875	1,875	–	1,949	1,949
Unrelieved expenses	(1,736)	–	(1,736)	(565)	–	(565)
Prior year adjustment	19	–	19	–	–	–
	19	–	19	–	–	–

The Company has an unrecognised deferred tax asset of £37,592,000 based on the prospective corporation tax rate of 28% (2008: £37,455,000). This has arisen from deductible expenses exceeding 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 deferred tax on any capital gains or losses arising on the revaluation or disposal of investments.

Notes to the Accounts – continued

	2009 £'000	2008 £'000
8. Dividends		
(a) Dividends paid and declared		
Unclaimed dividends refunded to the Company[1]	(10)	(38)
2008 fourth quarterly dividend of 17.5p (2007: 11.5p) paid to shareholders in May	18,253	13,742
2008 special dividend of 4.0p (2007: nil) paid to shareholders in May	4,172	–
First quarterly dividend of 6.0p (2008: 5.5p) paid to shareholders in August	6,186	6,039
Second quarterly dividend of 6.0p (2008: 5.5p) paid to shareholders in November	6,147	5,881
Third quarterly dividend of 6.0p (2008: 5.5p) paid to shareholders in February	6,147	5,768
Total dividends paid in the year	40,895	31,392

[1] Represents dividends which remain unclaimed after a period of 12 years and thereby become the property of the Company.
[2] Paid on 30th January.

	2009 £'000	2008 £'000
Fourth quarterly dividend of 18.0p (2008: 17.5p) payable to shareholders in May	18,418	18,253
Special dividend of nil (2008: 4.0p) payable to shareholders in May	–	4,172
	18,418	22,425

The fourth quarterly dividend has been declared in respect of the year ended 31st January 2009. In accordance with the accounting policy of the Company, this dividend will be reflected in the accounts for the year ending 31st January 2010.

(b) Dividend for the purposes of section 842 of the Income and Corporation Taxes Act 1988

The requirements of section 842 of the Income and Corporation Taxes Act 1988 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 £43,028,000 (2008: £44,345,000).

	2009 £'000	2008 £'000
First quarterly dividend of 6.0p (2008: 5.5p) paid in August	6,186	6,039
Second quarterly dividend of 6.0p (2008: 5.5p) paid in November	6,147	5,881
Third quarterly dividend of 6.0p (2008: 5.5p) paid in February	6,147	5,768
Fourth quarterly dividend of 18.0p (2008: 17.5p) payable in May	18,418	18,253
Special dividend of nil (2008: 4.0p) paid in May	–	4,172
	36,898	40,113

9. Return/(loss) per share

The revenue return per share is based on the earnings attributable to the ordinary shares of £43,028,000 (2008: £44,345,000) and on the weighted average number of ordinary shares in issue during the year of 103,110,703 (2008: 111,433,402).

The capital loss per share is based on the capital losses attributable to the ordinary shares of £495,399,000 (2008: £277,583,000) and on the weighted average number of ordinary shares in issue during the year of 103,110,703 (2008: 111,433,402).

The total loss per share is based on the total loss attributable to the ordinary shares of £452,371,000 (2008: £233,238,000) and on the weighted average number of ordinary shares in issue during the year of 103,110,703 (2008: 111,433,402).

	2009 £'000	2008 £'000
10. Investments		
Investments listed on a recognised stock exchange	651,722	1,053,473
Unlisted investments	65,169	92,207
	716,891	1,145,680

	Listed in UK £'000	Listed Overseas £'000	Unlisted £'000	Total £'000
Opening book cost	1,126,673	12,001	73,548	1,212,222
Opening investment holding (losses)/gains	(84,646)	(555)	18,659	(66,542)
Opening valuation	1,042,027	11,446	92,207	1,145,680
Movements in the year:				
Purchases at cost	1,229,115	5,603	43,900	1,278,618
Sales - proceeds	(1,198,664)	(8,772)	(10,274)	(1,217,710)
Losses on sales based on fair value at the previous balance sheet date	(138,025)	(2,673)	(3,734)	(144,432)
Net movement in investment holding losses	(283,789)	(4,546)	(56,930)	(345,265)
	650,664	1,058	65,169	716,891
Closing book cost	955,034	5,605	106,467	1,067,106
Closing investment holding losses	(304,370)	(4,547)	(41,298)	(350,215)
Total investments at fair value	650,664	1,058	65,169	716,891

Transaction costs on purchases during the year amounted to £7,449,000 (2008: £6,621,000) and on sales during the year amounted to £1,547,000 (2008: £2,125,000). These costs comprise stamp duty and broker commission.

Unlisted investments include Alternative Investment Market stocks which are valued at £50,096,000 (2008: £71,868,000).

During the year, prior year investment holding (losses)/gains have been transferred to gains on sales of investments as disclosed in note 16 on page 41. This was derived from the following sources:

	Listed in UK £'000	Listed Overseas £'000	Unlisted £'000	Total £'000
	(64,065)	(554)	3,027	(61,592)

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 are as follows:

Name of company	Country of registration	Class of share	% of class held
Tennants Consolidated	UK	15% Pref	24.9

In addition to the above, the Company has interests of 3% or more in the share capital of another 44 (2008: 31) 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 2009 was £143,173,000 (2008: £218,166,000).

Notes to the Accounts – continued

	2009 £'000	2008 £'000
12. Current assets		
Debtors		
Securities sold awaiting settlement	239	223
Amount due from subsidiary[1]	250	250
Dividends and interest receivable	1,193	1,433
VAT recoverable	–	5,843
Other debtors	104	49
	1,786	7,798

[1] The Company has incorporated a wholly owned subsidiary, 'Mercantile Management Limited', with share capital of £250,000. This amount was loaned back to the Company under commercial terms. This subsidiary is dormant.

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 cash held by the Company, including short term bank 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.

	2009 £'000	2008 £'000
13. Creditors: amounts falling due within one year		
Securities purchased awaiting settlement	9,268	50,975
Loan due to subsidiary[1]	287	277
Other creditors and accruals	6,411	5,352
	15,966	56,604

[1] Includes accrued interest payable on the loan due to the subsidiary. Further details are given in note 12.

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

The Company had a £70m 364 day revolving credit facility in place with Lloyds TSB, which was never drawn down and expired on 4th March 2008.

	2009 £'000	2008 £'000
14. Creditors: amounts falling due after more than one year		
Falling due after more than five years		
4.25% Perpetual debenture stock[1]	3,850	3,850
6.125% Debenture stock[2]	172,955	172,859
	176,805	176,709

[1] The 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 security is enforced.

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

	2009 £'000	2008 £'000
15. Called up share capital		
Authorised:		
163,875,000 (2008: 163,875,000) ordinary shares of 25p each	40,969	40,969
Allotted and fully paid:		
Opening balance of 104,303,166 (2008: 125,058,759) shares	26,075	31,264
Repurchase of 1,981,198 (2008: 20,755,593) shares	(495)	(5,189)
Closing balance of 102,321,968 (2008: 104,303,166) shares	25,580	26,075

During the year, the Company made market purchases of 1,981,198 of it own shares, nominal value £495,000, for cancellation, representing 1.9% of the shares outstanding at the beginning of the year. The total consideration paid for these shares was £17,586,000.

			Capital reserves		
	Share premium £'000	Capital redemption reserve £'000	Gains on sales of investments £'000	Investment holding – losses £000	Revenue reserve £'000
16. Reserves					
Opening balance	23,459	10,695	1,157,129	(66,542)	57,334
Net currency losses on cash and short term deposits held during the year	–	–	(26)	–	–
Losses on sales of investments based on fair value at the previous balance sheet date	–	–	(144,432)	–	–
Gains on option contracts	–	–	975	–	–
Net movement in investment holding losses	–	–	–	(345,265)	–
Transfer on disposal of investments	–	–	(61,592)	61,592	–
Repurchase and cancellation of shares	–	495	(17,586)	–	–
Management fee and finance costs charged to capital	–	–	(7,689)	–	–
Other capital charges	–	–	(31)	–	–
VAT recovered	–	–	1,069	–	–
Dividends appropriated in the year	–	–	–	–	(40,895)
Retained revenue for the year	–	–	–	–	43,028
Closing balance	23,459	11,190	927,817	(350,215)	59,467

17. Net asset value per share

The net asset value per share is based on the net assets attributable to the ordinary shareholders of £697,298,000 (2008: £1,208,150,000) and on the 102,321,968 (2008: 104,303,166) shares in issue at the year end.

Notes to the Accounts – continued

	2009 £'000	2008 £'000
18. Reconciliation of net loss on ordinary activities before finance costs and taxation to net cash inflow from operating activities		
Total loss on ordinary activities before finance costs and taxation	(441,348)	(222,202)
Less capital loss before finance costs and taxation	489,897	272,065
Decrease in accrued income	240	1,892
Decrease/(increase) in VAT recoverable	5,843	(5,843)
(Increase)/decrease in other debtors	(90)	6
Increase in accrued expenses	1,059	431
Expenses charged to capital	(1,118)	(978)
Net cash inflow from operating activities	54,483	45,371

	At 31st January 2008 £'000	Cash flow £'000	Other exchange movement £'000	Non cash movements £'000	At 31st January 2009 £'000
19. Analysis of changes in net funds/(debt)					
Cash and short term deposits	287,985	(116,567)	(26)	–	171,392
Debentures falling due after more than five years	(176,709)	–	–	(96)	(176,805)
Net funds/(debt)	111,276	(116,567)	(26)	(96)	(5,413)

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 £4,374,000 (2008: £6,936,000 excluding VAT) of which £262,000 (2008: £456,000) was outstanding at the year end.

During the year £113,000 (2008: £49,000) was payable to JPMAM for the marketing of 'wrapper' products, of which £28,000 (2008: £9,000) was outstanding at the year end.

Included in other management expenses in note 5 on page 36 are safe custody fees amounting to £11,000 (2008: £89,000) payable to JPMorgan Chase Bank of which £6,000 (2008: £25,000) 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 £32,000 (2008: £145,000) of which £nil (2008: £nil) was outstanding at the year end.

During the year, commission on dealing transactions amounting to £926,000 (2008: £546,000) was paid to JPMorgan subsidiaries of which £nil (2008: £nil) was outstanding at the year end.

Handling charges on dealing transactions amounting to £29,000 (2008: £46,000) were payable to JPMorgan Chase during the year of which £8,000 (2008: £6,000) was outstanding at the year end.

At the year end, a bank balance of £171.4 million (2008: £114.0 million) was held with JPMorgan Chase. A net amount of interest of £7.3 million (2008: £0.3 million) was received by the Company during the year from JPMorgan Chase.

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

As an investment trust the Company invests in equities for the long term so as secure its investment objective stated on page 17. 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 financial risks is set out below. The Company Secretary, in close cooperation with the Board and the Manager, coordinates the Company's risk management. The Company has no material exposure to foreign currencies.

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, which are held in accordance with the Company's investment objective;
- short term debtors, creditors and cash arising directly from its 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, which 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.

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 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 with an overdraft facility used when required.

Therefore the Company would not normally have any significant exposure to interest rate risk. However the Company was holding high levels of cash and short term deposits at the year end due to unusual market conditions. The Company's exposure to cash flow interest rate risk due to cash and deposit balances at the year end was as follows:

	2009 £'000	2008 £'000
Exposure to floating interest rates		
Cash at bank and short term deposits	171,392	287,985

Interest received on cash balances, or paid on overdrafts, is at a margin below or above LIBOR respectively (2008: same).

Notes to the Accounts – continued

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

The above year end amounts are not representative of the exposure to interest rates during the year as the level of cash balances has fluctuated. The maximum and minimum cash balances during the year are as follows:

	2009 £'000	2008 £'000
Maximum cash at bank and short term deposits	292,272	287,985
Minimum cash at bank and short term deposits	143,647	20,583

Interest rate sensitivity

The following table illustrates the sensitivity of the profit after taxation for the year and net assets to a 1% (2008: 1%) increase or decrease in interest rates applied to the Company's cash balances. 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 cash balances at the balance sheet date with all other variables held constant.

	2009		2008	
	1% Increase in rate £'000	1% Decrease in rate £'000	1% Increase in rate £'000	1% Decrease in rate £'000
Income statement – profit after taxation				
Revenue return	857	(857)	1,440	(1,440)
Capital return	857	(857)	1,440	(1,440)
Total profit after taxation for the year	1,714	(1,714)	2,880	(2,880)
Net assets	1,714	(1,714)	2,880	(2,880)

The above sensitivity analysis is not representative of the year as a whole as the level of cash balances has fluctuated.

(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.

The Board has used FTSE 100 index put options during the year to protect part of the portfolio from market falls.

Market price risk exposure

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

	2009 £'000	2008 £'000
Investments at fair value through profit or loss	716,891	1,145,680

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 14 to 15 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's country of domicile or of listing does not necessarily equate to its exposure to the economic conditions in that country.

Market price risk sensitivity

The following table illustrates the sensitivity of the profit after taxation for the year and net assets to an increase or decrease of 20% (2008: 10%) 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 with all other variables held constant.

	2009		2008	
	20% Increase in fair value £'000	20% Decrease in fair value £'000	10% Increase in fair value £'000	10% Decrease in fair value £'000
Income statement – profit after taxation				
Revenue return – (decrease)/increase	(358)	358	(286)	286
Capital return – increase/(decrease)	143,020	(143,020)	114,282	(114,282)
Total profit after taxation – increase/(decrease)	142,662	(142,662)	113,996	(113,996)
Net assets – increase/(decrease)	142,662	(142,662)	113,996	(113,996)

(b) Liquidity risk

This is the risk that the Company will encounter difficulty in meeting its obligations associated with financial liabilities.

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 and to gear the Company as appropriate.

	2009				2008			
	Three months or less £'000	Not more than one year £'000	More than one year £'000	Total £'000	Three months or less £'000	Not more than one year £'000	More than one year £'000	Total £'000
Creditors: amounts falling due after more than one year								
Debenture stock	–	–	176,805	176,805	–	–	176,709	176,709
Creditors: amounts falling due within one year								
Amounts due to brokers	9,268	–	–	9,268	50,975	–	–	50,975
Loan from subsidiary	–	287	–	287	–	277	–	277
Other creditors	6,411	–	–	6,411	5,352	–	–	5,352
	15,679	287	176,805	192,771	56,327	277	176,709	233,313

(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.

Notes to the Accounts – continued

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

Management of credit risk continued

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 clearly ring-fenced in client designated accounts. Therefore, in the event that JPMorgan Chase were to cease trading, these assets would be protected.

Credit risk exposure

Compared to the balance sheet the maximum exposure to credit risk at the year end was as follows:

	2009 Balance sheet £'000	2009 Maximum exposure £'000	2008 Balance sheet £'000	2008 Maximum exposure £'000
Fixed assets – investments at fair value through profit or loss	716,891	–	1,145,680	–
Current assets				
Debtors – amount due from brokers, income receivable, prepayments and VAT recoverable	1,536	1,536	7,548	7,548
Amount due from subsidiary	250	–	250	–
Cash and short term deposits	171,392	171,392	287,985	287,985
	890,069	172,928	1,441,463	295,533

Cash and short term deposits comprises balances held at banks that have a minimum credit rating of A1/P1 from Standard & Poor's and Moody's respectively (2008: same).

(d) Fair values of financial assets and financial liabilities

All financial assets and liabilities are either included 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 by comparison with the market value of an instrument carrying a similar interest rate, risk rating and repayment date, as follows:

	Accounts value 2009 £'m	Accounts value 2008 £'m	Fair value 2009 £'m	Fair value 2008 £'m
£175 million 6.125% debenture stock 25th February 2030	173.0	172.9	203.5	193.4
£3.85 million 4.25% irredeemable debenture stock	3.8	3.8	3.0	2.8
	176.8	176.7	206.5	196.2

23. Capital management policies and procedures

The Company's capital comprises the following:

	2009 £'000	2008 £'000
Debt		
£175 million 6.125% debenture stock 25th February 2030	172,955	172,859
£3.85 million 4.25% irredeemable debenture stock	3,850	3,850
	176,805	176,709
Equity		
Equity share capital	25,580	26,075
Reserves	671,718	1,182,075
	697,298	1,208,150
Total capital	874,103	1,384,859

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.

	2009 £'000	2008 £'000
Investments at fair value	716,891	1,145,680
Net assets	697,298	1,208,150
Gearing	102.8%	94.8%

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, or sale of shares from Treasury; and
- the extent to which revenue in excess of that which is required to be distributed should be retained.

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.

Directors
Hamish Leslie Melville (Chairman)
Lord Halifax
Richard Hambro
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 shares may be dealt in directly through a stockbroker or through a professional adviser acting on an investor's behalf. They may also be purchased and held through the JPMorgan Investment Trust Share Plan, Individual Savings Account (ISA) and Pension Account.

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
Reference 1101
Aspect House
Spencer Way
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Telephone number: 0871 384 2329

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.

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

Brokers
JPMorgan Cazenove
20 Moorgate
London EC2R 6DA

Savings Product Administrators
For queries on the JPMorgan ISA, Share Plan or Pension Plan, see contact details on the back cover of this report.

Shareholder Analysis

at 31st January 2009

	Number of shares	% holding
Pensions	14,399,235	14,07
Unit Trusts	9,821,659	9.60
Insurance Companies	8,431,438	8.24
Other institutions	5,239,674	5.12
Investment Trusts	2,430,059	2.05
Charities	395,471	0.39
Total Institutions	42,142,501	39.47
Private Client Brokers	33,793,491	33.03
Retail investors holding shares directly or through nominee accounts [1]	15,987,383	15.62
Individuals in the Investment Trust Individual Savings Account [1,2]	4,045,651	3.96
Individuals in the Investment Trust Share Plan [2]	2,925,667	2.86
Individuals in the Investment Trust Pension Account [2]	475,406	0.46
Total Retail Holdings	57,227,598	55.93
Total Shares in Issue	102,321,968	100.0

Nominee accounts have been allocated to their appropriate category.

[1] Includes shares below 10,000 threshold.

[2] Savings products managed by JPMorgan.

Notice of Meeting

Notice is hereby given that the one hundred and twenty third Annual General Meeting of The Mercantile Investment Trust plc will be held at Trinity House, Tower Hill, London EC3N 4DH on Wednesday 29th April 2009 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 2009.

2 To approve the Directors' Remuneration Report for the year ended 31st January 2009.

3 To re-elect Hamish Leslie Melville a Director of the Company.

4 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 repurchase the Company's shares – Special Resolution

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

PROVIDED ALWAYS THAT

(i) the maximum number of ordinary shares hereby authorised to be purchased shall be 15,338,063 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 (a) 105 per cent of the average of the middle market quotations for an ordinary share taken from and calculated by reference to the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the ordinary share is purchased, or (b) the price of the last independent trade; or (c) the highest current independent bid;

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

(v) the authority hereby conferred shall expire on 28th October 2010 unless the authority is renewed at the Company's Annual General Meeting in 2010 or at any other general meeting prior to such time; and

(vi) the Company may make a contract to purchase ordinary shares under the authority hereby conferred prior to the expiry of such authority and may make a purchase of ordinary shares pursuant to any such contract notwithstanding such expiry.

By order of the Board
JPMorgan Asset Management (UK) Limited,
Secretary
24th March 2009

Notes

These notes should be reading 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, 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 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 note 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.

4 An instrument appointing a proxy, to be valid, must be lodged in accordance with the instructions given on the proxy form.

5 You may change your proxy instruction by returning a new proxy appointment. The deadline for receipt of proxy appointments (see above) 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 sent shall be treated as replacing and revoking the other or others.

6 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 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 days prior to the adjourned Meeting or, if the Company gives notice of the adjourned Meeting, at the time specified in that notice.

7 Entry to the Meeting will be restricted to shareholders, with guests admitted only by prior arrangement.

8 A corporation, which is a shareholder, may appoint individuals to act as its representatives and to vote in person at the Meeting (see instructions given on the proxy form).

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

Representatives should bring to the Meeting evidence of their appointment, including any authority under which it is signed.

9 The register of interests of the Directors and connected persons in the share capital of the Company is available for inspection at the Company's registered office during usual business hours on any weekday (Saturdays, Sundays and public holidays excepted). It will also be available for inspection at the Annual General Meeting.

10 No Director has any contract of service with the Company.

11 As at 24th March 2009 (being the latest business day prior to the publication of this Notice), the Company's issued share capital consists of 102,321,968 ordinary shares, carrying one vote each. Therefore the total voting rights in the Company are 102,321,968.

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

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 in the shares of the Company at the time the shares were quoted ex-dividend. Transaction costs of reinvestment are not taken into account.

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.

Benchmark Return
Total return on the benchmark, on a mid-market value to mid-market value basis, assuming that all dividends received (net of tax) were reinvested 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 stated index.

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 was to increase by 100%.

Total Expense Ratio (TER)
Management fees and all other operating expenses excluding interest and professional fees incurred in connection with VAT recoveries, expressed as a percentage of the average of the opening and closing net assets.

Discount/Premium
If the share price of an investment company is lower than the net asset value (NAV) per share, the trust is 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 company to trade at a discount than 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 outside of 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.

Residual
Arises when there is a divergence between total return as calculated by Fundamental Data (includes dividends paid out by the Investment Trust) and total return from the attribution systems (includes dividend income received on the stocks held by the Investment Trust). This is a result of methodologies and timing differences.

Share Buyback
Measures the effect on relative performance of decreasing the number of shares in issue.

JPMorgan Helpline
Freephone 0800 20 40 20 or 020 7742 9999
9.00 am to 5.30 pm Monday to Friday

JPMorgan Pension Helpline
Freephone 0800 41 31 76 or 0172 241 4888
9.00 am to 5.00 pm Monday to Friday
Please use this number if you have any queries relating to the Pension Account.

Your telephone call may be recorded for your security

www.mercantileit.co.uk