



The Merchants Trust PLC

Half-Yearly Financial Report

31 July 2019



1889-2019



Why invest in The Merchants Trust PLC?



High income returns

Merchants aims to provide an above average level of income and income growth together with long-term growth of capital through a policy of investing mainly in higher yielding large UK companies. Portfolio Manager Simon Gergel draws on the considerable research resources of Allianz Global Investors as well as his 31 years of investment experience.



Long-term conviction

The Merchants Trust has been providing an actively managed portfolio of investments since its launch in 1889. With a permanent capital base, the portfolio manager is able to construct a high conviction portfolio of investments, based upon the fundamental characteristics of companies and their long term prospects.



37 consecutive years of dividend growth

The trust has paid increasingly higher dividends to its shareholders year-on-year for the last 37 years – from 2.1 pence per share in 1982 to 26.0 pence per share in 2019. The trust can draw on revenue reserves to help smooth dividend payments during short-term periods of difficult economic conditions, although income is not guaranteed and could go down as well as up.



Liquidity and gearing

With total assets of £680m and over 110 million shares in issue, Merchants is one of the larger trusts in the market place. As an investment trust, Merchants is also able to employ gearing. This enhances the earnings per share, and potentially increases long term returns. However, shareholders should be aware that losses are also amplified when markets fall, which could lead to a substantial loss on their initial investment.



Cost-effective solution

Buying shares in an investment trust can be less costly than purchasing the underlying stocks individually – with an annual management fee of 0.35% (ongoing charges 0.58%)* Merchants provides a cost-effective way to access an actively managed portfolio.

* At 31 January 2019. See glossary on page 24.

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Building materials group CRH made a positive contribution to portfolio performance in the period. CRH company Ancon manufactured over 100,000 joints for the steel used to reinforce the concrete in the 2.7 kilometre Queensferry Crossing, one of the longest cable-stayed bridges in the world.



Financial Highlights

As at 31 July 2019

Yield*

5.4%

31 January 2019 **5.5%**

Dividend for the period

+4.7%

31 July 2019 **13.5p**
31 July 2018 **12.9p**

Revenue earnings per ordinary share

+3.2%

31 July 2019 **16.1p**
31 July 2018 **15.6p**

Net Asset Value Total Return**

+7.4%

31 July 2018 **+7.4%**

Share Price Total Return*

+5.1%

31 July 2018 **+8.7%**

Benchmark[~] Total Return*

+10.6%

31 July 2018 **+5.0%**

Net Asset Value per ordinary share**

493.2p

+4.6%



Share price

481.8p

+2.3%



* Alternative Performance Measure (APM).

Debt at market value.

[~] FTSE All-Share Index

See Glossary on page 24.

Revenue

Six months ended 31 July

	2019	2018	% change
Income	£19.6m	£19.0m	+3.2
Revenue earnings attributable to ordinary shareholders	£17.6m	£17.0m	+3.5
Revenue earnings per ordinary share	16.1p	15.6p	+3.2
Dividends per ordinary share	13.5p	12.9p	+4.7

Assets

	31 July 2019	31 January 2019	Capital return % change	Total return % change*
Net asset value per ordinary share with debt at par	518.2p	491.1p	+5.5	+8.2
Net asset value per ordinary share with debt at market value (capital)	493.2p	471.4p	+4.6	+7.4
Ordinary share price	481.8p	471.0p	+2.3	+5.1
FTSE All-Share Index	4,134.0	3,825.6	+8.1	+10.6
Discount ordinary share price to net asset value (debt at par)	-7.0%	-4.1%	n/a	n/a
Discount (debt at market value)	-2.3%	-0.1%	n/a	n/a

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



The sale of our holding in satellite communications company Inmarsat following a takeover bid was the largest contributor to portfolio performance during the period. Inmarsat owns and operates Global Xpress, the world's only global Ka-band satellite network, which offers reliable, uninterrupted in-flight high-speed Wi-Fi to airline passengers.

Interim Management Report



Dear Shareholder

In this landmark year after celebrating the 130th anniversary of The Merchants Trust in February, I am proud to be writing to you as I start my tenure as Chairman. First of all I must thank Simon Fraser for his immense contribution to the trust and commitment to shareholders over the past decade. During that time, and including his nine years as Chairman, the trust has successfully navigated various market conditions, economic cycles and political upheavals, and, today, finds itself a leading option for investors within its peer group. On behalf of shareholders and the board I thank Simon for his valued stewardship of The Merchants Trust and wish him well in his future ventures.

Half year results

In the last published Annual Report shareholders received a report of a challenging year for equity markets, particularly in the final months of 2018. Fortunately, in the past six months investor confidence has returned, at least in select areas, and we ended the period in a more positive position. Over the six months to 31 July 2019, the company's net asset value (NAV) total return of 7.4% (with debt at market value), although positive, was adrift of a strong FTSE All-Share Index performance of 10.6%. This was predominantly due to the underperformance of the value oriented UK equity portfolio compared to the wider market. You will find a more in-depth explanation of this, as well as a description of the current polarised nature of the UK stock market, in the Investment Manager's Review beginning on page 8. A performance attribution analysis can be found on page 7.

Renegotiation of the company's debt

On 3 July 2019, the board announced that a three year revolving credit facility had been entered into which was to be used to repay early the company's borrowings from Fintrust Debenture PLC of £42 million at the beginning of August 2019. The additional cost of redeeming the debentures was £14.4m and this was funded from existing assets. This was part of an eighteen month strategy to restructure the company's debt profile and this refinancing has significantly lowered the company's finance cost. The company's weighted average interest rate on all borrowings has fallen from 8.5% in January 2018 to 6.0% at the half year end

and following this latest refinancing exercise it is 3.5%. This has enhanced the company's earnings potential and your board believes it will improve the long-term capital returns for shareholders. The refinancing has also provided more flexibility in the company's borrowings by introducing an element of shorter term debt.

Net earnings and dividends

Earnings in the six months to 31 July 2019 have been strong at 16.1p per ordinary share (2018: 15.6p), an increase of 3.2% over the equivalent period in the previous year.

The board has declared a second quarterly dividend of 6.8p per ordinary share, payable on 12 November 2019 to shareholders on the register at close of business on 4 October 2019. A Dividend Reinvestment Plan (DRIP) is available for this dividend and the relevant Election Date is 18 October 2019 and the ex-dividend date is 3 October 2019.

Merchants Trust continues to be an AIC 'Dividend Hero', an elite group of investment trust companies that have increased their dividends each year for 20 years or more. The company's dividend has increased for 37 consecutive years and a high and growing yield remains a key objective of the company. The total distribution declared for the first half of 2019/20 is 13.5p, an increase of 4.7% on the same period last year (12.9p). The directors intend to at least maintain the quarterly dividend payments at 6.8p for the rest of the year, leading to a minimum annual dividend of 27.1p, an increase of 4.2%. The company's revenue reserves remain strong, and, as at 31 July 2019 were 28.8p per share (2018 – 26.9p).

Net asset value

As at 31 July 2019, the NAV per ordinary share (with debt at market value) was 493.2p. On a capital basis, the NAV per ordinary share (with debt at market value) increased by 4.6%, underperforming the benchmark return of 8.1%.

The total return reflects both the change in NAV per ordinary share and the ordinary dividends paid. For the six months to 31 July 2019, the total return NAV per ordinary share increased by 7.4%, whilst the FTSE All-Share Index increased by 10.6%.

Interim Management Report *(continued)*

Material events and transactions

At the company's annual general meeting (AGM), held in May, all resolutions put to shareholders were passed.

The third quarterly dividend of 6.5p per share was paid on 6 March 2019 to shareholders on the register on 1 February 2019. A final dividend of 6.6p per share was paid on 22 May 2019 to shareholders on the register on 22 April 2019. The total paid and declared for the year ended 31 January 2019 was 26.0p.

There were no related party transactions in the period.

Since the period end, the first quarterly dividend for the year ending 31 January 2020 of 6.7p per share was paid on 20 August 2019 to shareholders on the register on 12 July 2019.

Buybacks and share issuances

The board has a policy in place to (i) issue new shares when the company's ordinary shares are trading at a premium to NAV with debt at market value and (ii) buy back shares for holding in treasury to help dampen share price volatility when it is at a sustained discount to NAV. The renewal of this programme was approved by shareholders at the AGM in May this year. During the period under review the company has issued 1,300,000 new shares.

Gearing

The company has gearing in place which is deployed in the market for investment purposes. As mentioned above, this gearing was partially refinanced just after the end of the half-year period under review. Gearing amounted to £111 million, or 19.5% of net assets at 31 July 2019. Following the refinancing, gearing primarily comprises long term loan notes maturing in 2052, secured bonds maturing in 2029 and the recent revolving credit facility maturing in 2022.

Gearing had a positive effect of 1.8% on the Net Asset Value, but this was cancelled out by movements in the value of debt, as bond yields fell, and the cost of finance.

Outlook

Although markets have undoubtedly been stronger over the period than in the final months of 2018, the main issues that were prevalent then are still present now and our managers remain cognisant of the potential ramifications of global trade tensions, Brexit and US interest rate policy in particular. That said, as to be expected when following a value based investment philosophy, uncertainty will often reveal opportunities to invest in companies with sound business models and whose share prices have been caught in a wider sentimental downdraught.

It was noted in the annual report at the start of the year that the UK stock market does not solely reflect the UK economy and we believe that this should be borne in mind when looking forward. Brexit is less of a structural risk for the portfolio than might be expected, given a high exposure to multinational businesses and the benefit of the weakness of sterling on overseas earnings. The fundamentals of much of the UK stock market should remain largely unaffected by Brexit and a fair buffer of pessimism is already priced in. In the near term, our investment manager reports an ongoing polarisation of the UK market due to investors favouring "quality" and "growth" stocks. This is causing a significant distortion of market valuations, and creating opportunities for value investors. The managers expect this polarisation to reverse at some point, although the trigger for that reversal remains uncertain.

Our manager remains focused on uncovering individual stock opportunities with sound business models that should generate attractive long-term total returns for investors. A primary consideration within this selection process remains the overall delivery of a high and rising income as a mainstay of the trust's objective.

Colin Clark
Chairman
17 September 2019

Interim Management Report *(continued)*

Principal Risks and Uncertainties

The principal risks and uncertainties facing the company, together with the board's controls and mitigation, are broadly unchanged from those described in the annual report for the year ended 31 January 2019 under the headings below:

- Investment and Portfolio Risks
- Business and Strategy Risks
- Operational Risks

The board's approach to mitigating these risks and uncertainties is set out in the explanation with the Risk Map in the annual report. In the board's view these will remain the principal risks and uncertainties for the six months to 31 January 2020.

Responsibility Statements

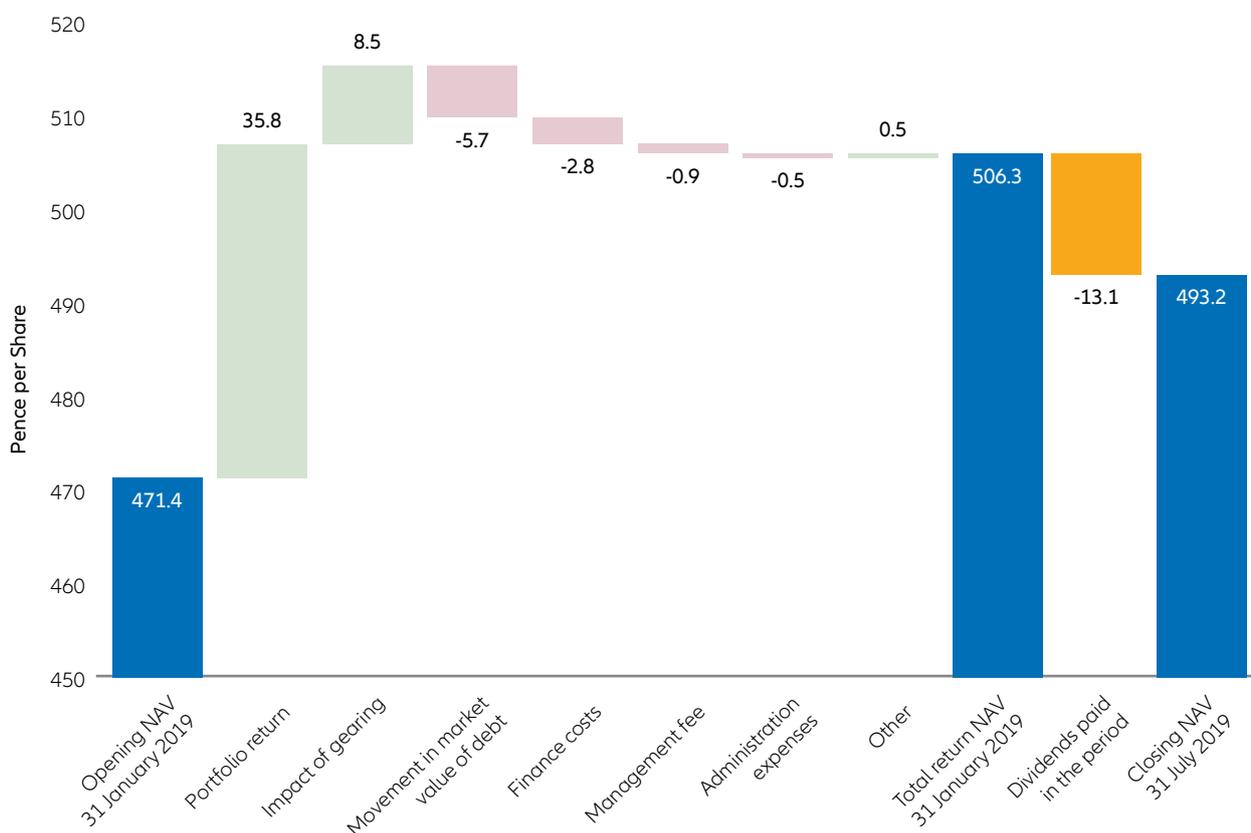
The directors confirm to the best of their knowledge that:

- The condensed set of financial statements contained within the half-yearly financial report has been prepared in accordance with FRS102 and FRS104, as set out in Note 2, the Accounting Standards Board's Statement 'Half-Yearly Financial Reports'; and
- The interim management report includes a fair review of the information required by Disclosure and Transparency Rule 4.2.7 R of important events that have occurred during the first six months of the financial year and their impact on the condensed set of financial statements, and a description of the principal risks and uncertainties for the remaining six months of the financial year; and
- The interim management report includes a fair review of the information concerning related parties transactions as required by the Disclosure and Transparency Rule 4.2.8 R.

Colin Clark
Chairman
17 September 2019

Attribution Analysis

Movement in Capital Return with Debt at Market Value for the six months ended 31 July 2019



The total return reflects both the change in net asset value, from 471.4p to 493.2p and the ordinary dividends paid in the period. The total return NAV of 506.3p as at 31 July 2019 is derived from the NAV with debt at market value of 493.2p plus dividends paid in the period of 13.1p.

Performance Attribution Analysis against FTSE All-Share Index

	Capital return %	Income return %	Total return %
Return of Index	8.1	2.5	10.6
Relative return from portfolio	-3.4	0.4	-3.0
Return of portfolio	4.7	2.9	7.6
Impact of gearing on portfolio	1.2	0.6	1.8
Movement in market value of debt	-1.2	-	-1.2
Finance costs	-0.4	-0.2	-0.6
Management fee	-0.1	-0.1	-0.2
Administration expenses	-	-0.1	-0.1
Other	0.4	-0.3	0.1
Change in net asset value per ordinary share (debt at market value)	4.6	2.8	7.4

Investment Manager's Review



Simon Gergel is Chief Investment Officer, UK Equities, Allianz Global Investors, based in London.

Economic & Market Background

The issues that dominated stock market sentiment at the start of the year; US/China trade tensions, Brexit and US interest rate policy, have remained key issues throughout the period. The US and China seem to be no closer to agreeing an end to their tariff war, with the US threatening further tariffs at the beginning of August. Brexit did not happen on 29th March. The new Prime Minister, Boris Johnson, has vowed to deliver Brexit on 31st October, with or without a deal with the EU, but parliamentary actions still make this event uncertain. However, US interest rate policy has arguably had the biggest impact on financial markets. Initial concerns that interest rate increases might slow the US (and world) economy, gradually gave way to an acceptance that US interest rates may need to come down in response to slowing economic growth and heightened trade tensions. The US Federal Reserve cut interest rates on the last day of July and the European Central Bank talked of further stimulus.

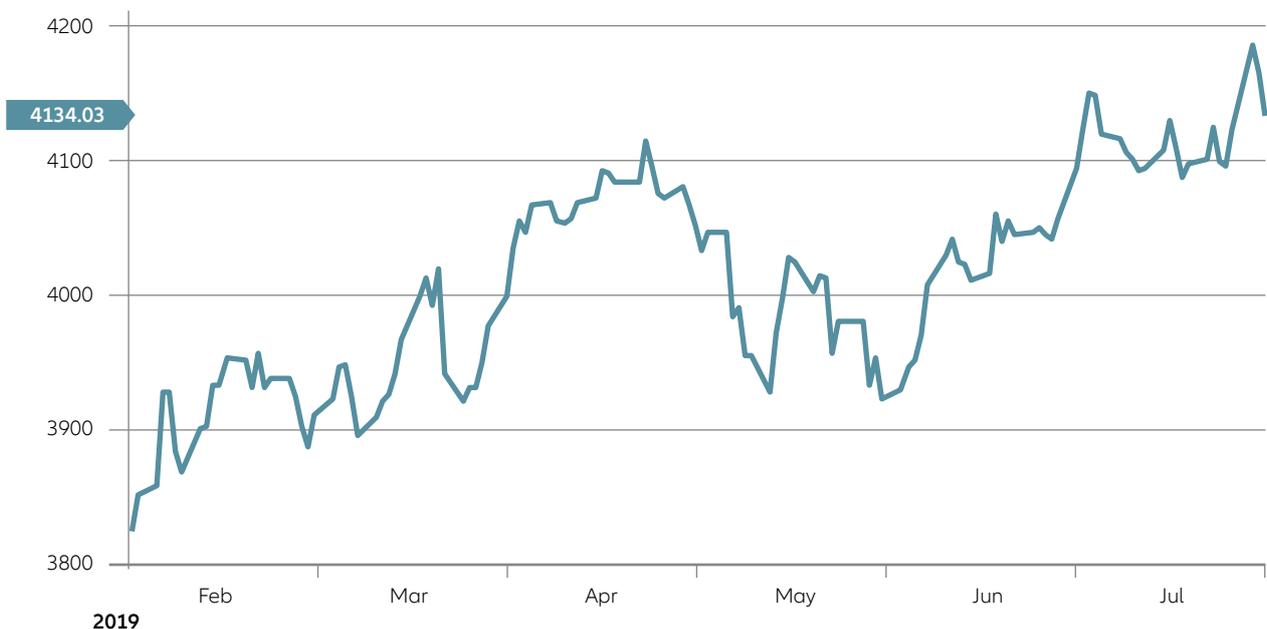
The decline in interest rate expectations drove financial asset prices upwards, as low interest rates force investors to take money out of bonds and cash to place into riskier assets, in order to

generate a decent return. In the USA, holders of government bonds can at least still make a positive return, whereas in Germany, by early August, investors in government bonds would have to pay the German government for the pleasure of lending them money, even out to 30 years.

This weight of money lifted most asset classes, and equities were no exception. The UK stock market, as represented by the FTSE All-Share Index gave a total return of 10.6%, with little volatility, recovering all of its losses in the last quarter of 2018. The pound was weak, especially later in the period on rising fears of a "no deal" Brexit. This bolstered the larger companies within the stock market, which tend to earn more money overseas. Large companies performed far better than medium and smaller sized companies.

We highlighted the polarisation of the stock market at the start of the year. This polarisation has become even more extreme. Share prices have been driven by two opposing forces. On the one hand, as discussed above, central bank policy and cheap money is forcing money into the stock market. On the other hand, investors

FTSE All-Share Index



FTSE All-Share 31.1.19 - 31.7.19. Source: AllianzGI/Datastream.

Investment Manager's Review *(continued)*

are nervous about the economic risks from trade wars and Brexit. This is leading to a strong polarisation in the market and investor preference for companies that are (not always justifiably) seen as relatively safe and defensive rather than cyclical, domestic and smaller companies. The outperformance of the "high quality" and "growth" companies is fuelling further investor money flows into investment styles that focus on these companies, and exacerbating this trend. Also, outflows from more value orientated strategies and inflows into passive investments, is further supporting the trend.

In this environment, the best performing larger sectors in the stock market included defensive sectors like personal goods, pharmaceuticals, healthcare and beverages, although financial services also performed well. The weakest large sectors included domestically exposed sectors like utilities and fixed line telecommunications which had difficult trading issues, and banks and real estate which are more cyclically exposed.

Investment Performance

It was a difficult period for our high yield and value oriented strategy. Although the portfolio produced a good absolute total return of 7.6%, this was some way behind the even stronger 10.6% return on the FTSE All-Share Index. There was a disconnect between trading results of the companies in the portfolio and the weak relative performance of the share prices, compared to the overall stock market. Whilst a few companies did experience trading difficulties, these instances were not unusual in either number or severity, and most companies performed satisfactorily or better. Furthermore, the level of income generation was healthy, which is important for underpinning future dividend payments.

The table shows the ten companies that had the biggest impact on relative performance, both positive and negative. Underperformance was driven by the themes above, with poor performance from a number of domestic and cyclical companies, and an impact from not

Contribution to Investment Performance relative to the FTSE All-Share Index

	Positive stocks	Performance impact %	Negative stocks	Performance impact %
Overweight (holding larger than index weight)	Inmarsat	0.5	Hammerson	-0.7
	Standard Life Aberdeen	0.4	Imperial Brands	-0.6
	Keller	0.3	IG Group	-0.4
	CRH	0.3	Balfour Beatty	-0.4
	Informa	0.2	Landsec	-0.4
	Man Group	0.2	Senior	-0.4
			Tyman	-0.3
Underweight (zero holding or weight lower than index weight)	Glencore	0.4	AstraZeneca	-0.7
	Lloyds Bank	0.3	Unilever	-0.3
	BT	0.3	Diageo	-0.3
	IAG	0.2		

Investment Manager's Review *(continued)*

owning certain defensive shares which rallied. However, there were positive drivers too, with the portfolio benefiting from takeover activity and a strong recovery in several stocks that had underperformed last year.

The biggest positive contributor was Inmarsat, the satellite communications company, which received a takeover offer. The fund management companies Standard Life Aberdeen and Man Group also performed well on the back of stronger financial markets and improving investment performance. Keller bounced back from last year's warning, on reassuring trading results, while CRH and Informa made solid trading progress. Relative performance also benefited from not owning Glencore, Lloyds, BT or British Airways parent – IAG - which were all weak shares and impacted the index return.

On the negative side, two real estate stocks, Hammerson and Landsec, underperformed amid investor nervousness about the outlook for the UK retail property sector in particular. Imperial Brands shares also weakened, despite relatively solid trading results and a 10% interim dividend increase, on investor concerns about future regulation and smoking

trends. IG Group, Senior and Tyman suffered from trading disappointments, posting modest share price declines against a rising stock market, whilst Balfour Beatty was impacted by investor sentiment against construction stocks, despite resilient trading results. There was also a significant impact from not owning AstraZeneca, Diageo and Unilever, which performed very well, as "quality growth" companies, even though they were highly valued at the start of the year.

Portfolio Changes

In a polarised stock market, we identified many opportunities to invest into companies where the share prices did not reflect our view of the intrinsic value of the businesses. These investments were financed by taking money out of other companies, typically where share prices had performed well, and shares were trading closer to fair value, but also in some situations where our view of the investment case had changed.

We added three new companies to the portfolio. All three were in the consumer sector and all three have significant exposure to emerging markets where we see superior long term

Life sciences, engineering and IT recruitment company SThree has seen profits treble in five years.



Investment Manager's Review *(continued)*

growth opportunities compared to developed markets. But that is where the similarities end as they are very different companies acting across different continents.

PZ Cussons is a leading manufacturer of soaps and beauty products, with brands such as Carex, Imperial Leather and St Tropez. The company is even older than The Merchants Trust, tracing its history back to 1884. The investment case rests on the long term attractions of a highly profitable UK and European consumer business, strong positions in growing emerging market countries, such as Nigeria and Indonesia, and a reasonable valuation. There is also considerable recovery potential as a third of group sales come from the African division, which is currently loss-making due to weak economic conditions in Nigeria, where PZ Cussons is a market leader.

Inchcape is a leading distributor and retailer in the luxury automotive sectors. Inchcape has long-standing relationships with car manufacturers and operates in over 30 markets, including an exclusive relationship with Toyota, to represent their brands in Hong Kong and Singapore. Inchcape's strategy is to broaden its distribution business further into emerging markets with more brands, consolidating a

fragmented global industry. The shares offered good value after a difficult period in the global car industry and did not reflect the improving quality of the business and its growth prospects.

The most recent addition to the portfolio was Stock Spirits, an Eastern European spirits company. It is market leader in the Czech Republic and number two in the much larger Polish market, with smaller operations in Italy and elsewhere. Primarily focused on vodka but with several other complementary brands and distribution arrangements, the company is benefiting from consumers trading up to premium spirits and it has been taking market share in the Polish market against weaker competitors. The shares were modestly valued, with strong cash generation and paying a good dividend yield.

Elsewhere, we added to existing positions in the tobacco sector, where sentiment was depressed and valuations were exceptionally low. Also, we increased holdings in specific opportunities in the media and aerospace & defence sectors. There were two switches on relative valuation grounds, adding to Royal Dutch Shell and Barclays, funded by reducing the BP and HSBC holdings.

New holding Inchcape has represented Toyota for over 45 years in the UK, Hong Kong and Singapore.



Investment Manager's Review *(continued)*

We sold three companies completely from the portfolio, Ashmore, Inmarsat and Marks & Spencer. Ashmore, the emerging market fund manager, has been a very strong performer over the last three years, benefiting from healthy asset flows as investor sentiment has improved towards emerging markets, and Ashmore's funds have outperformed. The shares had moved up to a high valuation, reflecting the attractive long-term growth prospects for the business, but leaving less upside potential, so we sold the position.

Inmarsat, the satellite communications company, received a takeover bid for the business from private equity bidders, backed by two Canadian pension funds. This was a good example of where the stock market was undervaluing the long term prospects of a market-leading business due to short-term trading issues. Whilst there could be further upside in the business in the long term, the bid was priced at a large premium to the preceding price and it was recommended unanimously by the board of directors, and so we decided to vote for the takeover bid and sold the holding.

Marks & Spencer was a case of us changing our view of the investment case. We had owned M&S as a long term restructuring situation, backed by healthy cash flow from a resilient and

differentiated food business. However, we sold out of the business when it became clear that the management had a different view of the food business, favouring an expansionary strategy, which could compromise the short-term cash generation of the group. Subsequently, M&S announced its intention to spend up to £750m on a joint venture with Ocado, funded by a £600m rights issue and by cutting the dividend.

As well as these complete sales, we took money out of several shares after strong performance had taken the prices closer to our assessment of fair value, notably BHP, Tate & Lyle, Informa, Greene King and Prudential.

Outlook

As explained above, the stock market is extremely polarised in the UK. Normally, active investors in the stock market arbitrage opportunities, selling highly valued companies to buy cheaper ones. This process keeps the market relatively efficient. However, this process is not working effectively at the moment. As we explained, investment flows are either going into passive strategies that buy the whole market or into "quality" and "growth" strategies which are largely valuation insensitive. Many years ago Benjamin Graham famously described the

Portfolio holding Greene King saw a recent takeover bid at a considerable premium to the prevailing share price.



Investment Manager's Review *(continued)*

stock market as a voting machine in the short term but a weighing machine in the long term. Currently investors voting with their money are overpowering the weighing process.

It is reminiscent of the technology, media and telecommunications (TMT) bubble at the end of the 1990s. In that period companies like Vodafone, BT, Dixons, and many others were seen as high growth businesses as they enabled consumers to access the emerging internet. These companies traded on extremely high valuations, whilst much of the rest of the stock market, known as "old economy" stocks languished with few buyers. As the word "bubble" implies, this period ended rather sharply. Inflated expectations could not be met by profits growth, and there was a huge rotation back towards better value companies in the early 2000s. Even a company like Amazon, which was one of the true winners and has grown into a phenomenal business, saw its share price sink by over 90% during the TMT crash. Many other TMT shares collapsed and, even if they survived, never recovered previous levels.

Perhaps the extremes today are not at the same level as in that period, but much of the market is partying like it's 1999. We are not going to chase the most fashionable companies if we cannot make a sensible valuation argument for investing in them. Especially as we can find many fundamentally sound businesses trading on really attractive valuations. To give just one example, we can look at SThree. This company is a leading provider of primarily contract employees in STEM markets, such as life sciences, engineering and IT, to large employers around the world. The company has just reported interim sales (net fees) of £163m, up 12% from a year ago, and operating profits of £25m up 21%, with 86% of its sales outside the challenging UK market. 5 years ago, in the same period in 2014, the company reported sales of £101m and operating profits of £8.4m. So sales are up 60% and profits have trebled in five years. The really remarkable thing is that the share price has fallen over that period, from 360p in July 2014 to 281p in July 2019! On consensus forecasts the shares* trade at just over 8x price to earnings, with a dividend yield of 5.6% and no debt on the balance sheet. Recruitment is a cyclical industry, so the valuation would be expected to come down late in the economic cycle. However, with substantial long-term growth opportunities and with most of its business overseas, this valuation looks far too low.

There are several potential triggers that could cause a reversal in the polarisation trend within the stock market. A resolution to trade and Brexit concerns could lead to a more optimistic economic outlook and raise consensus expectations for interest rates. This could quickly reverse sentiment and make investors more willing to look at less defensive, but much cheaper shares. We are also seeing rising interest in some depressed UK stocks from private equity or corporate buyers, who ironically seem to be taking a longer term view than many market participants. Indeed, we have seen a takeover bid for one of the portfolio holdings - Greene King - in August, at a considerable premium to the prevailing share price. If this trend gathers pace, it could also change sentiment. Ultimately, however, it is hard to call the timing on any change. History has shown over a long period of time that buying shares on low valuations tends to deliver outperformance and we believe that this will prove true in the future too. Having said that, careful analysis of business franchises, competitive forces, technological changes and environmental, social and governance risks remains critical to differentiate between cheap companies and "value traps": companies that appear cheap but for good reason.

We have constructed a portfolio of companies, like SThree, listed in the UK but with operations spread across many different industries, both in the UK and internationally. This provides the portfolio with a high level of diversification, whilst also being differentiated from the broad UK stock market. This also introduces an element of foreign currency exposure. Share valuations and income generation have benefited from the recent drop in the value of the pound. Whilst this could reverse, over time, it does provide some protection from domestic economic risks.

In conclusion, we believe that given the fundamental strengths of the businesses in the portfolio and their low valuations, the prospects for capital growth in the medium term are excellent. The portfolio pays a high yield and, in aggregate, is delivering a decent level of dividend growth, supporting Merchants' objective of paying a high and rising dividend yield.

* Source Bloomberg as at 8 August 2019

Simon Gergel
Allianz Global Investors

Investment Portfolio

as at 31 July 2019

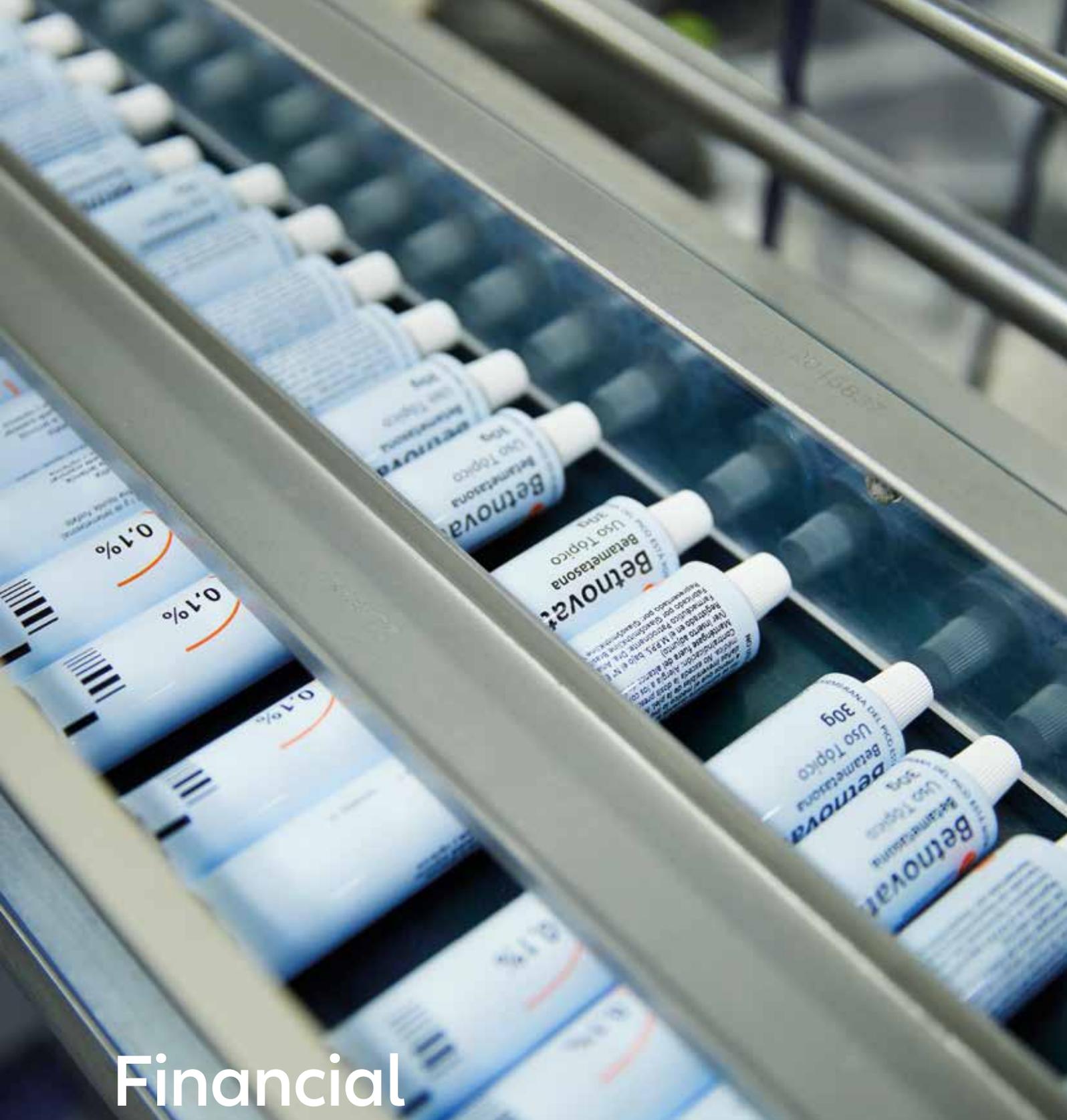
Twenty Largest Equity Holdings

Name	Value (£'000s)	% of Total Assets	Principal Activities
Royal Dutch Shell B	43,149	6.34	Oil & Gas Producers
GlaxoSmithKline	40,027	5.89	Pharmaceuticals & Biotechnology
Imperial Brands	29,540	4.33	Tobacco
HSBC Holdings	26,472	3.89	Banks
BAE Systems	25,912	3.81	Aerospace & Defence
British American Tobacco	23,604	3.47	Tobacco
Standard Life Aberdeen	21,368	3.14	Financial Services
Legal & General	20,813	3.06	Life Insurance
Barclays	18,944	2.79	Banks
CRH	18,051	2.65	Construction & Materials
Meggitt	17,987	2.64	Aerospace & Defence
BHP	17,697	2.60	Mining
St. James's Place	17,455	2.57	Life Insurance
BP	17,449	2.57	Oil & Gas Producers
Prudential	17,060	2.51	Life Insurance
SSE	16,995	2.50	Electricity
National Express Group	15,199	2.23	Travel & Leisure
Land Securities Group	15,174	2.23	Real Estate Investment Trusts
National Grid	15,151	2.23	Gas, Water & Multiutilities
WPP	14,071	2.07	Media
	432,118	63.52	% of Total Assets



Portfolio Analysis

Sector	% Held
Financials	27.29
Industrials	19.44
Consumer Goods	12.55
Consumer Services	11.09
Oil & Gas	8.91
Utilities	6.79
Health Care	5.88
Basic Materials	4.50
Net Current Assets	3.55



Financial Statements

Defensive sectors such as pharmaceuticals performed well over the period. GlaxoSmithKline remains a key holding.

Income Statement

	For the six months ended 31 July 2019			For the six months ended 31 July 2018		
	Revenue £'000s	Capital £'000s	Total Return £'000s (Note 1)	Revenue £'000s	Capital £'000s	Total Return £'000s (Note 1)
Gains on investments held at fair value through profit or loss	-	29,429	29,429	-	25,533	25,533
Income from investments	19,429	-	19,429	18,573	-	18,573
Other income	195	-	195	425	-	425
Investment management fee	(408)	(757)	(1,165)	(433)	(805)	(1,238)
Administrative expenses	(417)	(1)	(418)	(429)	(1)	(430)
Profit before finance costs and taxation	18,799	28,671	47,470	18,136	24,727	42,863
Finance costs: interest payable and similar charges	(1,164)	(2,122)	(3,286)	(1,168)	(2,130)	(3,298)
Profit on ordinary activities before taxation	17,635	26,549	44,184	16,968	22,597	39,565
Taxation	-	-	-	-	-	-
Profit after taxation attributable to ordinary shareholders	17,635	26,549	44,184	16,968	22,597	39,565
Earnings per ordinary share (basic and diluted) (Note 4)	16.13p	24.29p	40.42p	15.61p	20.78p	36.39p

Balance Sheet

	As at 31 July 2019 £'000s	As at 31 July 2018 £'000s	As at 31 January 2019 £'000s
Investments held at fair value through profit or loss	656,137	709,381	622,073
Net current assets	24,084	20,398	22,059
Total assets less current liabilities	680,221	729,779	644,132
Creditors: amounts falling due after more than one year	(110,077)	(110,327)	(110,205)
Total net assets	570,144	619,452	533,927
Called up share capital	27,507	27,182	27,182
Share premium account	39,699	33,718	33,718
Capital redemption reserve	293	293	293
Capital reserve	470,945	529,023	444,396
Revenue reserve	31,700	29,236	28,338
Equity shareholders' funds	570,144	619,452	533,927
Net asset value per ordinary share	518.2p	569.7p	491.1p

The net asset value is based on 110,028,464 ordinary shares at 31 July 2019.

The net asset value is based on 108,728,464 ordinary shares at 31 July 2018.

The net asset value is based on 108,728,464 ordinary shares at 31 January 2019.

Statement of Changes in Equity

	Called up Share Capital £'000s	Share Premium Account £'000s	Capital Redemption Reserve £'000s	Capital Reserve £'000s	Revenue Reserve £'000s	Total £'000s
Six months ended 31 July 2019						
Net assets at 1 February 2019	27,182	33,718	293	444,396	28,338	533,927
Revenue profit	-	-	-	-	17,635	17,635
Dividends on ordinary shares (Note 3)	-	-	-	-	(14,273)	(14,273)
Capital profit	-	-	-	26,549	-	26,549
Shares issued during the period	325	5,981	-	-	-	6,306
Net assets at 31 July 2019	27,507	39,699	293	470,945	31,700	570,144
Six months ended 31 July 2018						
Net assets at 1 February 2018	27,182	33,718	293	506,426	25,859	593,478
Revenue profit	-	-	-	-	16,968	16,968
Dividends on ordinary shares (Note 3)	-	-	-	-	(13,591)	(13,591)
Capital profit	-	-	-	22,597	-	22,597
Net assets at 31 July 2018	27,182	33,718	293	529,023	29,236	619,452

Cash Flow Statement

	Six months ended 31 July 2019 £'000s	Six months ended 31 July 2018 £'000s
Operating activities		
Profit before finance costs and taxation	47,470	42,863
Less: Gains on investments held at fair value	(29,429)	(25,533)
Purchase of fixed asset investments held at fair value through profit or loss	(81,967)	(124,680)
Sales of fixed asset investments held at fair value through profit or loss	79,035	128,031
Increase in other receivables	(1,600)	(2,010)
(Decrease) increase in other payables	(26)	733
Net cash inflow from operating activities	13,483	19,404
Financing activities		
Interest paid	(3,394)	(3,372)
Dividend paid on cumulative preference stock	(21)	(22)
Dividends paid on ordinary shares	(14,273)	(13,591)
Proceeds from issue of ordinary shares	6,306	-
Net cash outflow from financing activities	(11,382)	(16,985)
Increase in cash and cash equivalents	2,101	2,419
Cash and cash equivalents at the start of the period	22,952	20,096
Cash and cash equivalents at the end of the period	25,053	22,515
Composed of:		
Cash at bank	25,053	22,515

Notes

Note 1 – Financial Statements

The half-yearly financial report has been neither audited nor reviewed by the company's auditors. The financial information for the year ended 31 January 2019 has been extracted from the statutory financial statements for that year which have been delivered to the Registrar of Companies. The auditors' report on those financial statements was unqualified and did not contain a statement under section 498 of the Companies Act 2006.

The total return column of the Income Statement is the profit and loss account of the company.

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

Allianz Global Investors GmbH, UK Branch (AllianzGI), acts as Investment Manager to the company. Details of the services and fee arrangements are given in the latest annual report of the company, which is available on the company's website at www.merchantstrust.co.uk.

Note 2 – Accounting Policies

The Company presents its results and positions under 'The Financial Reporting Standard applicable in the UK and Republic of Ireland' (FRS 102), which forms part of revised Generally Accepted Accounting Practice ('New UK GAAP') issued by the Financial Reporting Council.

The condensed set of financial statements has been prepared on a going concern basis in accordance with FRS 102 and FRS 104, 'Interim Financial Reporting' and the Statement of Recommended Practice – 'Financial Statements of Investment Trust Companies and Venture Capital Trusts' (SORP). They have also been prepared on the assumption that approval as an investment trust will continue to be granted.

The interim financial statements and the net asset value per share figures have been prepared in accordance with FRS 102 using the same accounting policies as the preceding annual accounts.

Note 3 – Dividends on Ordinary Shares

Dividends paid on ordinary shares in respect of earnings for each period are as follows:

	Six months ended 31 July 2019 £'000s	Six months ended 31 July 2018 £'000s
Dividends on Ordinary Shares of 25p:		
Third quarterly dividend 6.5p paid 6 March 2019 (2018 - 6.2p)	7,067	6,741
Final dividend 6.6p paid 22 May 2019 (2018 - 6.3p)	7,206	6,850
	14,273	13,591

In accordance with FRS 102 section 32 'Events After the End of the Reporting Period', dividends payable at the period end have not been recognised as a liability. Details of these dividends are set out below.

	Six months ended 31 July 2019 £'000s	Six months ended 31 July 2018 £'000s
First quarterly dividend 6.7p paid 20 August 2019 (2018 - 6.4p)	7,372	6,959
Second quarterly dividend 6.8p payable 12 November 2019 (2018 - 6.5p)	7,482	7,067
	14,854	14,026

The final and quarterly dividends above are based on the number of shares in issue at the period end. However, the dividend payable will be based upon the number of shares in issue on the record date and will reflect any purchase or cancellation of shares by the company settled subsequent to the period end.

Notes *(continued)*

Note 4 – Earnings per Ordinary Share

The earnings per ordinary share is based on a weighted number of shares 109,323,492 (31 July 2018 - 108,728,464) ordinary shares in issue.

Note 5 – Fair Value Hierarchy

Investments and derivative financial instruments are designated as held at fair value through profit or loss in accordance with FRS 102 sections 11 and 12.

FRS 102 fair value hierarchy disclosures (March 2016) sets out three fair value levels.

Level 1: The unadjusted quoted price in an active market for identical assets or liabilities that the entity can access at the measurement date.

Level 2: Inputs other than quoted prices included within Level 1 that are observable (ie developed using market data) for the asset or liability, either directly or indirectly.

Level 3: Inputs are unobservable (ie for which market data is unavailable) for the asset or liability.

With the exception of those financial liabilities measured at amortised cost, all other financial assets and financial liabilities are either carried at their fair value or the balance sheet amount is a reasonable approximation of their fair value.

As at 31 July 2019, the financial assets at fair value through profit and loss of £656,050,000 (31 July 2018: £709,358,000; 31 January 2019: £622,063,000) are categorised as follows:

	Level 1 £'000s	Level 2 £'000s	Level 3 £'000s	Total £'000s
Financial assets at fair value through profit or loss at 31 July 2019				
Equity investments	656,133	-	-	656,133
Financial instruments	-	-	4	4
Derivatives financial instruments - written call options	-	(87)	-	(87)
	656,133	(87)	4	656,050

	Level 1 £'000s	Level 2 £'000s	Level 3 £'000s	Total £'000s
Financial assets at fair value through profit or loss at 31 July 2018				
Equity investments	709,353	-	-	709,353
Financial instruments	-	-	28	28
Derivative financial instruments - written call options	-	(23)	-	(23)
	709,353	(23)	28	709,358

	Level 1 £'000s	Level 2 £'000s	Level 3 £'000s	Total £'000s
Financial assets at fair value through profit or loss at 31 January 2019				
Equity investments	622,069	-	-	622,069
Financial instruments	-	-	4	4
Derivatives financial instruments - written call options	-	(10)	-	(10)
	622,069	(10)	4	622,063

Notes *(continued)*

For exchange listed equity investments the quoted price is either the bid price or the last traded price depending on the convention of the relevant exchange. For written options the value of the option is marked to market based on traded prices. Financial instruments valued using valuation techniques level 3 have, in the absence of relevant trading prices or market data, been valued based on the directors' best estimate.

Note 6 – Status of the Company

The company applied for and was accepted as an approved investment trust for accounting periods commencing on or after 1 February 2013, subject to it continuing to meet eligibility conditions at section 1158 Corporation Taxes Act 2010 and the on-going requirements for approved companies in Chapter 3 Part 2 Investment Trust (Approved Company) (Tax) Regulations 2011 (Statutory Instrument 2011/2999).

Note 7 – Transactions with the Investment Manager and related parties

As disclosed in the annual report, the existence of an independent board of directors demonstrates that the company is free to pursue its own financial and operating policies and therefore, under FRS 8: Related Party Disclosures, the investment manager is not considered to be a related party. The company's related parties are its directors.

There are no other identifiable related parties as at 31 July 2019, 31 July 2018 and 31 January 2019.

Investor Information

Directors

Colin Clark (Chairman)
Timon Drakesmith (Chairman – Audit Committee)
Mary Ann Sieghart
Sybella Stanley (Senior Independent Director)
Paul Yates

Managers

Allianz Global Investors GmbH, UK Branch
199 Bishopsgate, London, EC2M 3TY
Telephone: +44 (0)20 3246 7000
Represented by Simon Gergel

Secretary and Registered Office

Kirsten Salt BA (Hons) ACIS
199 Bishopsgate, London, EC2M 3TY
Telephone: +44 (0)20 3246 7513
Registered Number: 28276

Registrars

Link Asset Services
The Registry, 34 Beckenham Road, Beckenham,
Kent BR3 4TU.
Telephone: 0371 664 0300. Lines are open 9.00 a.m. to
5.30 p.m. (London time) Monday to Friday.
Email: enquiries@linkgroup.co.uk.
Website: www.linkassetservices.com

Financial Calendar

Half year announced in September
Half Yearly Financial Report posted to shareholders in
September
Full year announced in March
Annual report posted to shareholders in April
Annual general meeting held in May

Website

Further information about The Merchants Trust PLC,
including monthly fact sheets, daily share price and
performance, is available on the company's website:
www.merchantstrust.co.uk.

AIC Membership

The company is a member of the Association of
Investment Companies. Category: UK Equity Income.

Ordinary Dividends

1st quarterly	August
2nd quarterly	November
3rd quarterly	February/March
Final	May

How to invest

Shareholders can invest in Merchants by purchasing shares through an investment platform operated by a third party provider, a stockbroker or a financial adviser. Many online platforms allow share dealing in 'real time' and some offer an option to invest regularly each month as well as lump sum investing. Competition between platform providers is keen so charges are usually very competitive. More information is available from Allianz Global Investors either via Investor Services on 0800 389 4696 or see 'How to invest' on our website, www.merchantstrust.co.uk where there are links to a range of these platforms, many of which allow the holding of shares within an ISA, Junior ISA, SIPP and/or savings scheme.

Net Asset Value

The Net Asset Value of the ordinary shares is calculated daily and the top ten holdings are announced monthly. They are published through the London Stock Exchange Regulatory News Service. The company's share price is published in the Daily Telegraph and Financial Times. The net asset values and share prices are also available from Allianz Global Investors, via Investor Services on 0800 389 4696 or on the trust's website: www.merchantstrust.co.uk.

Shareholder Enquiries

In the event of queries regarding their holdings of shares, lost certificates, dividend payments, registered details, etc., shareholders should contact the registrars on 0371 664 0300. Lines are open 9.00 a.m. to 5.30 p.m. (London time) Monday to Friday. Calls to the helpline number from outside the UK are charged at applicable international rates. Different charges may apply to calls made from mobile telephones and calls may be recorded and monitored randomly for security and training purposes.

Changes of name and address must be notified to the registrars in writing. Any general enquiries about the company should be directed to the Company Secretary, The Merchants Trust PLC, 199 Bishopsgate, London EC2M 3TY. Telephone: 020 3246 7513.

Glossary of UK GAAP Performance Measures and Alternative Performance Measures

UK GAAP performance measures

Net Asset Value is the value of total assets less all liabilities. The Net Asset Value, or NAV, per ordinary share is calculated by dividing this amount by the total number of ordinary shares in issue. The debt in the company used in the calculation is measured at par value, that is, the net proceeds on issue plus accrued finance costs to date and, if issued at a premium, the amortised premium to date.

Earnings per ordinary share is the profit after taxation, divided by the weighted average number of shares in issue for the period.

Derivatives

The company operates a covered call overwriting strategy on a limited proportion of the portfolio to generate additional income. In “writing” or selling an option, Merchants gives the purchaser the right to buy a specific number of shares in a company at an agreed “strike” price within a fixed period. In exchange Merchants receives an option premium, which is taken to the revenue account. Merchants gets the full benefit of any move in the share price up to the strike price but not beyond. If the share price rises above the strike price, there is a potential “opportunity” (but not cash) cost, as the option holder can exercise their option to buy the shares at the strike price.

Merchants’ selective approach to option writing is driven by the investment fundamentals on each stock we hold, rather than by a separate derivatives rationale. We write calls on portions of shareholdings that we are happy to sell at the strike price, provided that the premium income received is sufficiently attractive. The options written are typically short dated with most less than four months duration. The total exposure is closely monitored and is limited to 15% of the portfolio value with all option positions “covered” by shares owned. From a holistic view, it can be argued that the overall strategy slightly reduces the Trust’s gearing to the equity market, neutralising a small part of the financial leverage. It tends to be more profitable in sideways or downwards markets but less profitable in rising markets.

Alternative Performance Measures (APMs)

Net Asset Value, debt at market value, is the value of total assets less all liabilities, with the company’s debt measured at the market value at the time of calculation. The Net Asset Value, or NAV, per ordinary share with debt at market value is calculated by dividing this amount by the total number of ordinary shares in issue.

Net Asset Value per ordinary share, total return represents the theoretical return on NAV per ordinary share, assuming that dividends paid to shareholders were reinvested at the NAV per ordinary share at the close of business on the day the shares were quoted ex dividend.

Share Price Total Return represents the theoretical return to a shareholder, on a closing market price basis, assuming that all dividends received were reinvested, without transaction costs, into the ordinary shares of the company at the close of business on the day the shares were quoted ex dividend.

Benchmark Total Return is the return on the benchmark, on a closing market price basis, assuming that all dividends received were reinvested into the shares of the underlying companies at the time their shares were quoted ex dividend.

Discount/premium is the amount by which the stock market price per ordinary share is lower than the Net Asset Value, or NAV, with either debt at par or debt at market value, per ordinary share. The discount is normally expressed as a percentage of the NAV per ordinary share. The opposite of a discount is a premium.

Ongoing Charges are operating expenses incurred in the running of the company, whether charged to revenue or capital, but excluding financing costs. These are expressed as a percentage of the average net asset value during the period and this is calculated in accordance with guidance issued by the Association of Investment Companies.

Yield represents dividends declared in the past year as a percentage of share price. This is shown as 5.4% at 31 July 2019 in the highlights on page 2.

The Merchants Trust PLC

199 Bishopsgate
London
EC2M 3TY

+44 (0)203 246 7000

www.merchantstrust.co.uk