

Investment Rationale

Investing in large UK companies, The Merchants Trust PLC aims to provide an above average level of income which increases over time. The Trust is managed by Simon Gergel, a Director at RCM with 23 years' investment experience.

Aim

The Trust's objective is to provide an above average level of income, income growth and long-term growth of capital through a policy of investing mainly in higher yielding UK FTSE 100 companies.

Fund Manager's Review

Simon Gergel



In March, the Directors declared an increased final dividend for the year ending 31st January 2012, representing the 30th year of dividend growth for The Merchants Trust. This record has been achieved during a period, over the last few years, which has included the most significant dividend cuts in the UK market for a generation. As portfolio income has recovered, the drawdown of reserves to help fund the dividend has been significantly lower than in the previous two years. The Trust retains about half a year's dividend in revenue reserves. Further details are available in the Annual Report on our website.

The Merchants Trust portfolio comprises predominantly high yielding, large capitalisation UK equities to match the objectives of delivering a high and rising level of income, together with capital growth. The structure of the portfolio has been defensively positioned for some time, with limited positions in cyclical natural resources and industrial businesses but with a higher exposure to less economically sensitive sectors such as food producers, telecommunications and utilities. This reflects both a cautious view about the prospects for economic growth in much of the developed world as well as the fundamental merits and valuation attractions of the companies we have selected.

The stock market traded within a tight range during the month after rising sharply in the previous five months. Some of the recent enthusiasm about an economic recovery in the USA and liquidity injections in the Eurozone began to wane. Concerns mounted about the effects of the high oil price, the continuing challenges of austerity in Europe and the growth outlook in China. Over the month the FTSE 100 posted a total return of -1.3%.

The Trust's NAV performance (0.11% total return) was ahead of the FTSE 100 Index. Strong gains in Cobham, United Business Media and DMGT boosted performance as well as having limited exposure to a very weak mining sector. There were few significant negative contributors although Mothercare and BAE Systems were weak and we did not own Prudential which rallied.

We added one new company to the portfolio, Smiths Group. Smiths is a conglomerate which manufactures mechanical seals for the oil & gas industry, consumable medical products, detection scanners for airports and border security and other industrial products. The business offers a combination of growth and recovery opportunities across its markets and trades at an attractive valuation following some trading disappointments, particularly in the detection operations. Elsewhere, we took profits on Bunzl and BT after a period of strong performance had reduced the future upside potential.

Our economic outlook remains relatively cautious as the high debt burden in the Western world is likely to keep economic growth below the long term trend for a considerable period. We maintain a relatively defensive portfolio bias. However we are finding selective opportunities, like Smiths Group and BBA Aviation, to buy fundamentally strong businesses with some economic sensitivity which trade on attractive valuations and offer future growth potential.

Performance (%)



Cumulative Performance (%)

	3 Months	6 Months	1 Year	3 Years	5 Years
Share Price	5.8	7.1	-1.4	96.8	-2.9
NAV	6.0	16.3	3.5	91.8	-3.7
FTSE 100	4.6	14.5	1.2	63.6	10.2

Discrete Performance (%)

From	30.03.07	31.03.08	31.03.09	31.03.10	31.03.11
To	31.03.08	31.03.09	31.03.10	31.03.11	30.03.12
Share Price	-18.7	-39.3	64.3	21.5	-1.4
NAV	-15.4	-40.7	67.5	10.7	3.5
FTSE 100	-6.3	-28.2	50.4	7.4	1.2

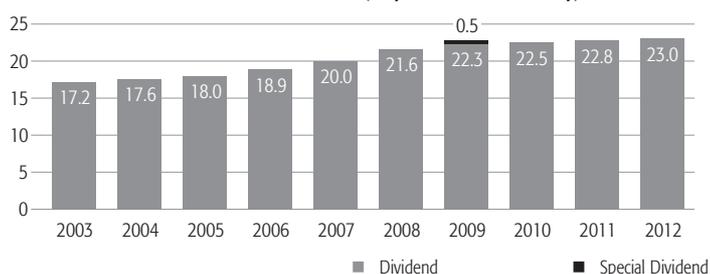
Source: Lipper, share price calculation percentage growth, mid to mid, total return to 31.03.12.

Benchmark: FTSE 100 Index

Past performance is not a reliable indicator of future performance. You should not make any assumptions on the future on the basis of performance information. The value of an investment and the income from it can fall as well as rise as a result of market fluctuations and you may not get back the amount originally invested. This investment trust charges 65% of its annual management fee to the capital account and 35% to revenue. This could lead to a higher level of income but capital growth will be constrained as a result. Your capital could also decrease if income paid out of capital exceeds the growth rate of the trust.

Dividend History

Ten Year Net Dividend Record in Pence (to year end 31 January)



Net Dividends Paid (year ending 31 Jan 2012)

	Pay Date	XD Date	Payment
1st quarterly dividend	17.08.11	15.07.11	5.7p per share
2nd quarterly dividend	11.11.11	7.10.11	5.7p per share
3rd quarterly dividend	23.02.12	27.01.12	5.8p per share
Final dividend	14.05.12	13.04.12.	5.8p per share



All data source RCM (UK) Limited as at 31.03.12 unless otherwise stated.

Capital Structure

Total Assets:	£542.3m
Gearing (net):	24.2%
Shares in Issue:	103,213,464 (Ordinary 25p)
Share Price ¹ :	376.5p
Net Asset Value ² :	406.6p (373.2p – debt at market value)
Premium/-Discount to NAV ³ :	-7.4% (0.9% – debt at market value)
NAV Frequency	Daily
Dividend Yield ² :	6.04%

1. Source: Lipper as at 31.03.12, market close mid price.

2. Source: Datastream as at 31.03.12. Calculated using the latest full year dividend divided by the current share price.

3. A trust's net asset value (NAV) is calculated as available shareholders' funds divided by the number of shares in issue, with shareholders' funds taken to be the net value of all the company's assets after deducting liabilities. In line with current industry best practice NAVs are now shown to take into account the 'fair value' of debt. This means NAVs are calculated after allowing for the valuation of debt at fair value or current market price, rather than at final repayment value. NAVs with debt at market value provide a more realistic impact of the cost of debt, and thus a more realistic discount. It is the capital NAV that is shown, which excludes any income.

Key Information

Launch Date:	16 February 1889
AIC Sector:	UK Growth and Income
Benchmark:	FTSE 100 Index
Annual Management Charge:	0.35%
Performance Fee:	No
Total Expense Ratio: ⁴	0.46%
Year end:	31 January
Annual Financial Report:	Final posted in April, Half-yearly posted in September
AGM:	May
Dividends:	February, May, August, November
Price Information:	Financial Times, The Daily Telegraph, www.rcm.com/investmenttrusts

Board of Directors:
Simon Fraser (Chairman), Mike McKeon (Chairman of the Audit Committee),
Henry Staunton (Senior Independent Director), Paul Yates

Company Secretary	Kirsten Salt
Investment Manager	Simon Gergel, Director, UK Equity
Codes:	RIC: MRCH SEDOL: 0580007 ISIN: GB0005800072

4. Source: Annual Financial Report

Risks & Features

Investment trusts are quoted companies listed on the London Stock Exchange. Their share prices are determined by factors including the balance of supply and demand in the market, which means that the shares may trade below (at a discount to) or above (at a premium to) the underlying net asset value.

Merchants seeks to enhance returns for its shareholders through gearing, in the form of long-term, fixed rate debentures. Gearing can boost the Trust's returns when investments perform well, though losses can be magnified when investments lose value. You should be aware that this Trust may be subject to sudden and large falls in value and you could suffer substantial capital loss. Derivatives are used to manage the trust efficiently.

Portfolio Analysis

Top Ten Holdings	(%)	(%)	
GlaxoSmithKline	7.4	British American Tobacco	3.7
Royal Dutch Shell "B" Shares	7.2	Scottish & Southern Energy	3.5
BP	6.7	BAE Systems	3.4
HSBC	6.5	Reed Elsevier	3.2
Vodafone	5.5	Unilever	3.1
Total Number of Holdings		61	

Sector Breakdown	(%)
Financials	17.4
Consumer Services	15.0
Oil & Gas	14.0
Consumer Goods	13.3
Industrials	11.4
Utilities	9.2
Telecommunications	8.9
Health Care	7.4
Cash	1.8
Basic Materials	1.6

HOW TO INVEST?

The Trust is a UK public limited company traded openly on the stock market. You can purchase shares through a stock broker. Shares in the Trust can be held within an ISA and/or savings scheme and a number of providers offer this facility. A list of suppliers is available on our website or from the AIC at www.theaic.co.uk

CONTACT US

To download the Annual Financial Report, Trust brochure or watch an interview with the fund manager, please visit us online at www.rcm.com/investmenttrusts



If you have any queries regarding our investment trusts our Investor Services team can be contacted on:

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All data source RCM (UK) Limited as at 31.03.12 unless otherwise stated.

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