

# THE MERCANTILE INVESTMENT TRUST PLC

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Annual Report & Accounts for the year ended 31st January 2017

Discovering Tomorrow's  
Market Leaders



**J.P.Morgan**  
Asset Management

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# Features

## Objective

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

## Investment Policy

- To emphasise capital 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 10% net cash to 20% geared.
- To invest no more than 15% of gross assets in other listed closed-ended investment funds (including investment trusts).

## Benchmark

The FTSE All-Share Index, excluding constituents of the FTSE 100 Index and investment trusts, with net dividends reinvested.

## Capital Structure

At 31st January 2017 the Company's share capital comprised 94,449,218 ordinary shares of 25p each, including 7,468,799 shares held in Treasury.

At 31st January 2017, the Company also had in issue a £3.85 million 4.25% perpetual debenture and a £175 million 6.125% debenture repayable on 25th February 2030.

## Management Company and Company Secretary

The Company employs JPMorgan Funds Limited ('JPMF' or the 'Manager') as its Alternative Investment Fund Manager and Company Secretary. JPMF is approved by the Financial Conduct Authority and delegates the management of the Company's portfolio to JPMorgan Asset Management ('JPMAM').

## FCA regulation of 'non-mainstream pooled investments'

The Company currently conducts its affairs so that the shares issued by the Company can be recommended by independent financial advisers to ordinary retail investors in accordance with the FCA's rules in relation to non-mainstream investment products and intends to do so for the foreseeable future.

The shares are excluded from the FCA's restrictions which apply to non-mainstream investment products because they are shares in an investment trust.

## AIC

The Company is a member of the Association of Investment Companies.

## Website

The Company's website, which can be found at [www.mercantileit.co.uk](http://www.mercantileit.co.uk), includes useful information on the Company, such as daily prices, factsheets and current and historic half year and annual reports.

THIS DOCUMENT IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION. If you are in any doubt as to the action you should take, you are recommended to seek your own independent financial advice from your stockbroker, bank manager, solicitor, accountant or other independent financial adviser authorised under the Financial Services and Markets Act 2000 if you are in the United Kingdom or, if not, from another appropriately authorised financial adviser. If you have sold or otherwise transferred all your ordinary shares in The Mercantile Investment Trust plc, please forward this document together with the accompanying documents immediately to the purchaser or transferee, or to the stockbroker, bank or agent through whom the sale or transfer was effected for onward transmission to the purchaser or transferee.

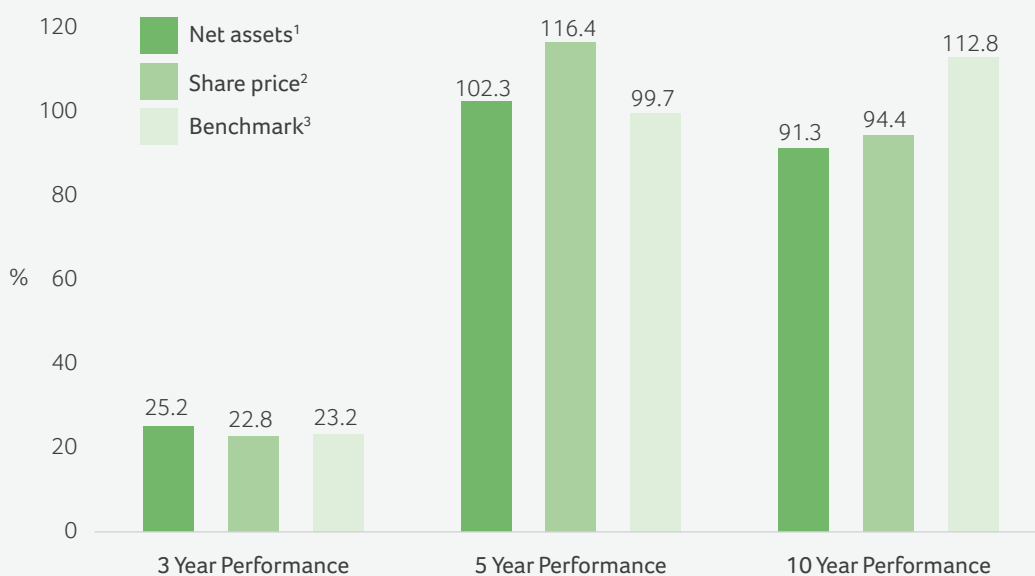
# Financial Highlights

Total returns (includes dividends reinvested)



## Long Term Performance

for periods ended 31st January 2017



A glossary of terms and definitions is provided on page 69.

<sup>1</sup>Source: J.P. Morgan/Morningstar, using net asset value per share, cum income, with debt at par value. 10 year performance is based on capital only NAVs, due to a lack of historic cum income NAVs.

<sup>2</sup>Source: Morningstar.

<sup>3</sup>Source: FTSE Russell. The Company's benchmark is the FTSE All-Share Index, excluding constituents of the FTSE 100 Index and investment trusts, with net dividends reinvested.

# Strategic Report

## Chairman's Statement

### Performance

Over the year to 31st January 2017, your Company returned 6.1% (cum income, debt at par) against 12.5% for the benchmark. Share price total return was 4.3%. As mentioned in the Half Year Report, your Company underperformed in the first half of the current financial year by being positioned wrongly for the outcome of the EU referendum. In the second half of the year your Company outperformed its benchmark, both in performance and share price total return, but that did not compensate for the loss incurred by the incorrect positioning of the portfolio for the EU referendum in June.

### Returns and Dividends

Earnings per share increased from 51.5p to 53.2p, compared with the year ended 31st January 2016. Your Company has paid three interim dividends of 10.25p per ordinary share over the year under review and the Board has declared a fourth quarterly interim dividend of 15.25p, giving a total dividend of 46.0p per share for the year, a 7.0% increase on last year's total dividend of 43.0p per share.

The Board intends to declare the first three interim dividends for the current year ending 31st January 2018 at 10.5p per ordinary share. The level of the fourth interim dividend will be determined by the Board following the end of the financial year and will depend on the level of dividends received and anticipated by the Company. The Board recognises the importance to shareholders of a smooth flow of dividends and also of maintaining a strong revenue reserve. At the year end, taking account of the payment of the fourth interim dividend, the revenue reserve stood at £36.7 million, which is the equivalent to 42.2p per share.

### Discount and Share Buybacks

Over the year under review, the discount widened from 10.6% to 12.5% on the basis of a cum income net asset value calculation, with debt valued at par. Using a cum income valuation with debt at fair value, the discount has widened from 7.4% to 8.6%. I would urge you to refer to page 20 where there is an explanation of the calculation methodologies.

During the year a total of 8,976,621 shares were repurchased, amounting to 9.4% of the issued share capital at the beginning of the year, at a total cost of approximately £150 million. Of those, 1,507,822 shares were cancelled and the balance held in Treasury. Share buy backs during the year under review have added approximately 16.13p to the net asset value per share.

The Board intends to continue to use the share repurchase authority to enhance value, to manage imbalances between the supply and demand of the Company's shares and so reduce the volatility of the discount. The Board believes that, to date, this mechanism has been helpful and therefore proposes and recommends that the powers to repurchase up to 14.99% of the Company's shares, to be cancelled or held in Treasury, be renewed for a further period.

# Strategic Report – continued

## Gearing

Your Company ended the year with gearing of 2.5%. During the year gearing varied between 8.3% net cash and 2.5% geared (using month end data). It is the Board's intention to continue to operate within the range of 10% net cash to 20% geared, under normal market conditions. Gearing is regularly discussed between the Board and the Investment Managers. The Company has long term debenture gearing, details of which are set out on the Features page.

## Board

All Directors other than myself will stand for annual reappointment, in line with the Company's policy. See the Directors' biographies on pages 23 and 24 for further details.

As announced in last year's Annual Report, I will retire from the Board at the conclusion of the AGM and Angus Gordon Lennox will succeed me as Chairman. Angus Gordon Lennox has very considerable experience in financial services and particularly in the investment trust sector and I am delighted that the Board has chosen him to succeed me as Chairman.

The Board undertakes a formal and rigorous annual evaluation of its performance, and that of its committees, the individual Directors and myself as the Chairman. Further details of this are given in the Corporate Governance Statement.

## Board Apprentice

In 2016 the Board decided once again to participate in the initiative launched by Board Apprentice Limited, a not-for-profit company with the objective of promoting diversity. Our current Board Apprentice, Anjola Adeniyi, is not paid, although the Company does reimburse reasonable expenses.

## Investment Managers

The Company's investment management team, which continues to be led by Guy Anderson, had a very good year to 31st January 2016. Last year it was positioned incorrectly for the outcome of the EU referendum. The Board continues to monitor the performance of the Manager on a regular basis.

## Management Fee Change

During the year the Board was very pleased to reach agreement with JPMorgan on a reduction in the management fee. With effect from 1st February 2017 the fee has been reduced from 0.5% of the Company's market capitalisation to 0.475% and it will further reduce to 0.45% with effect from 1st February 2018. This agreement recognises the changing conditions within the fund management industry and it ensures that the Company's shareholders benefit from an ongoing charges ratio that remains amongst the most competitive in the investment trust market.

## Changes to the Company's Articles of Association

The Board is recommending to shareholders that the Company adopt new Articles of Association to update the investment restriction provisions (which are set out in the Investment Restrictions and Guidelines in any event). Although the total fees paid to Directors will fall by £36,000 this year following the retirement of the Chairman, the Board is also proposing an increase in the maximum aggregate annual limit on Directors' fees from £300,000 to £400,000. This will provide scope for future recruitment and fee increases. Further, there are some minor revisions which accommodate changes to the Alternative Investment Fund Managers Directive ('AIFMD') and to international tax regimes. Please refer to the Appendix to the Notice of AGM.

# Strategic Report – continued

## Annual General Meeting

Your Company's one hundred and thirty first AGM will be held at Trinity House, Tower Hill, London EC3N 4DH on Wednesday 24th May 2017 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. 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 JPMorgan. I look forward to seeing as many of you as possible at the meeting.

## Outlook

We entered 2017 with a positive macroeconomic backdrop. Industrial lead indicators suggest that global economic growth is accelerating and this growth appears to be broadly based by region and industry.

However, economic growth will not be without its challenges. The fall in the value of sterling, combined with an increase in global commodity prices, will lead to imported inflation in the UK this year. This inflation will need to be absorbed either by the margins of businesses, through higher prices for consumers, or both. With time this may also result in a rising interest rate environment from which there will be a number of winners and losers.

To date the effects of the EU referendum have had a limited impact on company results. The fall in the value of sterling has been a net beneficiary to some businesses with UK operations but internationally diverse revenues. Your Board and our Investment Managers remain positive that the UK market is positioned to perform strongly in the long term and that attractively valued medium and small sized companies are well placed to continue to perform well.

**Hamish Leslie Melville**  
Chairman

6th April 2017

For further information, please contact:  
Juliet Dearlove  
For and on behalf of  
JPMorgan Funds Limited – Secretary  
020 7742 4000

# Strategic Report – continued

## Investment Managers' Report

### Contributions to total returns in the year ended 31st January 2017

	%
Benchmark total return	12.5
Stock/Sector – selection/allocation	-4.7
Cost of Gearing/Cash effect	-1.4
Effect of Management fee/Other expenses	-0.5
Cost of debentures	-0.6
Repurchase of shares	0.8
Return on net assets	6.1
Effect of increase in discount	-1.8
Return to shareholders	4.3

Source: JPMAM and Morningstar.

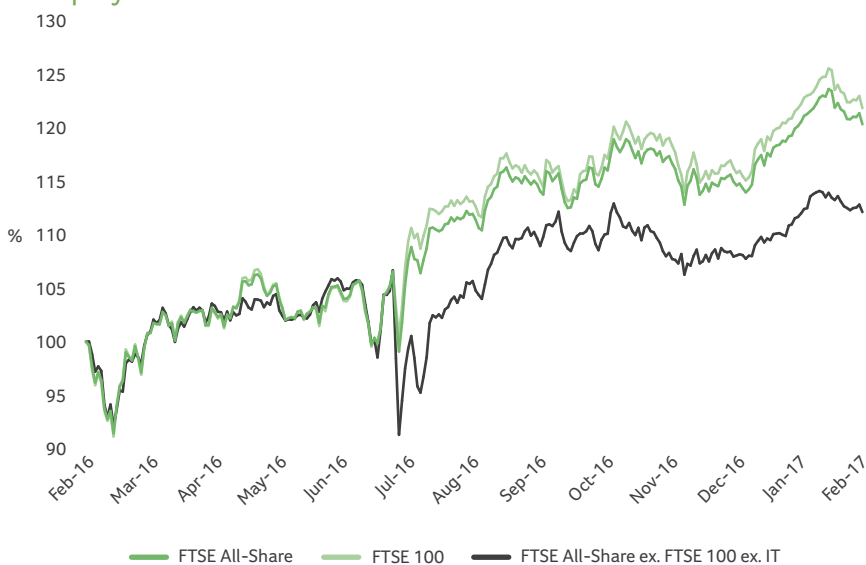
The table provides a breakdown, relative to the benchmark, of the contributions to total return.

A glossary of terms and definitions is provided on page 69.

### Market background: a year of change

The UK equity market delivered a resilient performance last year, with the FTSE All-Share generating a total return of 20.1% for the twelve months ended 31st January 2017. However, as can be seen in the graph below, the trajectory was far from smooth. Having recovered from the start of year sell-off that was driven primarily by concerns over the pace of Chinese economic growth, the market generated minor gains up until June when the focus turned to the EU referendum. Following the vote to leave the EU there was an immediate and sharp sell-off. This was then recouped through July following a swift political transition to Theresa May as Prime Minister and the actions of the Bank of England to reduce interest rates and introduce a further round of quantitative easing. The market then entered somewhat of a holding pattern through the third quarter, before regaining momentum in the final quarter, as the UK economy proved itself to be more resilient than had been expected and as international growth showed signs of acceleration.

### UK Equity Market Total Return



Source: J.P. Morgan Asset Management, Bloomberg.

However, underlying this aggregate view there was a notable difference between the different components of the market, with the FTSE 100 returning 21.5% compared to 12.5% for those companies outside of the FTSE 100, as represented by the FTSE All-Share Index excluding FTSE 100 constituents and investment trusts (the 'Benchmark'). This divergence was particularly notable in the week that followed the EU referendum as the more internationally focused FTSE 100, buoyed by the depreciation of sterling, outperformed the more domestically oriented Benchmark by nearly ten percentage points. The chart on page 7 illustrates the geographic mix of the FTSE 100 and the FTSE 250, showing just how stark the differences are in end market exposures.



# Strategic Report – continued

## Geographic Revenue Exposure (FTSE 100, FTSE 250)

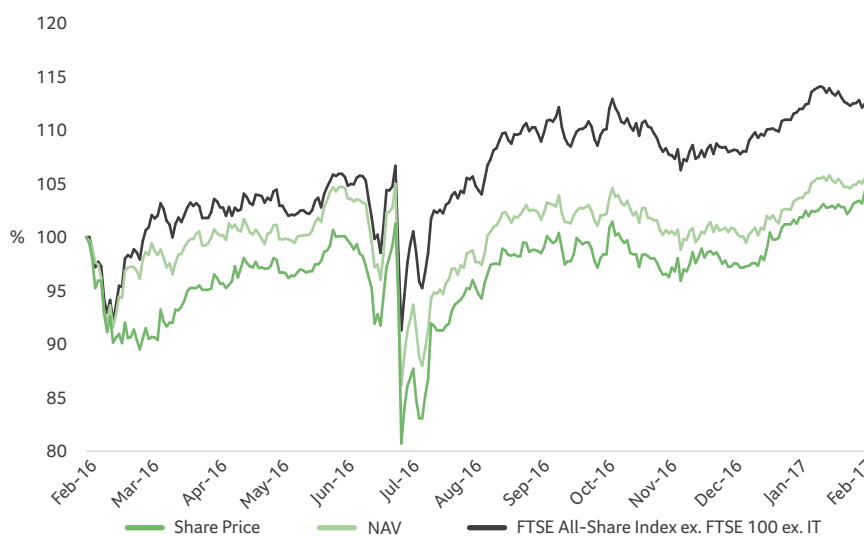


Source: J.P. Morgan Asset Management, Bloomberg data, Company data; data as of 31st January 2017.

## Mercantile performance: a challenging year

Following a strong performance in the previous year, your Company had a more difficult twelve months; the return on net assets was 6.1%, behind the 12.5% return from the Benchmark. The share price total return was 4.3%, reflecting the widening of the discount experienced early in the year that did not fully reverse. Pleasingly however, this was another robust year for income in the portfolio, which has supported the 7.0% increase in dividend payable as announced.

## Mercantile Performance



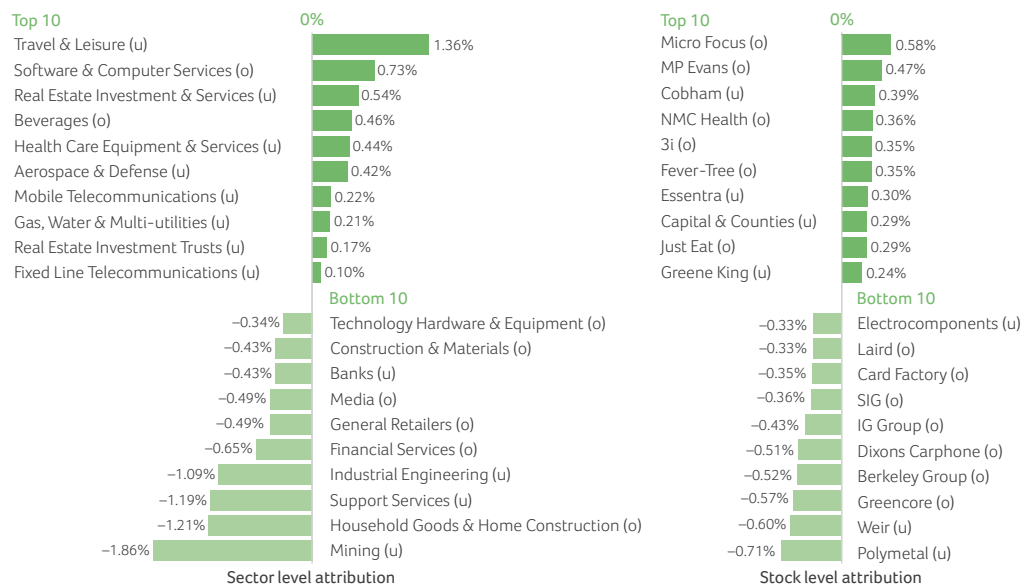
Source: J.P. Morgan Asset Management, Bloomberg data.

Our negative relative performance was driven by stock selection as well as the conservative level of market exposure, where holding a net cash position proved to be a drag on returns in what was ultimately a positive market environment. While this latter component is of course disappointing, we believe that through periods of heightened risk the preservation of capital does merit a greater focus. The chart overleaf shows the relative contributions to performance for the best and worst ten sectors and stocks within the portfolio.

# Strategic Report – continued

## Mercantile Performance Attribution Relative to Benchmark (Sector and Stock level)<sup>1</sup>

Year to 31st January 2017



<sup>1</sup>o = overweight

u = underweight

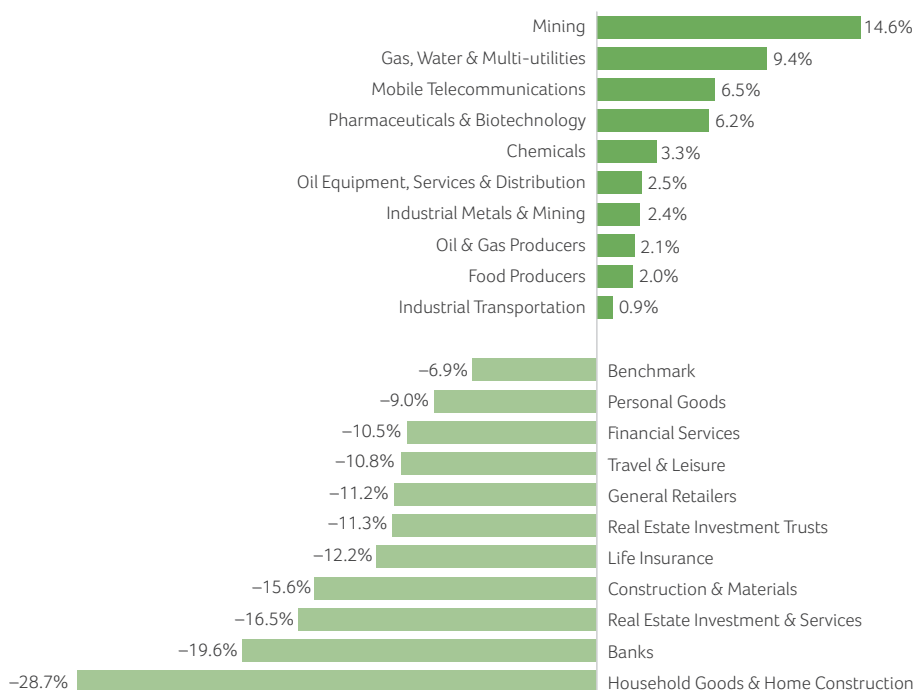
Source: J.P. Morgan Asset Management, B-One.

While there are of course a myriad of performance drivers, last year there were two significant negative factors that had the greatest impact on relative performance. The first and lesser of those was Mining, which at a sector level was the largest detractor. The portfolio had benefitted from not holding any miners in the previous year as the sector was under tremendous pressure due to industry over-capacity and the subsequent weakness of commodity prices. However, 2016 marked a turning point with commodity prices recovering and the stocks that benefit from this more than doubling in aggregate over the course of the year, and thus driving relative underperformance. In our outlook piece last year we highlighted that it would be hard to judge the exact timing of our move into this sector, but it is nevertheless disappointing to have been slow in this regard.

The second and more significant driver of performance was an event rather than a single stock or sector: the portfolio suffered significant negative relative performance in the week that followed the outcome of the referendum on EU membership. As is illustrated in the chart on page 9, in the immediate aftermath of the referendum share price performance at a stock and sector level diverged sharply. This was due to a combination of the different currency exposures of those companies and the increase in perceived risks for the domestic economy. In broad terms this led to outperformance of international and defensive earners and the underperformance of domestic and cyclical earners. As the portfolio was overweight domestic consumer and underweight international, this led to significant underperformance through that week. Pleasingly, performance has improved since July and the portfolio outperformed the Benchmark in the second half of the year.

# Strategic Report – continued

Benchmark Sector Level  
Performance 24th-  
30th June 2016  
(Top 10/Bottom 10)

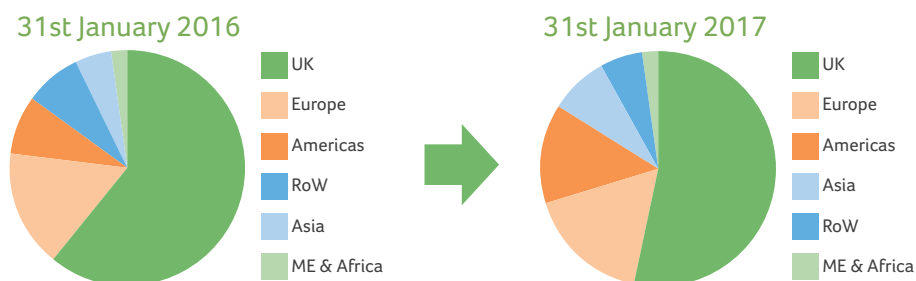


Source: J.P. Morgan Asset Management, B-One.

## Portfolio positioning and the year ahead – where are the opportunities?

While our investment approach is primarily focused on company specific analysis and stock selection, we remain aware of the broader macro-economic conditions and trends that may influence the relative attractiveness of different industries over time and this year was a year of adjustment in that regard. The most material changes to the portfolio positioning occurred after the EU referendum and reflected two factors: on the one hand the increased level of uncertainty over the outlook for the UK economy and therefore domestic consumption, and on the other hand the potentially improving outlook for industrial markets, most of which are more international in nature. Reflecting these two factors, and as is shown in the charts below, the portfolio has increased its exposure to more internationally facing and industrial companies at the expense of more domestically facing and consumer exposed companies. For example, we made new investments in Spirax-Sarco Engineering and Fenner, while exiting from holdings in Dixons Carphone, Greggs and Halfords.

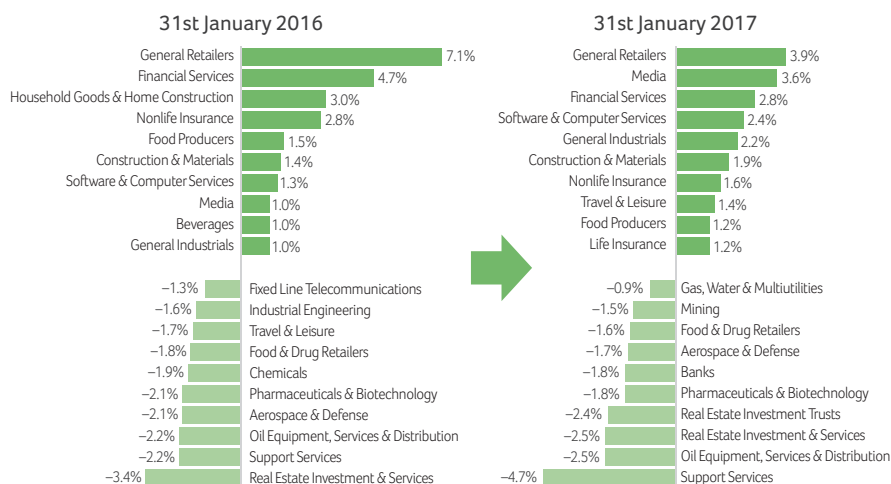
## Portfolio Geographic Revenue Exposure



# Strategic Report – continued

## Top 10/Bottom 10 Sector Active Positions

Portfolio weights relative to the Benchmark weight, 31st January 2016 and 31st January 2017



Source: J.P. Morgan Asset Management, Factset.

Last year we explained our positive view of the domestic consumer, as *'the slight uptick in earnings combined with negligible inflation has ushered forth a period of sustained real wage growth'*. While disposable income has increased and encouragingly consumption has thus far remained robust, this is no longer a prominent theme for the portfolio, given the increasing evidence of inflation and therefore risks to real wage growth and future consumption. In contrast to this and as highlighted above, we have increased our exposure to industrial companies, where the combination of an improving outlook for global industrial production and increasing inflation should provide a positive operating environment after an extended period of limited activity and minimal growth.

Fundamentally, we remain confident about the investment opportunities that can be found in our market and the structural advantages of investing in medium- and small-sized companies. Across the portfolio we remain excited about the prospects of our holdings in a broad range of industry sectors, but perhaps none more so than the disruptive business models that are thriving from a host of structural changes underway in the industries that they serve. Examples would include the online marketplaces such as Just Eat and Auto Trader – two companies that we have held since their Initial Public Offerings – and companies that are using technology to increase both their efficiency and the attractiveness of their customer offerings, such as Rentokil and Marshalls.

In terms of aggregate market exposure, the portfolio ended the year 2.5% geared which, while modest, was the highest level of gearing reached in the year. This reflected several factors: for the past few months global economic growth has shown signs of improvement, forecasts for UK economic growth have been revised upwards from very low levels and there are signs of increasing but crucially still moderate levels of inflation. These factors combined should provide a positive backdrop for equities. Counterbalancing this somewhat, there remain a whole host of domestic and international political uncertainties that must be faced in the year ahead and which will inevitably cause periods of increased market volatility. Reflecting these factors, we believe that it is appropriate to be modestly but positively geared and are 5.8% geared at the time of writing, leaving us with plenty of capacity to take advantage of any market driven or company specific opportunities for further reinvestment.

Guy Anderson  
Martin Hudson  
Anthony Lynch  
Investment Managers

6th April 2017



Guy Anderson



Martin Hudson



Anthony Lynch

# Strategic Report – continued

## Summary of Results

	2017	2016	
<b>Total returns for the year ended 31st January</b>			
Return on net assets <sup>1</sup>	+6.1%	+12.9%	
Return to shareholders <sup>2</sup>	+4.3%	+18.6%	
Benchmark <sup>3</sup>	+12.5%	+4.7%	
<b>Net asset value and discount at 31st January</b>			% change
Shareholders' funds (£'000)	1,744,143	1,853,730	-5.9
Net asset value per share with debt at par value	2,005.2p	1,931.8p	+3.8
Net asset value per share with debt at fair value <sup>4</sup>	1,921.0p	1,864.1p	+3.1
Share price discount to net asset value with debt at par value	12.5%	10.6%	
Share price discount to net asset value with debt at fair value <sup>4</sup>	8.6%	7.4%	
<b>Market Data at 31st January</b>			
The FTSE All-Share Index (capital only) excluding constituents of the FTSE 100 Index and investment trusts with net dividends reinvested <sup>5</sup>	3,746.8	3,425.7	+9.4
Share price	1,755.0p	1,727.0p	+1.6
Ordinary shares in issue at year end (excluding shares held in Treasury)	86,980,419	95,957,040	
<b>Revenue for the year ended 31st January</b>			
Net revenue available for shareholders (£'000)	49,296	49,580	-0.6
Revenue return per share	53.2p	51.5p	+3.3
Dividend per share	46.0p	43.0p	+7.0
<b>Ongoing Charges</b>	0.48%	0.48%	
<b>Gearing/(Net cash)<sup>6</sup></b>	2.5%	(4.2)%	

A glossary of terms and definitions is provided on page 69.

<sup>1</sup>Source: J.P.Morgan, using net asset value per share, cum income, with debt at par value.

<sup>2</sup>Source: Morningstar.

<sup>3</sup>Source: FTSE Russell. The Company's benchmark is the FTSE All-Share Index excluding constituents of the FTSE 100 Index and investment trusts with net dividends reinvested.

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

<sup>5</sup>Source: Datastream.

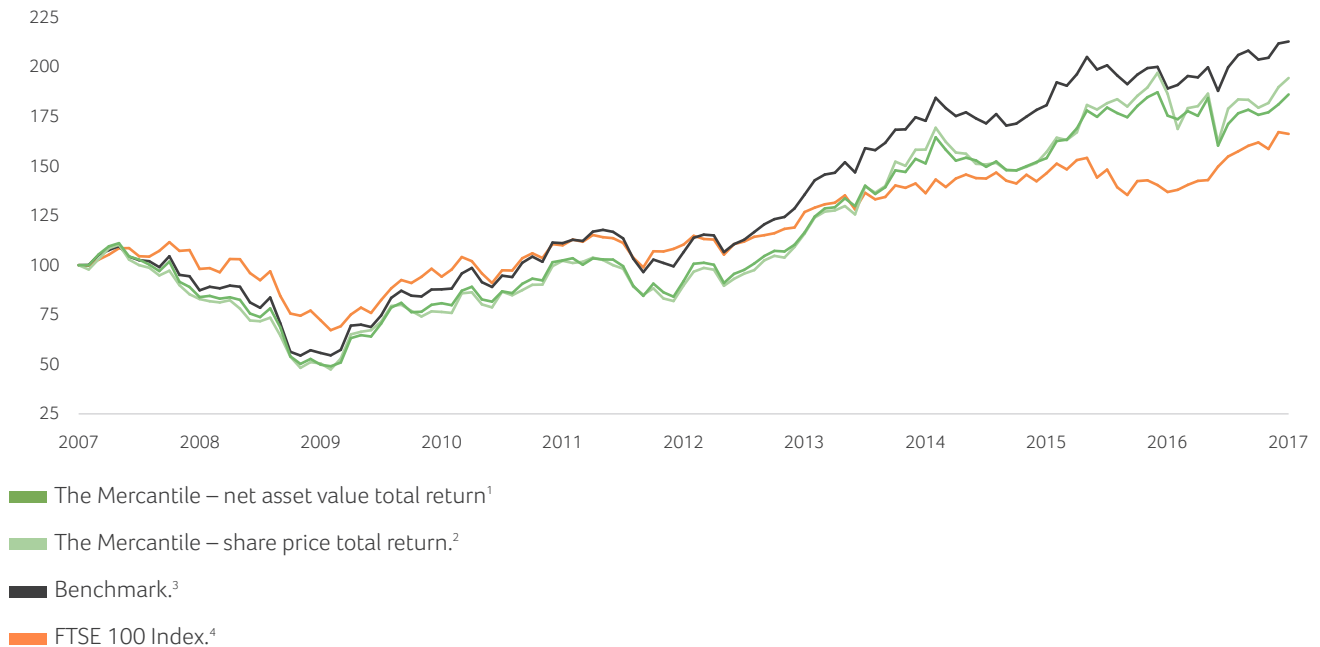
<sup>6</sup>The methodology to calculate gearing has been amended during the year. The previous years' figure has been amended for fair comparison. Please refer to the glossary of terms and definitions on page 69 for the revised calculation.

# Strategic Report – continued

## Performance

### Ten Year Performance

Figures have been rebased to 100 at 31st January 2007



Sources: <sup>1</sup>J.P.Morgan/Morningstar, using net asset value per share, cum income, with debt at fair. Prior to 30th June 2008, capital only NAV with debt at par value. <sup>2</sup>Morningstar, <sup>3</sup>FTSE Russell. <sup>4</sup>FTSE.

### Discount History



Source: Morningstar.

# Strategic Report – continued

## Ten Year Financial Record

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
<b>At 31st January</b>											
Total assets less current liabilities (€'m)	1,920.5	1,384.9	874.1	1,212.3	1,414.3	1,287.5	1,538.6	1,865.2	1,890.5	2,031.2	1,921.7
Net asset value per share (p) <sup>3</sup>	1,394.4	1,158.3	681.5	1,015.6	1,249.3	1,124.9	1,382.8	1,718.1	1,753.3	1,931.8	2,005.2
Share price (p)	1,258.0	1,020.0	592.5	860.0	1,109.0	940.0	1,171.0	1,550.0	1,498.0	1,727.0	1,755.0
<b>Year to 31st January</b>											
Gross revenue (€'000)	45,493	51,684	51,750	32,248	32,237	37,384	37,447	53,104	48,136	56,848	56,369
Revenue available for shareholders (€'000)	35,043	44,345	43,028	23,703	26,769	31,555	31,643	46,646	41,352	49,580	49,296
Revenue return per share (p)	27.5	39.8	41.7	23.2	26.9	31.9	32.1	47.5	42.1	51.5	53.2
Dividend per share (net) (p) <sup>1</sup>	25.0	38.0	36.0	36.0	36.0	36.0	36.0	40.0	41.0	43.0	46.0
Discount (%)	9.8	11.9	13.0	15.3	11.2	16.4	15.3	9.8	14.6	10.6	12.5
Gearing/(net cash) (%)	2.0	(5.2)	2.8	11.9	8.9	14.3	2.7	8.9	(0.9)	(4.2)	2.5
Ongoing Charges (%) <sup>2</sup>	0.55	0.59	0.56	0.54	0.49	0.51	0.49	0.48	0.49	0.48	0.48
<b>Rebased to 100 at 31st January 2007</b>											
Net asset value per share <sup>3</sup>	100.0	83.1	48.9	72.8	89.6	80.7	99.2	123.2	125.7	138.5	143.8
Net asset value per share – total return <sup>4</sup>	100.0	83.9	49.8	80.8	102.4	92.0	116.5	151.3	154.0	175.4	186.1
Share price	100.0	81.1	47.1	68.4	88.2	74.7	93.1	123.2	119.1	137.3	139.5
Share price – total return <sup>5</sup>	100.0	82.9	50.4	76.4	102.2	89.8	115.9	158.3	157.1	186.9	194.4
Benchmark <sup>5</sup>	100.0	87.3	55.7	87.8	111.1	106.6	135.6	172.8	180.7	189.1	212.8
Revenue return per share	100.0	144.7	151.6	84.4	97.9	115.9	116.7	172.6	153.1	187.3	193.5
Dividends per share <sup>1</sup>	100.0	152.0	144.0	144.0	144.0	144.0	144.0	160.0	164.0	172.0	184.0

<sup>1</sup>2008 includes ordinary dividends of 34.0p and a special dividend of 4.0p.

<sup>2</sup>Ongoing Charges represents the management fee and all other operating expenses excluding finance costs, expressed as a percentage of the average of the daily net assets during the year (2009 to 2011: Total Expense Ratio, calculated on the average of the month end net assets; 2008 and prior years; the average of the opening and closing net assets). The ongoing charges are calculated in accordance with guidance issued by the Association of Investment Companies in May 2012.

<sup>3</sup>Source: J.P. Morgan, using net asset value per share, cum income, with debt at par value.

<sup>4</sup>Source: J.P. Morgan/Morningstar, using net asset value per share, cum income, with debt at fair value. Prior to 30th June 2008, capital only NAV with debt at par value.

<sup>5</sup>Source: Morningstar, FTSE Russell.

# Strategic Report – continued

## Ten Largest Investments

Company	At 31st January 2017		At 31st January 2016	
	Valuation £'000	% <sup>1</sup>	Valuation £'000	% <sup>1</sup>
<b>DS Smith<sup>2</sup></b>	46,603	2.6	—	—
<b>Phoenix<sup>3</sup></b>	42,864	2.4	18,986	1.1
<b>Auto Trader<sup>3</sup></b>	40,424	2.3	25,948	1.5
<b>Inchcape</b>	38,646	2.2	34,285	1.9
<b>SEGRO</b>	38,489	2.2	35,554	2.0
<b>Domino's Pizza</b>	37,175	2.1	42,086	2.4
<b>Just Eat<sup>3</sup></b>	36,308	2.0	18,292	1.0
<b>Rentokil Initial<sup>3</sup></b>	35,898	2.0	24,618	1.4
<b>Bellway</b>	34,261	1.9	40,003	2.2
<b>Halma<sup>3</sup></b>	33,532	1.9	28,631	1.6
<b>Total<sup>4</sup></b>	<b>384,200</b>	<b>21.6</b>		

All of the above investments are listed in the UK.

<sup>1</sup>Based on total portfolio of £1,787m (2016: £1,776m).

<sup>2</sup>Not held in the portfolio at 31st January 2016.

<sup>3</sup>Not included in the ten largest investments at 31st January 2016.

<sup>4</sup>At 31st January 2016, the value of the ten largest investments amounted to £382m representing 21.5% of the total portfolio.



# Strategic Report – continued

## Portfolio Analyses

### Listed Equity Market Capitalisation

at 31st January

	2017 % <sup>1</sup>	2016 % <sup>1</sup>
UK FTSE Mid Sized	84.4	78.9
UK FTSE Small & Fledgling	7.1	9.3
UK AIM	4.7	5.9
UK FTSE 100	3.5	5.6
UK Unquoted	0.2	0.2
Overseas	0.1	0.1
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

<sup>1</sup>Based on total portfolio of £1,787m (2016: £1,776m).

### Sector Analysis

at 31st January

	Portfolio 2017 % <sup>1</sup>	Benchmark 2017 %	Portfolio 2016 % <sup>1</sup>	Benchmark 2016 %
Industrials	29.8	30.7	24.1	28.1
Consumer Services	27.3	20.1	28.9	24.2
Financials	19.7	22.2	21.7	20.6
Consumer Goods	7.6	7.3	11.6	6.9
Real Estate	4.8	2.9	6.8	4.0
Technology	3.9	2.0	4.3	2.8
Basic Materials	2.4	4.2	0.5	3.7
Oil & Gas	1.9	4.3	1.4	3.4
Health Care	1.6	3.5	0.7	3.5
Utilities	0.7	1.4	-	1.5
Telecommunications	0.3	1.4	-	1.3
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

<sup>1</sup>Based on total portfolio of £1,787m (2016: £1,776m).

# Strategic Report – continued

## List of Investments

at 31st January 2017

Company	Valuation £'000	Company	Valuation £'000
<b>Industrials</b>		<b>Consumer Services</b>	
DS Smith	46,603	Auto Trader	40,424
Rentokil Initial	35,898	Inchcape	38,646
Halma	33,532	Domino's Pizza	37,175
Spirax-Sarco Engineering	29,691	Just Eat	36,308
RPC	28,756	Moneysupermarket.com	31,458
Ricardo	28,680	Rightmove	27,336
BBA Aviation	28,219	Saga	25,710
WS Atkins	26,116	SSP	25,093
Weir	22,256	National Express	21,178
Polypipe	20,832	JD Sports Fashion	20,137
QinetiQ	20,700	B&M European Value Retail	19,813
Bodycote	18,900	Playtech	19,274
Morgan Advanced Materials	17,732	WH Smith	17,457
Serco	17,720	William Hill	17,130
VP	17,274	Card Factory	15,949
Grafton	17,046	888	15,635
Renishaw	15,847	Zoopla Property	14,201
Keller	15,094	Young & Co's Brewery 'A'	11,952
Marshalls	14,667	Ascential	11,002
Hill & Smith	13,858	Cineworld	10,651
Morgan Sindall	11,482	Daily Mail & General Trust 'A'	8,102
Diploma	10,725	4imprint	5,701
Fenner	7,613	Trinity Mirror	5,543
Howden Joinery	7,528	Lookers	4,855
Renold	7,188	M&C Saatchi <sup>1</sup>	4,762
Ibstock	6,281	Gocompare.Com	1,832
XP Power	4,937	Peel Hotels <sup>1</sup>	1,587
Charles Taylor	3,783		
T Clarke	1,907		
Kier	1,519		
	<b>532,384</b>		<b>488,911</b>

## Strategic Report – continued

Company	Valuation £'000
<b>Financials</b>	
Phoenix	42,864
Intermediate Capital	29,639
Hiscox	27,189
Beazley	25,933
TP ICAP	24,386
Close Brothers	24,215
Jupiter Fund Management	21,274
3i	20,985
Man	20,068
Henderson	16,996
Jardine Lloyd Thompson	15,450
Brewin Dolphin	14,461
John Laing	11,625
IG	9,807
Arrow	9,471
Melrose Industries	8,970
Novae	8,390
Shawbrook	8,089
Mortgage Advice Bureau <sup>1</sup>	4,531
Cenkos Securities <sup>1</sup>	3,654
Shore Capital <sup>1</sup>	3,395
	<b>351,392</b>

Company	Valuation £'000
<b>Consumer Goods</b>	
Bellway	34,261
Cranswick	25,530
MP Evans <sup>1</sup>	20,160
Greencore	13,725
Berkeley	12,600
Fevertree Drinks <sup>1</sup>	10,566
Taylor Wimpey	9,218
Headlam	5,033
Countryside Properties	4,904
	<b>135,997</b>
<b>Real Estate</b>	
SEGRO	38,489
Great Portland Estates	17,927
LondonMetric Property	11,724
Savills	11,121
Shaftesbury	4,332
Channel Islands Property Fund <sup>2</sup>	2,170
	<b>85,763</b>
<b>Technology</b>	
Micro Focus International	32,160
Sophos	21,517
Softcat	8,564
Fidessa	5,596
FDM	2,343
	<b>70,180</b>
<b>Basic Materials</b>	
Polymetal International	12,631
Synthomer	12,617
Acacia Mining	6,888
Evraz	5,352
Tennants Consolidated <sup>3,4</sup>	3,606
KAZ Minerals	1,266
	<b>42,360</b>

## Strategic Report – continued

Company	Valuation £'000
<b>Oil &amp; Gas</b>	
Cairn Energy	18,679
Faroe Petroleum <sup>1</sup>	9,953
BowLeven <sup>1</sup>	3,634
Egdon Resources <sup>1</sup>	1,998
	<b>34,264</b>
<b>Health Care</b>	
NMC Health	20,269
Abcam <sup>1</sup>	8,054
	<b>28,323</b>
<b>Utilities</b>	
Drax	12,029
	<b>12,029</b>
<b>Telecommunications</b>	
Telecom Plus	5,528
	<b>5,528</b>
<b>Materials</b>	
International Ferro Metals <sup>3</sup>	—
	<b>—</b>
<b>Total Investments<sup>5</sup></b>	<b>1,787,131</b>

<sup>1</sup>AIM listed investment.

<sup>2</sup>Listed overseas.

<sup>3</sup>Unquoted investment.

<sup>4</sup>Includes a fixed interest investment.

<sup>5</sup>The portfolio comprises investments in equity shares, and a fixed interest investment.

# Strategic Report

## Business Review

The aim of the Strategic Report is to provide shareholders with the ability to assess how the Directors have performed their duty to promote the success of the Company during the year under review.

### Objective and Strategy of the Company

The Mercantile Investment Trust plc is an investment trust company that has a premium listing on the London Stock Exchange. Its objective is to achieve long term capital growth from a portfolio of UK medium and smaller companies. The Company employs JPMorgan Funds Limited ('JPMF' or the 'Manager') to actively manage its assets. The Board has determined an investment policy and related guidelines and limits, as described below.

### Structure of the Company

The Company is subject to UK and European legislation and regulations including UK company law, UK Financial Reporting Standards, the UK Listing, Prospectus, Disclosure Guidance and Transparency Rules, taxation law and the Company's own Articles of Association.

The Company is an investment company within the meaning of Section 833 of the Companies Act 2006 and has been approved by HM Revenue & Customs as an investment trust (for the purposes of Sections 1158 and 1159 of the Corporation Tax Act 2010). As a result the Company is not liable for taxation on capital gains. The Directors have no reason to believe that approval will not continue to be retained. 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 3 to 5, and in the Investment Managers' Report on pages 6 to 10.

### Investment Policies and Risk Management

In order to achieve its objective and to seek to manage risk, the Company's business model is to invest in a diversified portfolio and it 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 Restrictions and Guidelines

- 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 total assets. The Company may hold five positions

of up to 8%, totalling no more than 40% of the Company's gross assets. Thereafter a maximum of 3% of gross assets may be held in any one investment.

- Capital 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 10% net cash to 20% geared.
- The Company does not invest more than 15% of its gross assets in other listed closed-ended investment funds (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 2017, the Company produced a total return to shareholders of 4.3% and a total return on net assets of 6.1%. This compares with the return on the Company's benchmark of 12.5%. At 31st January 2017, the value of the Company's investment portfolio was £1,787 million. The Investment Managers' Report on pages 6 to 10 includes a review of developments during the year as well as information on investment activity within the Company's portfolio.

### Total Return, Revenue and Dividends

Gross total return for the year amounted to £101.6 million (2016: £234.2 million) and net total return after deducting interest, management expenses and taxation amounted to £81.7 million (2016: £213.8 million). Distributable income for the year amounted to £49.3 million (2016: £49.6 million). The Directors have declared quarterly interim dividends totalling 46.0p (2016: 43.0p) per ordinary share for the year which totalled £41.4 million (2016: £41.3 million). The year end revenue reserve after allowing for these dividends will amount to £36.7 million (2016: £28.8 million).

### Key Performance Indicators ('KPIs')

The Company's objective is to achieve long term capital growth from a portfolio of UK medium and smaller companies. In order to monitor performance against this objective, 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. Please refer to the graph headed 'Ten Year Performance' on page 12.

# Strategic Report – continued

- **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 stock selection and sector allocation. Details of the attribution analysis for the year ended 31st January 2017 are given in the Investment Managers' Report on page 6.

- **Share price discount to net asset value ('NAV') per share**

The Board operates a share repurchase programme that seeks to enhance value and address imbalances in supply and demand of the Company's shares within the market and thereby reduce the volatility and absolute level of the discount to NAV at which the Company's shares trade. Please refer to the graph headed 'Discount History' on page 12.

- **Ongoing Charges**

The ongoing charges represent the Company's management fee and all other operating expenses, excluding finance costs, expressed as a percentage of the average of the daily net assets during the year. The ongoing charges for the year ended 31st January 2017 were 0.48% (2016: 0.48%). The Board reviews each year an analysis which shows a comparison of the Company's ongoing charges and its main expenses with those of its peers.

## Share Capital

During the year, the Company repurchased a total of 8,976,621 shares, amounting to 9.4% of issued share capital at the beginning of the year. Of those shares 1,507,822 (2016: 1,747,595) were repurchased for a total consideration of £25,073,000 (2016: £27,955,000) and cancelled. The balance of 7,468,799 shares were repurchased for a total consideration of £125,610,000 and held in Treasury. As the shares were repurchased at a discount to the underlying net asset value ('NAV') they enhanced the NAV of the remaining shares. The Company has repurchased a further 1,816,868 shares since the year end (as at 5th April 2017).

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 and has not issued any shares since the year end.

## Board Diversity

At 31st January 2017, there were six male Directors and one female Director on the Board. The Company has no employees. The Board's policy on diversity is set out on page 28.

## Discount

The Board monitors closely the level of the Company's share price discount to net asset value. During the year the discount increased from 10.6% to 12.5% on the basis of a cum income calculation with debt at par. Several different methodologies are currently employed by different bodies to assess net asset value and consequently different conclusions are drawn which can be difficult to interpret.

The Company reports its performance (Financial Highlights, Chairman's Statement, Investment Managers' report etc.) to shareholders on a cum income NAV with debt at par value basis. For the NAV stated in the Company's monthly factsheets and on its website, debt is valued at its fair value.

The AIC, for its industry statistics, stipulates the NAV as Shareholder Funds, both capital and income, expressed as an amount per ordinary share. Shareholder Funds are the net value of total assets having deducted prior charges at their fair (not par) value. The AIC does not however prescribe a methodology for the basis of calculation of fair value. Income for the current financial year is included (dividends are deducted from the income value on the day that shares go ex-dividend). This is equivalent to the cum income NAV with debt at fair value as calculated and published by ourselves, via the Regulatory News Service, on a daily basis.

The fair value of the Company's debentures is calculated using a discounted cash flow technique which applies the yield from a similarly dated gilt to the debentures issued by the Company and adds to that a margin based on the five year average for the AA Barclays Sterling Corporate Bond spread.

Using this calculation, i.e. NAV cum income with debt at fair value, the discount would be shown to have increased over the course of the year from 7.4% to 8.6%.

# Strategic Report – continued

## Employees, Social, Community and Human Rights Issues

The Company has no employees. Since many of its functions are carried out by employees of the Manager and its affiliate, JPMorgan Asset Management (UK) Limited ('JPMAM'), it notes the JPMAM policy statements in respect of social and environmental issues.

### Social, Environmental and Human Rights

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

*JPMAM is also a signatory to the United Nations Principles of Responsible Investment, which commits participants to six principles, with the aim of incorporating ESG criteria into their processes when making stock selection decisions and promoting ESG disclosure. Our detailed approach to how we implement the principles is available on request.*

*The Manager has implemented a policy which seeks to restrict investments in securities issued by companies that have been identified by an independent third party provider as being involved in the manufacture, production or supply of cluster munitions, depleted uranium ammunition and armour/and/or anti-personnel mines. Shareholders can obtain further details on the policy by contacting the Manager.*

### Greenhouse Gas Emissions

The Company has no premises, consumes no electricity, gas or diesel fuel and consequently does not have a measurable carbon footprint. *JPMAM is a signatory to Carbon Disclosure Project. JPMorgan Chase is a signatory to the Equator Principles on managing social and environmental risk in project finance.*

### The Modern Slavery Act 2015 (the 'MSA')

The MSA requires companies to prepare a slavery and human trafficking statement for each financial year of the organisation. As the Company has no employees and does not supply goods and services, the MSA does not apply directly to it. The MSA

requirements more appropriately relate to JPMF and JPMAM. JPMorgan's statement on Human Rights can be found on the following website: [www.jpmmorganchase.com/corporate/About-JPMC/ab-human-rights.htm](http://www.jpmmorganchase.com/corporate/About-JPMC/ab-human-rights.htm)

## Principal Risks

The Directors confirm that they have carried out a robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, viability, solvency or liquidity.

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 sector 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 on by the Manager. JPMF provides the Directors with timely and accurate management information, including performance data and attribution analyses, revenue estimates, liquidity reports and shareholder analyses. The Board monitors the implementation and results of the investment process with the Investment Managers, who attend all Board meetings, and reviews data which show statistical measures of the Company's risk profile. The Investment Managers employ the Company's gearing tactically, within a strategic range set by the Board.
- **Accounting, Legal and Regulatory:** In order to qualify as an investment trust, the Company must comply with Section 1158 of the Corporation Tax Act 2010 ('Section 1158'). Details of the Company's approval are given under 'Structure of the Company' above. Were the Company to breach Section 1158, it might lose investment trust status and, as a consequence, gains within the Company's portfolio could be subject to Capital Gains Tax. The Section 1158 qualification criteria are monitored continually by JPMF and the results reported to the Board each month. The Company must also comply with the provisions of the Companies Act and, since its shares are listed on the London Stock Exchange, the UKLA Listing Rules and Disclosure Guidance & Transparency Rules ('DTRs'). A breach of the Companies Act could result in the Company and/or the

# Strategic Report – continued

Directors being fined or the subject of criminal proceedings. Breach of the UKLA Listing Rules or DTRs could result in the Company's shares being suspended from listing which in turn would breach Section 1158. The Board relies on the services of its Company Secretary, JPMF, to ensure compliance with The Companies Act and the UKLA Listing Rules and DTRs.

- Corporate Governance and Shareholder Relations: Details of the Company's compliance with Corporate Governance best practice, including information on relations with shareholders, are set out in the Corporate Governance Statement on pages 27 to 31.
- Operational and Cybercrime: Disruption to, or failure of, JPMF's accounting, dealing or payments systems or the custodian's records could prevent accurate reporting and monitoring of the Company's financial position. This includes the risk of cybercrime and the consequent potential threat to security and business continuity. Details of how the Board monitors the services provided by JPMF and its associates and the key elements designed to provide effective risk management and internal control are included within the Risk Management and Internal Control section of the Corporate Governance statement on pages 30 and 31.

The threat of cyber attack, in all its guises, is regarded as at least as important as more traditional physical threats to business continuity and security. The Company benefits directly or indirectly from all elements of JPMorgan's Cyber Security programme. The information technology controls around the physical security of JPMorgan's data centres, security of its networks and security of its trading applications are tested by independent reporting accountants and reported on every six months against the Audit and Assurance Faculty ('AAF') standard.

- 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 regular 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 24 on pages 57 to 61.

## Long Term Viability

Taking account of the Company's current position, the principal risks that it faces and their potential impact on its future development and prospects, the Directors have assessed the prospects of the Company, to the extent that they are able to do so, over the next five years. They have made that assessment by considering those principal risks, the Company's investment objective and strategy, the investment capabilities of the Manager and the current outlook for the UK economy and equity market.

In determining the appropriate period of assessment the Directors had regard to their view that, given the Company's objective of achieving long term capital growth, shareholders should consider the Company as a long term investment proposition. This is consistent with advice provided by investment advisers, that investors should consider investing in equities for a minimum of five years. Thus the Directors consider five years to be an appropriate time horizon to assess the Company's viability.

The Directors confirm that they have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the five year period of assessment.

By order of the Board  
Jonathan Latter, for and on behalf of  
JPMorgan Funds Limited,  
Company Secretary

6th April 2017



# Governance

## Board of Directors



### Hamish Leslie Melville (Chairman)#

A Director since 1996 and Chairman since 2003.

Having served as an executive director of Hambros Bank, he founded Enskilda Securities. He was then chairman of Capel-Cure Myers Capital Management and then of Dunedin Fund Managers. He was chairman of the Investment Banking Committee of Credit Suisse Securities (Europe) Ltd for 12 years until 2010 when he joined The Royal Bank of Scotland to set up an Investment Banking Committee, leaving in 2012. He has served as chairman or director of a number of UK listed companies, and was chairman of The National Trust for Scotland for three years from 1995.



### Helen James\*#

A Director since September 2011.

Helen is CEO of Investis, a leading digital corporate communications company. She took on this role in October 2012, having been Managing Director and a co-founder of the Company in 2000. Prior to Investis Helen was head of Pan-European Equity Sales at Paribas. She is also a non-executive director of Edinburgh Worldwide Investment Trust plc.



### Angus Gordon Lennox\*#

A Director since September 2015.

Angus is a non-executive Director of Securities Trust of Scotland plc. He is also Executive Chairman of two private family businesses. Previously he had a 24 year career as a corporate broker, first as a partner of Cazenove & Co, and later as a Managing Director of JPMorgan Cazenove, which he resigned from in August 2010.



### Harry Morley\*#

A Director since May 2014 and Chairman of the Audit Committee since March 2015.

Harry was CEO of Armajaro Asset Management LLP from 2010 until 2016, and a non-executive Director of Bibendum Wine Holdings Ltd until May 2016. He was Co-founder and CFO of Tragus Holdings Ltd, owner of Café Rouge and Bella Italia restaurant chains, and also worked in the shipping industry for P&O. He is currently a non-executive Director of JD Wetherspoon plc. He will become a Trustee of The Ascot Authority in July 2017. He qualified as a chartered accountant with Price Waterhouse.

## Governance – continued



### Sandy Nairn\*#

A Director since 2003 and Senior Independent Director since December 2014.

Sandy 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.

Sandy is the sole shareholder of Nairn Capital Ltd, which holds a 30% interest in Goodhart Partners LLP.



### Ian Russell\*#

A Director since January 2007 and Chairman of the Audit Committee from May 2007 to March 2015.

Ian is Chairman of HICL Infrastructure Company Limited and of Scottish Futures Trust Limited. He is also a non-executive director of Aberdeen Diversified Income and Growth Trust plc. Previously he held senior positions with Scottish Power, Tomkins and HSBC.



### Jeremy Tighe\*#

A Director since March 2012.

Jeremy joined F&C Management in 1981 and was the fund manager of Foreign and Colonial Investment Trust plc from 1997 to July 2014. He was, until January 2013, a Director of the Association of Investment Companies. He is a non-executive Director of ICG Enterprise Trust plc, The Monks Investment Trust plc and Standard Life Equity Income Trust plc. He is Chairman of Syncona Limited.

\*A member of the Audit Committee throughout the year.

#A member of the Nomination Committee throughout the year.

All Directors are considered independent of the Manager.

# Governance – continued

## Directors' Report

The Directors present their report and the audited financial statements for the year ended 31st January 2017.

### Management of the Company

JPMorgan Funds Limited ('JPMF') is employed as Manager and Company Secretary to the Company 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.

JPMF 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 thoroughly reviewed the performance of JPMF in the course of the year. The review covered the performance of the Manager, its management processes, investment style, resources and risk controls and the quality of support that the Company receives from JPMF including the marketing support provided. The Board is of the opinion that the continuing appointment of the Manager is in the best interests of shareholders as a whole. Such a review is carried out on an annual basis.

The Board conducts a formal evaluation of the performance of, and contractual relationship with, the Manager on an annual basis. No separate Management Engagement Committee has been established because all Directors are considered to be independent of the Manager and, given the nature of the Company's business, it is felt that all Directors should take part in the review process.

### The Alternative Investment Fund Managers Directive ('AIFMD')

JPMF is the Company's alternative investment fund manager ('AIFM'). It is approved as an AIFM by the FCA. For the purposes of the AIFMD the Company is an alternative investment fund ('AIF'). JPMF has delegated responsibility for the day to day management of the Company's portfolio to JPMAM. The Company has appointed BNY Mellon Trust and Depositary (UK) Limited ('BNY') as its depositary. BNY has appointed JPMorgan Chase Bank, N.A. as the Company's custodian. BNY is responsible for the oversight of the custody of the Company's assets and for monitoring its cash flows.

The AIFMD requires certain information to be made available to investors in AIFs before they invest and requires that material changes to this information be disclosed in the annual report of each AIF. Investor Disclosure Documents, which set out information on the Company's investment strategy and policies, leverage, risk, liquidity, administration, management, fees, conflicts of interest and other shareholder information are available on the Company's website at [www.mercantileit.co.uk](http://www.mercantileit.co.uk). There have been no material changes (other than those reflected in these financial statements) to this information requiring disclosure. Any information requiring immediate disclosure pursuant to the AIFMD will be disclosed to

the London Stock Exchange through a primary information provider.

JPMF's remuneration disclosures are set out on page 63.

### Management Fee

With effect from 1st February 2017, the management fee is charged at the rate of 0.475% of the value of the Company's market capitalisation and is calculated and paid monthly in arrears. On 1st February 2018 the rate will reduce further, to 0.45% of the Company's market capitalisation. If the Company invests in funds managed or advised by JPMF, or any of its associated companies that charge an underlying fee, they are excluded from the calculation and therefore attract no fee. Prior to 1st February 2017, the management fee was charged at the rate of 0.5% of the Company's market capitalisation.

### Directors

The Directors of the Company during the year and subsequent to the year end, are detailed on pages 23 and 24.

Details of Directors' beneficial shareholdings may be found in the Directors' Remuneration Report on page 33.

No Director reported an interest in the Company's debentures during the year.

In accordance with corporate governance best practice, all Directors (with the exception of Hamish Leslie Melville) will retire at the Company's forthcoming Annual General Meeting and, being eligible, will offer themselves for reappointment by shareholders.

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

### Director Indemnification and Insurance

As permitted by the Company's Articles of Association, the Directors have the benefit of an indemnity which is a qualifying third party indemnity, as defined by Section 234 of the Companies Act 2006. This was in place throughout the financial year and also as at the date of approval of these financial statements.

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

### Disclosure of Information to Auditors

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

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

# Governance – continued

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

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

## Independent Auditors

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

## Capital Structure and Voting Rights

### Capital Structure

The Company's capital structure is summarised on page 1 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 16 to the Notice of AGM on page 66.

### Notifiable Interests in the Company's Voting Rights

At the year end, the following had declared a notifiable interest in the Company's voting rights:

Shareholders	Number of voting rights	% <sup>1</sup>
Brewin Dolphin Ltd	9,587,481	10.0
Rathbone Brothers Plc	9,416,994	10.0
Old Mutual Plc	6,765,884	7.1
Investec Wealth & Investment Ltd	4,141,454	4.3

<sup>1</sup>The percentage stated reflects the percentage of the Company's total voting rights held by the shareholder at the time of the notification to the Company.

The Company is also aware that approximately 6.1% of the Company's total voting rights are held by individuals through savings products managed by JPMAM, registered in the name of Chase Nominees Limited. If those voting rights are not exercised by the beneficial holders, in accordance with the terms and conditions of those savings products, under certain circumstances the Manager has the right to exercise those voting rights. That right is subject to certain limits and restrictions and falls away at the conclusion of the relevant general meeting.

## Miscellaneous Information

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.

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.

## Listing Rule 9.8.4R

Listing Rule 9.8.4R requires the Company to include certain information in an identified section of the Annual Report or a cross reference table indicating where the information is set out. The Directors confirm that there are no disclosures to be made in this report.

## 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 ('AGM'):

### Adoption of new Articles of Association (Resolution 11)

The Board proposes that the Company adopts new articles of association. For a detailed explanation of the proposed amendments to the Company's current Articles please refer to the Appendix to the Notice of Meeting on pages 67 and 68 of this report.

### Authority to allot new shares and to disapply statutory pre-emption rights (resolutions 12 and 13)

The Directors will seek renewal of the authority at the AGM to issue up to 4,258,177 Ordinary shares for cash up to an aggregate nominal amount of €1,064,544, such amount being equivalent to 5% of the present issued ordinary share capital as at the last practicable date before the publication of this document. The full text of the resolutions is set out in the Notice of Meeting on page 64. This authority will expire at the conclusion of the AGM of the Company in 2018 unless renewed at a prior general meeting.

It is advantageous for the Company to be able to issue new shares to participants purchasing shares through the JPMorgan savings products and also to other investors when the Directors consider that it is in the best interests of shareholders to do so. As such issues are only made at prices greater than the net asset value (the 'NAV'), they increase the NAV per share and spread the Company's administrative expenses, other than the management fee which is charged on the value of the Company's market capitalisation, over a greater number of shares. The issue proceeds are available for investment in line with the Company's investment policies.

# Governance – continued

## Authority to repurchase the Company's shares for cancellation (resolution 14)

At the Annual General Meeting held in May 2016, shareholders gave authority to the Company to purchase up to 14.99% of its then issued share capital. This authority will expire on 24th November 2017 unless renewed by shareholders. The Directors consider that the renewing of the authority is in the interests of shareholders as a whole, as the repurchase of shares at a discount to the underlying net asset value ('NAV') enhances the NAV of the remaining shares. Repurchased shares may be cancelled or held in Treasury. Any shares held in Treasury will only be reissued at a premium to NAV.

## Approval of dividend policy (resolution 15)

The Directors seek approval of the Company's dividend policy to continue to pay four quarterly interim dividends, which for the year ended 31st January 2017 have totalled 46.0 pence per share.

## Recommendation

The Board considers resolutions 11-15 are likely to promote the success of the Company and are in the best interests of the Company and its shareholders as a whole. The Directors unanimously recommend that you vote in favour of the resolutions as they intend to do in respect of their own beneficial holdings which amount in aggregate to 77,487 shares representing approximately 0.09% of the existing issued ordinary share capital of the Company. The full text of the resolutions are set out in the Notice of Meeting on pages 64 and 65.

## Corporate Governance Statement

### Compliance

The Company is committed to high standards of corporate governance. This statement, together with the Statement of Directors' Responsibilities on page 35, indicates how the Company has applied the principles of good governance of the Financial Reporting Council UK Corporate Governance Code (the 'UK Corporate Governance Code') and the AIC's Code of Corporate Governance, (the 'AIC Code'), which complements the UK Corporate Governance 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 UK Corporate Governance Code, insofar as they are relevant to the Company's business, and the AIC Code throughout the year under review.

### Role of the Board

A management agreement between the Company and JPMF sets out the matters which have been delegated to the Manager. This includes management of the Company's assets and the provision of accounting, company secretarial, administration and some marketing services.

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

At each Board meeting, Directors' interests are considered. These are reviewed carefully, taking into account the circumstances surrounding them, and, if considered appropriate, are approved. It was resolved that there were no actual or indirect interests of a Director which conflicted with the interests of the Company, which arose during the year.

The Board has procedures in place to deal with potential conflicts of interest and following the introduction of The Bribery Act 2010, has adopted appropriate procedures designed to prevent bribery. It 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, JPMF, 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, chaired by Hamish Leslie Melville, consists of seven 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 pages 23 and 24. Upon the retirement of Hamish Leslie Melville the Board will comprise six Directors.

There have been no changes to the Chairman's other significant commitments during the year under review.

A review of Board composition and balance is included as part of the annual performance evaluation of the Board. The Board appointed Sandy Nairn as its Senior Independent Director with effect from 3rd December 2014.

The Senior Independent Director leads the evaluation of the performance of the Chairman and may be contacted by shareholders if they have concerns that cannot be resolved through discussion with the Chairman.

# Governance – continued

## Tenure

The Chairman, Sandy Nairn and Ian Russell, having been Directors of the Company for more than nine years, have retained their independence by standing for annual reappointment. In this regard, the Board recommends the reappointment of Sandy Nairn and Ian Russell, who, having served in excess of nine years, retire and offer themselves for reappointment at this year's AGM. They have a wealth of experience in the financial sector, as set out in their biographies on pages 23 and 24, and make a valuable contribution to the workings of the Board.

The Board has agreed that, subject to his reappointment by shareholders at the forthcoming AGM, Angus Gordon Lennox will succeed Hamish Leslie Melville as Chairman, with effect from the close of the 2017 AGM.

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

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.

## Induction and Training

On appointment, the Manager and Company Secretary provide all Directors with induction training. Thereafter, regular briefings are provided on changes in law and regulatory requirements that affect the Company and the Directors. Directors are encouraged to attend industry and other seminars covering issues relevant to investment trust companies. Regular reviews of the Directors' training needs are carried out by the Nomination Committee by means of the evaluation process described below.

## Meetings and Committees

The Board delegates certain responsibilities and functions to committees. Details of membership of committees are shown with the Directors' profiles on pages 23 and 24. Directors who are not members of Committees may attend at the invitation of the Chairman.

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

These meetings were supplemented by additional meetings held to cover procedural matters and formal approvals. In addition there is regular contact between the Directors and the Manager and Company Secretary throughout the year.

Director	Board Meetings Attended	Audit Committee Meetings Attended	Nomination Committee Meetings Attended
Hamish Leslie Melville	6	3 <sup>1</sup>	1
Helen James	6	3	1
Angus Gordon Lennox	6	3	1
Harry Morley	6	3	1
Sandy Nairn	6	3	1
Ian Russell	5	2	—
Jeremy Tigue	6	3	1

<sup>1</sup>Attended by invitation.

## 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 and experience to carry out its fiduciary duties and to select and propose suitable candidates for appointment when necessary. The appointment process takes account of the benefits of diversity, including gender.

The Board's policy on diversity, including gender, is to take account of the benefits of these during the appointment process. However, the Board remains committed to appointing the most appropriate candidate, regardless of gender or other forms of diversity. Therefore, no targets have been set against which to report.

The Committee conducts an annual performance evaluation, to ensure that the Board, all members of the Board and its committees 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, in relation to remuneration policy and implementation.

An externally facilitated Board evaluation is carried out every three years. In 2011 and 2014 such evaluations were carried out by Stephenson & Co, which has no other connection to the Company. Such an evaluation is due to be carried out later in 2017.

### Audit Committee

The Audit Committee, chaired by Harry Morley, consists of all the Directors other than the Chairman and meets at least three times each year. The members of the Committee consider that they have the requisite skills and experience to fulfil the responsibilities of the Committee. For details of their qualifications see pages 23 and 24. Hamish Leslie Melville is not a member of the Audit Committee, however, he is invited to attend meetings as a guest.

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 UK Corporate Governance Code.

## Governance – continued

At the request of the Board, the Audit Committee provides confirmation to the Board as to how it has discharged its responsibilities so that the Board may ensure that information presented to it is fair, balanced and understandable, together with details of how it has done so.

During its review of the Company's financial statements for the year ended 31st January 2017, the Audit Committee considered the following significant issues, including those communicated by the Auditors during their reporting:

Significant issue	How the issue was addressed
Valuation and existence of investments	The valuation of investments is undertaken in accordance with the accounting policies, disclosed in note 1(b) to the accounts on page 46. Controls are in place to ensure that valuations are appropriate and existence is verified through custodian reconciliations.
Recognition of investment income	The recognition of investment income is undertaken in accordance with accounting policy note 1(d) to the accounts on pages 46 and 47. The Board regularly reviews subjective elements of income such as special dividends and agrees their accounting treatment.
Going concern	The Directors have considered the Company's investment objective, risk management policies, capital management policies and procedures, the nature of the portfolio and expenditure and cash flow projections. As a result, they have determined that the Company has adequate resources, an appropriate financial structure and suitable management arrangements in place to continue in operational existence for at least twelve months from the date of approval of these financial statements. Please refer to the section headed 'Going Concern' on page 31 for further details.
Compliance with Sections 1158 and 1159	Approval for the Company as an investment trust under Sections 1158 and 1159 has been obtained and ongoing compliance with the eligibility criteria is monitored on a regular basis.

The Board was made fully aware of any significant financial reporting issues and judgements made in connection with the preparation of the financial statements.

Having taken all available information into consideration and having discussed the content of the annual report and accounts with the Alternative Investment Fund Manager, Investment Managers, Company Secretary and other third party service providers, the Audit Committee has concluded that the Annual Report and Accounts for the year ended 31st January 2017, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy and has reported these findings to the Board. The Board's conclusions in this respect are set out in the Statement of Directors' Responsibilities on page 35.

The Audit Committee examines the effectiveness of the Company's risk management and internal control systems, receives information from the Manager's Compliance department and reviews the scope and results of the external audit, its effectiveness and cost effectiveness, the balance of audit and non-audit services and the independence and objectivity of the external auditors. The Audit Committee also receives confirmations from the Auditors, as part of their reporting, in regard to their objectivity and independence. In the Directors' opinion, the Auditors are considered independent.

The Audit Committee also has a primary responsibility for making recommendations to the Board on the reappointment and removal of external auditors. A predecessor firm of PricewaterhouseCoopers LLP ('PwC') was appointed on 8th January 1885, shortly after the Company's launch. The audit engagement partner rotates every five years in accordance with ethical guidelines and 2017 is the second year for the current partner.

As part of its review of the continuing appointment of the Auditors, the Audit Committee considered the length of tenure of the audit firm, its fee, its independence from JPMF and the Investment Managers and any matters raised during the audit. A formal tender exercise was undertaken in 2014, as a result of which PwC was reappointed. Written submissions were received from five audit firms. These were considered in full by Board representatives and a shortlist of three firms was drawn up. Meetings were held between a Committee of the Board and the shortlisted firms, using a selection checklist. Following those meetings, PwC was chosen, which was discussed with all Directors and the reappointment approved by Board resolution. A further tender review will be conducted in 2019 and a change of Audit firm will be proposed to shareholders for approval at the 2020 AGM.

The Audit Committee reviews and approves any non-audit services provided by the independent Auditors and assesses the impact of any non-audit work on the ability of the Auditors to remain independent. PwC reviews debenture loan covenants on an annual basis. Otherwise, no such work was undertaken during the year. Details of the fees paid for audit services are included in note 6 on page 49.

Representatives of the Company's Auditors attend the Audit Committee meeting at which the draft Annual Report & Accounts are considered. Having conducted the formal tender in 2014, and reviewed the performance of the external auditors, including the quality of work, timing of communications and work with JPMF, the Committee considered it appropriate to recommend their reappointment. The Board supported this recommendation which was put to shareholders at the 2016 Annual General Meeting.

In order to safeguard the Auditors' objectivity and independence, any significant non-audit services are carried out through a partner other than the audit engagement partner where appropriate. Fees paid for audit services, audit-related services and other non-audit services are set out, where relevant, in note 6 on page 49. There were no

## Governance – continued

significant non-audit engagements during the year under review. The Audit Committee has assessed the impact of any non-audit work carried out and is content with the Auditors' ability to remain independent and objective. The Directors' statement on the Company's system of risk management and internal control is set out below.

### Terms of Reference

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

### Relations with Shareholders

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

All shareholders have the opportunity, and are encouraged, to attend the Company's Annual General Meeting at which the Directors and representatives of the Manager are available in person to meet with shareholders and answer questions. In addition, a presentation is given by the Investment Managers who review the Company's performance. During the year the Company's brokers and the Investment Managers hold regular discussions with larger shareholders. The Directors are made fully aware of their views. The Chairman and Directors conduct visits to larger shareholders when requested and 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 71. The Chairman can also be contacted via the Company's website at [www.mercantileit.co.uk](http://www.mercantileit.co.uk).

The Company's Annual Report and Accounts is published in time to give shareholders at least 20 working days' notice of the Annual General Meeting. Shareholders wishing to raise questions in advance of the meeting are encouraged to submit questions via the Company's website or write to the Company Secretary at the address shown on page 71.

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

### Risk Management and Internal Control

The UK Corporate Governance Code requires the Directors, at least annually, to review the effectiveness of the Company's system of risk management and 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 risk management and 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 JPMF and its associates, the Company's system of risk management and internal control mainly consists of monitoring the services provided by JPMF and its associates, including the operating controls established by them, to ensure they meet the Company's business objectives. There is an ongoing process for identifying, evaluating and managing the significant risks faced by the Company (see Principal Risks on pages 21 and 22). This process, which was in place during the year under review and up to the date of approval of the Annual Report and Accounts, accords with the guidance of the Financial Reporting Council. As explained above, the Company is not required to have an internal audit function of its own, but relies on the internal audit department of the Manager. This arrangement is kept under review. The key elements designed to provide effective risk management and 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, depositary and custodian regulated by the Financial Conduct Authority (FCA), whose responsibilities are clearly defined in a written agreement.

**Management Systems** – The Manager's system of risk management and internal control includes organisational agreements which clearly define the lines of responsibility, delegated authority, control procedures and systems. These are monitored by the Manager's Compliance department which regularly monitors compliance with FCA 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 risk management and 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 the Manager's Compliance department;
- reviews reports on the risk management and internal controls and the operations of its Custodian, JPMorgan Chase Bank, which is itself independently reviewed;



## Governance – continued

- reviews every six months an independent report on the risk management and internal controls and the operations of the Manager; and
- reviews quarterly reports from the Company's depository.

By the means of the procedures set out above, the Board confirms that it has carried out a robust assessment of the effectiveness of the Company's system of risk management and internal control for the year ended 31st January 2017 and to the date of approval of this Annual Report and Accounts.

During the course of its review of the system of risk management and internal control, the Board has not identified nor been advised of any failings or weaknesses which it has determined to be significant.

### Going Concern

The Directors believe that, having considered the Company's investment objective (see page 19), risk management policies (see pages 57 and 61), capital management policies and procedures (see page 62), the nature of the portfolio and expenditure and cash flow projections, the Company has adequate resources, an appropriate financial structure and suitable management arrangements in place to continue in operational existence and they have not identified any material uncertainties to the Company's ability to continue to do so over a period of at least 12 months from the date of approval of these financial statements.

For these reasons, the Directors consider that there is reasonable evidence to continue to adopt the going concern basis in preparing the Company's financial statements.

### Corporate Governance and Voting Policy

The Company delegates responsibility for voting to the Manager.

The following is a summary of the Manager's policy statements on corporate governance, voting policy and social and environmental issues, which has been reviewed and noted by the Board. Details of social and environmental issues are included in the Strategic Report on page 21.

#### Corporate Governance

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

#### Proxy Voting

*JPMAM manages the voting rights of the shares entrusted to it as it would manage any other asset. It is the policy of JPMAM to vote in a prudent and diligent manner, based exclusively on our reasonable*

*judgement of what will best serve the financial interests of our clients. So far as is practicable, we will vote at all of the meetings called by companies in which we are invested.*

#### Stewardship/Engagement

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

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

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

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

By order of the Board  
Jonathan Latter, for and on behalf of  
JPMorgan Funds Limited,  
Company Secretary

6th April 2017

Copies of the UK Corporate Governance Code and the AIC Code may be found on the respective organisations' websites: [www.frc.org.uk](http://www.frc.org.uk) and [www.theaic.co.uk](http://www.theaic.co.uk)

# Governance – continued

## Directors' Remuneration Report

The Board presents the Directors' Remuneration Report for the year ended 31st January 2017, which has been prepared this Report in accordance with the requirements of Section 421 of the Companies Act 2006 as amended.

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 Auditor's opinion is included in their report on pages 36 to 41.

As all the Directors are non-executive, the Board has not established a Remuneration Committee. Instead, the Nomination Committee reviews Directors' fees on a regular basis and makes recommendations to the Board as and when appropriate.

### Directors' Remuneration Policy

The law requires that the Directors' Remuneration Policy Report is subject to a triennial binding vote. However, the Board has decided to seek annual approval and therefore an ordinary resolution to approve this report will be put to shareholders at the forthcoming Annual General Meeting. The policy subject to the vote, is set out in full below and is currently in force.

The Board's policy for this and subsequent years 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, the Chairman of the Audit Committee and the Senior Independent Director are paid higher fees than other Directors, reflecting the greater time commitment involved in fulfilling those roles.

The Nomination Committee, comprising all Directors, reviews 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 includes research carried out by third parties on the level of fees paid to the directors of the Company's peers and within the investment trust industry generally. The involvement of remuneration consultants has not been deemed necessary as part of this review.

All of the Directors are non-executive. There are no performance-related elements to their fees and the Company does not operate any type of incentive, share scheme, award 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 granted exit payments and are not provided with compensation for loss of office. No other payments are made to Directors, other than the reimbursement of reasonable out-of-pocket expenses incurred in attending the Company's business.

The Company's Articles of Association currently stipulate that aggregate fees must not exceed £300,000 per annum and provide

that any increase in this limit requires both Board and shareholder approval. At the forthcoming AGM, shareholders will be requested to approve an increase in the limit to £400,000 per annum, to allow for future fee increases. There has been no change in the maximum limit since 2010.

In the year under review, Directors' fees were paid at the following annual rates: Chairman £66,000; Chairman of the Audit Committee £48,000; Senior Independent Director £40,000; and other Directors £36,000.

The Company has no Chief Executive Officer and no employees and therefore no consultation of employees is required, and there is no employee comparative data to provide, in relation to the setting of the remuneration policy for Directors.

The Company has not sought shareholder views on its remuneration policy. The Nomination Committee considers any comments received from shareholders on remuneration policy on an ongoing basis.

The terms and conditions of Directors' appointments are set out in formal letters of appointment which are available for review at the Company's Annual General Meeting and the Company's registered office. Details of the Board's policy on tenure are set out on page 28.

### Directors Remuneration Policy Implementation

The Directors' Remuneration Policy Implementation Report is subject to an annual advisory vote and therefore an ordinary resolution to approve this report will be put to shareholders at the forthcoming Annual General Meeting. There have been no changes to the policy compared with 31st January 2016 and no changes are proposed for the year ending 31st January 2018.

At the Annual General Meeting held on 25th May 2016, of votes cast, 99.6% of votes cast were in favour of (or granted discretion to the Chairman who voted in favour of) both the remuneration policy and the remuneration report and 0.4% voted against. Votes withheld were the equivalent of less than 1.0% of the votes cast. Similar details for the 2017 AGM will be given in next year's Annual Report.

Details of the implementation of the Company's remuneration policy are given below. No advice from remuneration consultants was received during the year under review.

### Single total figure of remuneration

The single total figure of remuneration for each Director is detailed below together with the prior year comparative.

There are no performance targets in place for the Directors of the Company and there are no benefits for any of the Directors which will vest in the future. There are no benefits, pension, bonus, long term incentive plans, exit payments or arrangements in place on which to report.

# Governance – continued

## Single total figure table<sup>1</sup>

	2017		2016	
	Fees £	Taxable expenses <sup>2</sup> £	Fees £	Taxable expenses <sup>2</sup> £
Hamish Leslie Melville	66,000	61	66,000	—
Helen James	36,000	—	36,000	—
Angus Gordon Lennox <sup>3</sup>	36,000	2,163	12,789	—
Harry Morley <sup>4</sup>	48,000	1,240	44,248	—
Sandy Nairn	40,000	1,227	40,000	—
Ian Russell <sup>5</sup>	36,000	3,726	39,677	—
Jeremy Tigue	36,000	—	36,000	—
<b>Total</b>	<b>298,000</b>	<b>8,417</b>	<b>274,714</b>	<b>—</b>

<sup>1</sup>Audited information.

<sup>2</sup>Taxable travel and subsistence expenses incurred in attending Board and Committee meetings.

<sup>3</sup>Appointed 23rd September 2015.

<sup>4</sup>Appointed Chairman of the Audit Committee 25th March 2015.

<sup>5</sup>Resigned as Chairman of the Audit Committee 25th March 2015.

## Directors' Shareholdings<sup>1</sup>

The Directors' beneficial shareholdings are detailed below. The Directors have no other share interests or share options in the Company and no share schemes are available.

	31st January <sup>1</sup> 2017	1st February <sup>1</sup> 2016 or at date of appointment
Hamish Leslie Melville	40,000	40,000
Helen James <sup>2</sup>	650	650
Angus Gordon Lennox <sup>3</sup>	11,000	5,000
Harry Morley	3,000	2,000
Sandy Nairn	5,000	5,000
Ian Russell	5,000	5,000
Jeremy Tigue <sup>4</sup>	12,763	9,345
	<b>77,413</b>	<b>66,995</b>

<sup>1</sup>Audited information.

<sup>2</sup>Non-beneficial holding.

<sup>3</sup>Includes SIPP of 6,000 shares.

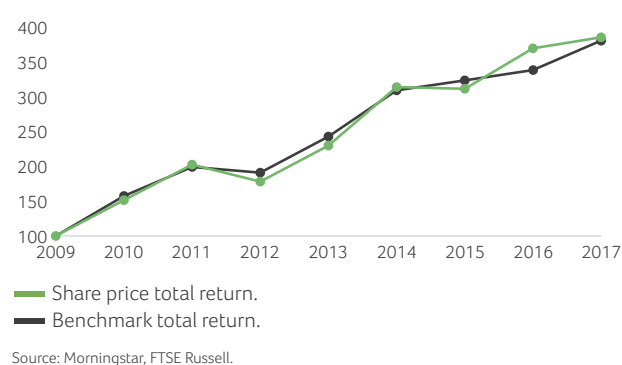
<sup>4</sup>On 1st February 2017 Jeremy Tigue acquired 74 shares through the Company's dividend reinvestment plan, taking his shareholding in the Company at the date of this report to 12,837.

No other changes to the Directors' holdings have been recorded at the date of this report.

No amounts (2016: nil) were paid to third parties for making available the services of Directors.

In accordance with the Companies Act 2006, a graph showing the Company's share price total return compared with its benchmark, the FTSE All-Share Index excluding constituents of the FTSE 100 Index and investment trusts, with net dividends reinvested, over the last eight years is shown below. The Board believes this benchmark is the most representative comparator for the Company.

### Eight year share price and benchmark total return to 31st January 2017



A table showing the total remuneration for the Chairman over the five years ended 31st January 2017 is below:

### Remuneration for the Chairman over the five years ended 31st January 2017

Year ended 31st January	Fees	Performance related benefits received as a percentage of maximum payable <sup>1</sup>
2017	£66,000	n/a
2016	£66,000	n/a
2015	£60,000	n/a
2014	£60,000	n/a
2013	£60,000	n/a

<sup>1</sup>In respect of one year period and periods of more than one year.

## Governance – continued

A table showing actual expenditure by the Company on remuneration and distributions to shareholders for the year and the prior year is below:

### Expenditure by the Company on remuneration and distributions to shareholders

	Year ended 31st January	
	2017 £	2016 £
Remuneration paid to all Directors	298,000	274,714
Distribution to shareholders		
— by way of dividend	40,564,000	45,227,000
— by way of share repurchases	150,683,000	27,955,000
Total distribution to shareholders	191,247,000	73,182,000

For and on behalf of the Board  
Hamish Leslie Melville  
Chairman

6th April 2017

## Governance – continued

### Statement of Directors' Responsibilities

The Directors are responsible for preparing the annual report and the accounts in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law, the Directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising Financial Reporting Standard 102, the Financial Reporting Standard applicable in the UK and Republic of Ireland ('FRS 102') and applicable law). Under Company law the Directors must not approve the financial statements unless they are satisfied that taken as a whole, the annual report and accounts are fair, balanced and understandable, provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy and that they give a true and fair view of the state of affairs of the Company and of the total return or loss of the Company for that period. In order to provide these confirmations, and in preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards, comprising FRS 102, have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Company will continue in business; and
- notify the Company's shareholders in writing about the use, if any, of disclosure exemptions in FRS 102 in the preparation of the financial statements

and the Directors confirm that they have done so.

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

2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Under applicable law and regulations the Directors are also responsible for preparing a Directors' Report and Directors' Remuneration Report that comply with that law and those regulations.

Each of the Directors, whose names and functions are listed on pages 23 and 24 confirms that, to the best of his/her knowledge, the financial statements, which have been prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), give a true and fair view of the assets, liabilities, financial position and net return or loss of the Company.

The Board confirms that it is satisfied that the Annual Report and Accounts taken as a whole are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

The Board also confirms that it is satisfied that the Strategic Report and Directors' Report include a fair review of the development and performance of the business, and the Company, together with a description of the principal risks and uncertainties that it faces.

The Financial Statements are published on the [www.mercantileit.co.uk](http://www.mercantileit.co.uk) website, which is maintained by the Manager. The maintenance and integrity of the website maintained by the Manager is, so far as it relates to the Company, the responsibility of the Manager. The work carried out by the Auditors does not involve consideration of the maintenance and integrity of this website and, accordingly, the Auditors accept no responsibility for any changes that have occurred to the accounts since they were initially presented to the website. The accounts are prepared in accordance with UK legislation, which may differ from legislation in other jurisdictions.

For and on behalf of the Board  
Hamish Leslie Melville  
Chairman

6th April 2017

# Independent Auditors' Report

to the members of The Mercantile Investment Trust plc

## Report on the financial statements

### Our opinion

In our opinion, The Mercantile Investment Trust plc's financial statements (the 'financial statements'):

- give a true and fair view of the state of the Company's affairs as at 31st January 2017 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

## What we have audited

The financial statements, included within the Annual Report & Accounts (the 'Annual Report'), comprise:

- the Statement of Financial Position as at 31st January 2017;
- the Statement of Comprehensive Income for the year then ended;
- the Statement of Cash Flows for the year then ended;
- the Statement of Changes in Equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

Certain required disclosures have been presented elsewhere in the Annual Report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

The financial reporting framework that has been applied in the preparation of the financial statements is United Kingdom Accounting Standards, comprising FRS 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland', and applicable law (United Kingdom Generally Accepted Accounting Practice).

## Our audit approach

The Mercantile Investment Trust plc is an investment trust company listed on the London Stock Exchange and invests primarily in UK equities. The Company engages JPMorgan Funds Limited to manage its assets. The operations of the Company are located in the UK.

### Overview



- Overall materiality: £17.4 million which represents 1% of the net assets.

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- The Company is a standalone investment trust company and engages JPMorgan Funds Limited (the 'Manager') to manage its assets.
- We conducted our audit of the financial statements from information provided by JPMorgan Corporate & Investment Bank (the 'Administrator') to whom the Manager has, with the consent of the Directors, delegated the provision of certain administrative functions.
- We tailored the scope of our audit taking into account the types of investments within the Company, the involvement of the third parties referred to above, the accounting processes and controls, and the industry in which the Company operates.

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- Income from investments
- Valuation and existence of investments

### The scope of our audit and our areas of focus

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ('ISAs (UK & Ireland)').

We designed our audit by determining materiality and assessing the risks of material misstatement in the financial statements. In particular, we looked at where the Directors made subjective judgements, for example in respect of significant accounting estimates

# Independent Auditors' Report – continued

that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits we also addressed the risk of management override of internal controls, including evaluating whether there was evidence of bias by the Directors that represented a risk of material misstatement due to fraud.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are identified as 'areas of focus' in the table below. We have also set out how we tailored our audit to address these specific areas in order to provide an opinion on the financial statements as a whole and any comments we make on the results of our procedures should be read in this context. This is not a complete list of all risks identified by our audit.

## Area of focus

## How our audit addressed the area of focus

### Income from investments

*Refer to page 29 (Directors' Report), page 46 (Accounting Policies) and 49 (Notes to the Financial Statements).*

ISAs (UK & Ireland) presume there is a risk of fraud in revenue recognition because of the pressure management may feel to meet their company's objective; for the Company management may feel pressure to achieve capital growth.

We focused on the accuracy and completeness of dividend income recognition and its presentation in the Statement of Comprehensive Income as set out in the requirements of The Association of Investment Companies Statement of Recommended Practice (the 'AIC SORP').

This is because incomplete or inaccurate income could have a material impact on the Company's net asset value and dividend cover.

We assessed the accounting policy for income recognition for compliance with accounting standards and the AIC SORP and performed testing to check that income had been accounted for in accordance with this stated accounting policy. We found that the accounting policies implemented were in accordance with accounting standards and the AIC SORP and that income had been accounted for in accordance with the stated accounting policy.

We understood and assessed the design and implementation of key controls surrounding income recognition.

In addition, we tested dividend receipts by agreeing the dividend rates to independent third party sources.

No misstatements were identified by our testing which required reporting to those charged with governance.

To test for completeness of dividend income, we tested that the appropriate dividends had been received in the year by reference to independent data of dividends declared for investment holdings in the portfolio. Our testing did not identify any unrecorded dividends.

We tested the allocation and presentation of dividend income between the income and capital return columns of the Statement of Comprehensive Income in line with the requirements set out in the AIC SORP. We then tested the validity of income and capital special dividends to independent third party sources.

We did not find any special dividends that were not treated in accordance with the AIC SORP.

### Valuation and existence of investments

*Refer to page 29 (Directors' Report), page 46 (Accounting Policies) and page 52 (Notes to the Financial Statements).*

The investment portfolio at the year-end principally comprised of listed equity investments of £1,783.5 million and unlisted equity investments of £3.6 million.

We focused on the valuation and existence of investments because investments represent the principal element of the net asset value as disclosed on the Statement of Financial Position in the financial statements.

We tested the valuation of the listed investment portfolio by agreeing the prices used in the valuation to independent third party sources. We reviewed the Directors' valuation of the unquoted stocks.

No misstatements were identified by our testing which required reporting to those charged with governance.

We tested the existence of the investment portfolio by agreeing the holdings to an independent custodian confirmation from JPMorgan Chase Bank, N.A.

No differences were identified by our testing which required reporting to those charged with governance.

# Independent Auditors' Report – continued

## How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the geographic structure of the Company, the accounting processes and controls, and the industry in which the company operates.

The Company is a standalone Investment Trust Company and engages JPMorgan Funds Limited (the 'Manager') to manage its assets.

We conducted our audit of the financial statements from information provided by JPMorgan Corporate & Investment Bank (the 'Administrator') to whom the Manager has, with the consent of the Directors, delegated the provision of certain administrative functions.

We tailored the scope of our audit taking into account the types of investments within the Company, the involvement of the third parties referred to above, the accounting processes and controls, and the industry in which the Company operates.

## Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

<b>Overall materiality</b>	£17.4 million (2016: £18.5 million).
<b>How we determined it</b>	1% of net assets.
<b>Rationale for benchmark applied</b>	We have applied this benchmark, a generally accepted auditing practice for investment trust audits, in the absence of indicators that an alternative benchmark would be appropriate and because we believe this provides an appropriate and consistent year on-year basis for our audit.

We agreed with the Audit Committee that we would report to it misstatements identified during our audit above £872,000 (2016: £927,000) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

## Going concern

Under the Listing Rules we are required to review the Directors' statement, set out on page 31, in relation to going concern. We have nothing to report having performed our review.

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to the Directors' statement about whether they considered it appropriate to adopt the going concern basis in preparing the financial statements. We have nothing material to add or to draw attention to.

As noted in the Directors' statement, the Directors have concluded that it is appropriate to adopt the going concern basis in preparing the financial statements. The going concern basis presumes that the Company has adequate resources to remain in operation and that the Directors intend it to do so, for at least one year from the date the financial statements were signed. As part of our audit we have concluded that the Directors' use of the going concern basis is appropriate. However, because not all future events or conditions can be predicted, these statements are not a guarantee as to the company's ability to continue as a going concern.



# Independent Auditors' Report – continued

## Other required reporting

### Consistency of other information and compliance with applicable requirements

#### *Companies Act 2006 reporting*

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In addition, in light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the Strategic Report and the Directors' Report. We have nothing to report in this respect.

#### *ISAs (UK & Ireland) reporting*

Under ISAs (UK & Ireland) we are required to report to you if, in our opinion:

<ul style="list-style-type: none"> <li>• information in the Annual Report is:               <ul style="list-style-type: none"> <li>– materially inconsistent with the information in the audited financial statements; or</li> <li>– apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Company acquired in the course of performing our audit; or</li> <li>– otherwise misleading.</li> </ul> </li> </ul>	We have no exceptions to report.
<ul style="list-style-type: none"> <li>• the explanation given by the Directors on page 35, in accordance with provision C.1.1 of the UK Corporate Governance Code (the 'Code'), as to why the Annual Report does not include a statement that they consider the Annual Report taken as a whole to be fair, balanced and understandable and provides the information necessary for members to assess the Company's position and performance, business model and strategy is materially inconsistent with our knowledge of the Company acquired in the course of performing our audit.</li> </ul>	We have no exceptions to report.
<ul style="list-style-type: none"> <li>• the section of the Annual Report on pages 28 to 30, as required by provision C.3.8 of the Code, describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.</li> </ul>	We have no exceptions to report.

#### *The directors' assessment of the prospects of the company and of the principal risks that would threaten the solvency or liquidity of the company*

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to:

<ul style="list-style-type: none"> <li>• the Directors' confirmation on page 21 of the Annual Report, in accordance with provision C.2.1 of the Code, that they have carried out a robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity.</li> </ul>	We have nothing material to add or to draw attention to.
<ul style="list-style-type: none"> <li>• the disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.</li> </ul>	We have nothing material to add or to draw attention to.
<ul style="list-style-type: none"> <li>• the Directors' explanation on page 22 of the Annual Report, in accordance with provision C.2.2 of the Code, as to how they have assessed the prospects of the Company, over what period they have done so and why they consider that period to be appropriate and their statement as to whether they have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.</li> </ul>	We have nothing material to add or to draw attention to.

Under the Listing Rules we are required to review the Directors' statement that they have carried out a robust assessment of the principal risks facing the Company and the Directors' statement in relation to the longer-term viability of the Company. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the Directors' process supporting their

# Independent Auditors' Report – continued

statements; checking that the statements are in alignment with the relevant provisions of the Code; and considering whether the statements are consistent with the knowledge acquired by us in the course of performing our audit. We have nothing to report having performed our review.

## Adequacy of accounting records and information and explanations received

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

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

We have no exceptions to report arising from this responsibility.

## Directors' remuneration

### Directors' Remuneration Report – Companies Act 2006 opinion

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

### Other Companies Act 2006 reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of Directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

## Corporate governance statement

Under the Listing Rules we are required to review the part of the Corporate Governance Statement relating to ten further provisions of the Code. We have nothing to report having performed our review.

## Responsibilities for the financial statements and the audit

### Our responsibilities and those of the Directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 35, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, 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.

### What an audit of financial statements involves

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

## Independent Auditors' Report – continued

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report. With respect to the Strategic Report and Directors' Report, we consider whether those reports include the disclosures required by applicable legal requirements.

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

6th April 2017

# Financial Statements

## Statement of Comprehensive Income for the year ended 31st January 2017

	Notes	2017			2016		
		Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
Gains on investments held at fair value through profit or loss	3	—	45,220	45,220	—	177,274	177,274
Net foreign currency (losses)/gains		—	(2)	(2)	—	85	85
Income from investments	4	55,112	—	55,112	55,783	—	55,783
Interest receivable and similar income	4	1,257	—	1,257	1,065	—	1,065
<b>Gross return</b>		<b>56,369</b>	<b>45,218</b>	<b>101,587</b>	<b>56,848</b>	<b>177,359</b>	<b>234,207</b>
Management fee	5	(2,173)	(5,071)	(7,244)	(2,279)	(5,317)	(7,596)
Other administrative expenses	6	(1,382)	—	(1,382)	(1,362)	—	(1,362)
<b>Net return on ordinary activities before finance costs and taxation</b>		<b>52,814</b>	<b>40,147</b>	<b>92,961</b>	<b>53,207</b>	<b>172,042</b>	<b>225,249</b>
Finance costs	7	(3,335)	(7,783)	(11,118)	(3,345)	(7,806)	(11,151)
<b>Net return on ordinary activities before taxation</b>		<b>49,479</b>	<b>32,364</b>	<b>81,843</b>	<b>49,862</b>	<b>164,236</b>	<b>214,098</b>
Taxation	8	(183)	—	(183)	(282)	—	(282)
<b>Net return on ordinary activities after taxation</b>		<b>49,296</b>	<b>32,364</b>	<b>81,660</b>	<b>49,580</b>	<b>164,236</b>	<b>213,816</b>
<b>Return per share</b>	10	<b>53.20p</b>	<b>34.93p</b>	<b>88.13p</b>	<b>51.46p</b>	<b>170.47p</b>	<b>221.93p</b>

Dividends declared in respect of the financial year ended 31st January 2017 total 46.0p (2016: 43.0p) per share amounting to £41,433,000 (2016: £41,320,000). Further information on dividends is given in note 9 on page 51.

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. Net return on ordinary activities after taxation represents the profit for the year and also Total Comprehensive Income.

The notes on pages 46 to 62 form an integral part of these financial statements.

## Financial Statements – continued

### Statement of Changes in Equity for the year ended 31st January 2017

	Called up share capital £'000	Share premium account £'000	Capital redemption reserve £'000	Capital reserves £'000	Revenue reserve <sup>1</sup> £'000	Total £'000
<b>At 31st January 2015</b>	24,426	23,459	12,344	1,615,974	36,893	1,713,096
Repurchase and cancellation of the Company's own shares	(437)	—	437	(27,955)	—	(27,955)
Net return on ordinary activities	—	—	—	164,236	49,580	213,816
Dividends paid in the year	—	—	—	—	(45,227)	(45,227)
<b>At 31st January 2016</b>	23,989	23,459	12,781	1,752,255	41,246	1,853,730
Repurchase and cancellation of Company's own shares	(377)	—	377	(25,073)	—	(25,073)
Repurchase of shares into Treasury	—	—	—	(125,610)	—	(125,610)
Net return on ordinary activities	—	—	—	32,364	49,296	81,660
Dividends paid in the year	—	—	—	—	(40,564)	(40,564)
<b>At 31st January 2017</b>	23,612	23,459	13,158	1,633,936	49,978	1,744,143

<sup>1</sup>This reserve forms the distributable reserve of the Company and may be used to fund distribution of profits to investors via dividend payments.

The notes on pages 46 to 62 form an integral part of these financial statements.

# Financial Statements – continued

## Statement of Financial Position at 31st January 2017

	Notes	2017 £'000	2016 £'000
<b>Fixed assets</b>			
Investments held at fair value through profit or loss	11	1,787,131	1,775,622
<b>Current assets</b>			
Debtors	13	10,945	6,185
Cash and short term deposits		38,295	162,719
Cash equivalents: liquidity funds		99,763	99,925
		149,003	268,829
<b>Creditors: amounts falling due within one year</b>	14	(14,415)	(13,242)
<b>Net current assets</b>		134,588	255,587
<b>Total assets less current liabilities</b>		1,921,719	2,031,209
<b>Creditors: amounts falling due after more than one year</b>	15	(177,576)	(177,479)
<b>Net assets</b>		1,744,143	1,853,730
<b>Capital and reserves</b>			
Called up share capital	16	23,612	23,989
Share premium	17	23,459	23,459
Capital redemption reserve	17	13,158	12,781
Capital reserves	17	1,633,936	1,752,255
Revenue reserve	17	49,978	41,246
<b>Total shareholders' funds</b>		1,744,143	1,853,730
<b>Net asset value per share</b>	18	2,005.2p	1,931.8p

The financial statements on pages 42 to 62 were approved and authorised for issue by the Directors on 6th April 2017 and are signed on their behalf by:

**Hamish Leslie Melville**

Chairman

The notes on pages 46 to 62 form an integral part of these financial statements.

The Mercantile Investment Trust plc

**Registered in England, company registration number 20537**

# Financial Statements – continued

## Statement of Cash Flows for the year ended 31st January 2017

	Notes	2017 £'000	2016 £'000
Net cash outflow from operations before dividends and interest	19	(8,427)	(9,076)
Dividends received		55,055	53,827
Interest received		944	840
Overseas tax recovered		412	—
Interest paid		(11,060)	(11,058)
<b>Net cash inflow from operating activities</b>		<b>36,924</b>	<b>34,533</b>
Purchases of investments		(732,866)	(726,385)
Sales of investments		755,321	838,773
Settlement of foreign currency contracts		15	(21)
<b>Net cash inflow from investing activities</b>		<b>22,470</b>	<b>112,367</b>
Dividends paid		(40,564)	(45,227)
Repurchase and cancellation of the Company's own shares		(25,073)	(32,201)
Repurchase of shares into Treasury		(118,356)	—
<b>Net cash outflow from financing activities</b>		<b>(183,993)</b>	<b>(77,428)</b>
<b>(Decrease)/increase in cash and cash equivalents</b>		<b>(124,599)</b>	<b>69,472</b>
Cash and cash equivalents at start of year		262,644	193,167
Exchange movements		13	5
Cash and cash equivalents at end of year		138,058	262,644
<b>(Decrease)/increase in cash and cash equivalents</b>		<b>(124,599)</b>	<b>69,472</b>
<b>Cash and cash equivalents consist of:</b>	20		
Cash and short term deposits		38,295	162,719
Cash held in JPMorgan Sterling Liquidity Fund		99,763	99,925
<b>Total</b>		<b>138,058</b>	<b>262,644</b>

The notes on pages 46 to 62 form an integral part of these financial statements.

# Financial Statements – continued

## Notes to the Financial Statements for the year ended 31st January 2017

### 1. Accounting Policies

#### (a) Basis of accounting

The financial statements are prepared in accordance with the Companies Act 2006, United Kingdom Generally Accepted Accounting Practice ('UK GAAP'), including FRS 102 'Financial Reporting Standard applicable in the UK and Republic of Ireland' and the Statement of Recommended Practice 'Financial Statements of Investment Trust Companies and Venture Capital Trusts' (the 'SORP') issued by the Association of Investment Companies in November 2014.

All of the Company's operations are of a continuing nature.

The financial statements have been prepared on a going concern basis. The disclosures on going concern on page 31 of the Directors' Report form part of these financial statements.

The policies applied in these financial statements are consistent with those applied in the preceding year, except for the following matters:

In March 2016, the FRC published amendments to FRS 102 concerning the fair value hierarchy disclosures. These amendments are effective for accounting periods beginning on or after 1st January 2017. Full disclosure is given in note 23 on pages 56 to 57.

#### (b) Valuation of investments

The Company has chosen to adopt Sections 11 and 12 of FRS 102 in respect of financial instruments.

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. The 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 treated by the Company as 'held at fair value through profit or loss'. They are included initially at fair value which is taken to be their cost, excluding expenses incidental to purchase which are written off to capital at the time of acquisition. Subsequently the investments are valued at fair value, which are quoted bid prices for investments traded in active markets. For investments which are not traded in active markets, unlisted and restricted investments, the Board takes into account the latest traded prices, other observable market data and asset values based on the latest management accounts.

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

#### (c) Accounting for reserves

Gains and losses on sales of investments including the related foreign exchange gains and losses, realised gains and losses on cash and short term deposits, realised gains and losses on foreign currency contracts, management fee and finance costs allocated to capital and any other capital charges, are included in the Statement of Comprehensive Income and dealt with in capital reserves within '(Losses)/gains on sales of investments based on the carrying value at the previous balance sheet date'.

Increases and decreases in the valuation of investments held at the year end including the related foreign exchange gains and losses, are included in the Statement of Comprehensive Income and dealt with in capital reserves within 'Net movement in investment holding gains and losses'.

#### (d) Income

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

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

Special dividends are looked at individually to ascertain the reason behind the payment. This will determine whether they are treated as income or capital.

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

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

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

Underwriting commission is recognised in revenue where it relates to shares that the Company is not required to take up.



# Financial Statements – continued

Where the Company is required to take up a proportion of the shares underwritten, the same proportion of commission received is deducted from the cost of the shares taken up, with the balance taken to revenue.

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

## (e) Expenses

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

- The management fee is allocated 30% to revenue and 70% to capital, 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 of an investment are included within the cost of the investment and those incidental to the sale are deducted from the sale proceeds. These expenses are commonly referred to as transaction costs and comprise brokerage commission and stamp duty. Details of transaction costs are given in note 11 on page 52.

## (f) Finance costs

Finance costs are accounted for on an accruals basis using the effective interest rate method.

Finance costs are allocated 30% to revenue and 70% to capital, in line with the Board's expected long term split of revenue and capital return from the Company's investment portfolio.

## (g) Financial instruments

Cash and cash equivalents may comprise cash (including demand deposits which are readily convertible to a known amount of cash and are subject to an insignificant risk of change in value) as well as cash equivalents. Liquidity funds are considered cash equivalents as they are held for cash management purposes as an alternative to cash.

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

The debenture in issue is classified as a financial liability at amortised cost. It was initially measured at the proceeds net of direct issue costs and subsequently measured at amortised cost. The amortisation of direct issue costs are accounted for on an accruals basis in the Statement of Comprehensive Income using the effective interest rate method.

Bank loans are classified as financial liabilities measured at amortised cost. They are initially measured as proceeds and subsequently measured at amortised cost. Interest payable on the bank loan is accounted for on an accruals basis in the Statement of Comprehensive Income.

Derivative transactions which the Company may enter into comprises forward exchange contract, the purpose of which is to manage currency risk arising from the Company's investing activities. The Company does not use derivative financial instruments for speculative purposes.

## (h) Taxation

Current tax is provided at the amounts expected to be paid or recovered.

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 more likely than not that taxable profits will be available against which those timing differences can be utilised.

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

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

## (i) Value Added Tax ('VAT')

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

## (j) Functional currency

The Company is required to identify a functional currency, being the currency of the primary economic environment in which the Company 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 also the currency in which the financial statements are presented.

# Financial Statements – continued

## 1. Accounting Policies – continued

### (j) Functional currency – continued

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 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 'Investment holding gains and losses' for investments still held at year end, and in 'Gains and losses on sales of investments' for investments sold during the year.

### (k) Dividends payable

Dividends are included in the financial statements in the year in which they are approved by shareholders.

### (l) Repurchase of ordinary shares for cancellation

The cost of repurchasing ordinary shares including the related stamp duty and transactions costs is charged to 'Capital reserves' and dealt with in the Statement of Changes in Equity. Share repurchase transactions are accounted for on a trade date basis.

The nominal value of ordinary share capital repurchased and cancelled is transferred out of 'Called up share capital' and into 'Capital redemption reserve'.

### (m) Repurchase of shares into Treasury

The cost of repurchasing shares into Treasury, including the related stamp duty and transaction costs is charged to 'Capital reserves' and dealt with in the Statement of Changes in Equity. Share repurchase transactions are accounted for on a trade date basis. Where shares held in Treasury are subsequently cancelled, the nominal value of those shares is transferred out of 'Called up share capital' and into 'Capital redemption reserve'.

Should shares held in Treasury be reissued, the sales proceeds will be treated as a realised profit up to the amount of the purchase price of those shares and will be transferred to capital reserves. The excess of the sales proceeds over the purchase price will be transferred to share premium.

## 2. Significant accounting judgements, estimates and assumptions

The preparation of the Company's financial statements on occasion requires the Directors to make judgements, estimates and assumptions that affect the reported amounts in the primary financial statements and the accompanying disclosures. These assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in the current and future periods, depending on circumstance.

The Directors do not believe that any significant accounting judgements or estimates have been applied to this set of financial statements, that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year.

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

	2017 £'000	2016 £'000
Gains on investments held at fair value through profit or loss based on historical cost	50,192	122,898
Amounts recognised in investment holding gains and losses in the previous year in respect of investments sold during the year	(128,025)	(90,115)
(Losses)/gains on sales of investments based on the carrying value at the previous balance sheet date	(77,833)	32,783
Net movement in investment holding gains	123,076	144,510
Other capital charges	(23)	(19)
Total capital gains on investments held at fair value through profit or loss	45,220	177,274

# Financial Statements – continued

## 4. Income

	2017 £'000	2016 £'000
Income from investments:		
UK dividends	36,092	36,335
Special dividends	11,361	10,886
Property income distribution from UK REITS	1,164	1,339
Overseas dividends	6,393	6,622
Scrip dividends	102	601
	55,112	55,783
Interest receivable and similar income		
Interest from liquidity fund	494	269
Deposit interest	406	615
Underwriting commission	357	181
	1,257	1,065
Total income	56,369	56,848

## 5. Management fee

	2017			2016		
	Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
Management fee	2,173	5,071	7,244	2,279	5,317	7,596

Details of the management fee are given in the Directors' Report on page 25.

## 6. Other administrative expenses

	2017 £'000	2016 £'000
Administration expenses	928	931
Directors' fees <sup>1</sup>	298	275
Savings scheme costs <sup>2</sup>	118	118
Auditors' remuneration for audit services <sup>3</sup>	36	36
Auditors' remuneration for all other services	2	2
	1,382	1,362

<sup>1</sup>Full disclosure is given in the Directors' Remuneration Report on pages 32 and 34.

<sup>2</sup>These amounts were paid to the Manager for the administration of saving scheme products. Includes £19,000 (2016: £19,000) irrecoverable VAT.

<sup>3</sup>Includes £6,000 (2016: £6,000) irrecoverable VAT.

# Financial Statements – continued

## 7. Finance costs

	2017			2016		
	Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
Interest on bank loans and overdrafts	41	97	138	51	121	172
Debenture interest	3,265	7,618	10,883	3,265	7,618	10,883
Amortisation of debenture issue costs	29	68	97	29	67	96
	3,335	7,783	11,118	3,345	7,806	11,151

## 8. Taxation

### (a) Analysis of tax charge in the year

	2017 £'000	2016 £'000
Overseas withholding tax	183	282
Total tax charge for the year	183	282

### (b) Factors affecting the total tax charge for the year

The tax charge for the year is lower (2016: lower) than the Company's applicable rate of corporation tax for the year of 20.00% (2016: 20.16%). The factors affecting the total tax charge for the year are as follows:

	2017			2016		
	Revenue £'000	Capital £'000	Total £'000	Revenue £'000	Capital £'000	Total £'000
Net return on ordinary activities before taxation	49,479	32,364	81,843	49,862	164,236	214,098
Net return on ordinary activities before taxation multiplied by the Company's applicable rate of corporation tax of 20.00% (2016: 20.16%)	9,896	6,473	16,369	10,052	33,110	43,162
Effects of:						
Non taxable scrip dividends	(20)	—	(20)	(121)	—	(121)
Non taxable UK dividends	(8,714)	—	(8,714)	(9,520)	—	(9,520)
Non taxable overseas dividends	(2,056)	—	(2,056)	(1,277)	—	(1,277)
Non taxable capital gains	—	(9,044)	(9,044)	—	(35,755)	(35,755)
Unrelieved expenses	894	2,571	3,465	866	2,645	3,511
Overseas withholding tax	183	—	183	282	—	282
Total tax charge for the year	183	—	183	282	—	282

### (c) Deferred taxation

The Company has an unrecognised deferred tax asset of £43,633,000 (2016: £43,081,000) based on a prospective corporation tax rate of 17% (2016: 18%). The UK Government announced in July 2015 that the corporation tax rate is set to be cut to 19% in 2017 and 18% in 2020. In March 2016 a further cut to 17% in 2020 was announced. These reductions in the standard rate of corporation tax were substantively enacted on 15th September 2016 and became effective from 1st January 2017. The deferred tax asset has arisen due to the cumulative excess of deductible expenses over taxable income. Given the composition of the Company's portfolio, it is not likely that this asset will be utilised in the foreseeable future and therefore no asset has been recognised in the financial statements.

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

# Financial Statements – continued

## 9. Dividends

### (a) Dividends paid and proposed

	2017 £'000	2016 £'000
<b>Dividends paid</b>		
Unclaimed dividends refunded to the Company <sup>1</sup>	(26)	(14)
2016 fourth quarterly dividend of 13.0p (2015: 17.0p) paid to shareholders in May	12,422	16,395
First quarterly dividend of 10.25p (2016: 10.0p) paid to shareholders in August	9,648	9,625
Second quarterly dividend of 10.25p (2016: 10.0p) paid to shareholders in November	9,471	9,625
Third quarterly dividend of 10.25p (2016: 10.0p) paid to shareholders in February	9,049	9,596
<b>Total dividends paid in the year</b>	<b>40,564</b>	<b>45,227</b>
	2017 £'000	2016 £'000
<b>Dividends proposed</b>		
Fourth quarterly dividend declared of 15.25p (2016: 13.0p) payable to shareholders in May	13,265	12,474
<b>Total proposed dividend</b>	<b>13,265</b>	<b>12,474</b>

<sup>1</sup>Represents dividends which remain unclaimed after a period of twelve years and thereby become the property of the Company.

All dividends paid and proposed in the year have been funded from the revenue reserve.

The fourth quarterly dividend declared in respect of the year ended 31st January 2016 amounted to £12,474,000. However, the amount paid amounted to £12,422,000 due to share repurchases after the balance sheet date but prior to the share register record date.

The fourth quarterly dividend has been declared in respect of the year ended 31st January 2017. In accordance with the accounting policy of the Company, this dividend will be reflected in the financial statements for the year ending 31st January 2018.

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

The requirements of Section 1158 are considered on the basis of dividends declared in respect of the financial year as shown below. The revenue available for distribution by way of dividend for the year is £49,296,000 (2016: £49,580,000). The maximum amount of income that the Company is permitted to retain under Section 1158 is £8,455,000 (2015: £8,527,000), calculated as 15% of total income. Therefore the minimum distribution required by way of dividend is £40,841,000 (2015: £41,053,000).

	2017 £'000	2016 £'000
First quarterly dividend of 10.25p (2016: 10.0p) paid to shareholders in August	9,648	9,625
Second quarterly dividend of 10.25p (2016: 10.0p) paid to shareholders in November	9,471	9,625
Third quarterly dividend of 10.25p (2016: 10.0p) paid to shareholders in February	9,049	9,596
Fourth quarterly dividend of 15.25p (2016: 13.0p) payable in May	13,265	12,474
	<b>41,433</b>	<b>41,320</b>

# Financial Statements – continued

## 10. Return per share

	2017 £'000	2016 £'000
Revenue return	49,296	49,580
Capital return	32,364	164,236
Total return	81,660	213,816
Weighted average number of shares in issue during the year	92,666,092	96,340,857
Revenue return per share	53.20p	51.46p
Capital return per share	34.93p	170.47p
Total return per share	88.13p	221.93p

## 11. Investments

	2017 £'000	2016 £'000
Investments listed on a recognised stock exchange	1,699,279	1,666,924
Investments listed on AIM and unlisted investments	87,852	108,698
	1,787,131	1,775,622

	Listed UK £'000	Listed Overseas £'000	AIM and Unlisted £'000	Total £'000
Opening book cost	1,311,138	2,170	66,110	1,379,418
Opening investment holding gains	353,573	43	42,588	396,204
Opening valuation	1,664,711	2,213	108,698	1,775,622
Movements in the year:				
Purchases at cost	705,704	—	21,327	727,031
Sales – proceeds	(701,634)	—	(59,131)	(760,765)
Losses on sales of investments based on the carrying value at the previous balance sheet date	(77,317)	—	(516)	(77,833)
Net movement in investment holding gains and losses	105,645	(43)	17,474	123,076
	1,697,109	2,170	87,852	1,787,131
Closing book cost	1,342,746	2,170	50,960	1,395,876
Closing investment holding gains	354,363	—	36,892	391,255
Total investments held at fair value through profit or loss	1,697,109	2,170	87,852	1,787,131

Stamp duty and brokerage commission on purchases during the year amounted to £3,204,000 (2016: £2,897,000) and £608,000 (2016: £598,000) respectively. Brokerage commission on sales during the year amounted to £635,000 (2016: £756,000).

Investments include Alternative Investment Market stocks which are valued at £84,246,000 (2016: £105,821,000).

During the year, prior year investment holding gains amounting to £128,025,000 have been transferred to gains on sales of investments as disclosed in note 17.

# Financial Statements – continued

## 12. Significant interests

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

Name of company	Country of registration	Class of share	% of class held
Ricardo	UK	Ordinary	5.6
VP	UK	Ordinary	5.4
MP Evans Group	UK	Ordinary	5.1
Morgan Sindall Group	UK	Ordinary	3.1
Polypipe Group	UK	Ordinary	3.1
Young & Co.'s Brewery 'A'	UK	Ordinary	3.1

In addition to the above, the Company has interests of 3% or more in the share capital of another 8 (2016: 11) 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 2017 was £135,911,000 (2016: £161,033,000).

## 13. Current assets

### Debtors

	2017 £'000	2016 £'000
Securities sold awaiting settlement	9,027	3,605
Dividends and interest receivable	1,647	1,987
Overseas tax recoverable	230	574
Other debtors	41	19
	10,945	6,185

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

### Cash and cash equivalents

Cash and cash equivalents comprise bank balances, short term deposits and liquidity funds. The carrying amount of these represents their fair value.

## 14. Creditors: amounts falling due within one year

	2017 £'000	2016 £'000
Securities purchased awaiting settlement	2,261	8,198
Repurchases of the Company's own shares awaiting settlement	7,254	—
Other creditors and accruals	4,900	5,044
	14,415	13,242

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

## Financial Statements – continued

### 15. Creditors: amounts falling due after more than one year

	2017 £'000	2016 £'000
£175 million 6.125% debenture stock <sup>1</sup>	173,726	173,629
£3,850,000 4.25% perpetual debenture stock <sup>2</sup>	3,850	3,850
	177,576	177,479

<sup>1</sup>The £175 million 6.125% debenture stock is repayable at par on 25th February 2030 and is secured by a floating charge over the assets of the Company.

<sup>2</sup>The £3,850,000 4.25% debenture stock is irredeemable and secured by a floating charge over the assets of the Company. The debenture is repayable at 105% if the Company goes into default and the security is enforced.

### 16. Called up share capital

	2017 £'000	2016 £'000
<b>Ordinary shares allotted and fully paid:</b>		
Opening Balance of 95,957,040 ordinary shares of 25p each (2016: 97,704,635) shares excluding shares held in Treasury	23,989	24,426
Repurchase and cancellation of 1,507,822 shares (2016: 1,747,595)	(377)	(437)
Repurchase of 7,468,799 shares into Treasury (2016: nil)	(1,867)	—
Subtotal of 86,980,419 (2016: 95,957,040) shares of 25p each excluding shares held in Treasury	21,745	23,989
7,468,799 (2016: nil) shares held in Treasury	1,867	—
Closing Balance of 94,449,218 (2016: 95,957,040) shares of 25p each including shares held in Treasury	23,612	23,989

During the year, the Company repurchased a total of 8,976,621 shares, amounting to 9.4% of issued share capital at the beginning of the year. Of those shares 1,507,822 (2016: 1,747,595), nominal value £377,000 (2016: £437,000) were repurchased for cancellation, for a total consideration of £25,073,000 (2016: £27,955,000). Following the date of the AGM, when powers were taken to allow repurchased shares to be held in Treasury, 7,468,799 shares were repurchased, for a total consideration of £125,610,000.



# Financial Statements – continued

## 17. Capital and reserves

	Called up share capital £'000	Share premium £'000	Capital redemption reserve £'000	Capital reserves		Revenue reserve <sup>1</sup> £'000	Total £'000
				Gains on sales of investments £'000	Investment holding gains £'000		
Opening balance	23,989	23,459	12,781	1,356,051	396,204	41,246	1,853,730
Net foreign currency losses on cash and cash equivalents	—	—	—	(2)	—	—	(2)
Losses on sales of investments based on the carrying value at the previous balance sheet date	—	—	—	(77,833)	—	—	(77,833)
Net movement in investment holding gains and losses	—	—	—	—	123,076	—	123,076
Transfer on disposal of investments	—	—	—	128,025	(128,025)	—	—
Repurchase of shares into Treasury	—	—	—	(125,610)	—	—	(125,610)
Repurchase and cancellation of the Company's own shares	(377)	—	377	(25,073)	—	—	(25,073)
Management fee and finance costs charged to capital	—	—	—	(12,854)	—	—	(12,854)
Other capital charges	—	—	—	(23)	—	—	(23)
Dividends paid in the year	—	—	—	—	—	(40,564)	(40,564)
Retained revenue for the year	—	—	—	—	—	49,296	49,296
Closing balance	23,612	23,459	13,158	1,242,681	391,255	49,978	1,744,143

<sup>1</sup>This reserve forms the distributable reserve of the Company and may be used to fund distribution of profits to investors via dividend payments.

## 18. Net asset value per share

	2017	2016
Net assets (£'000)	1,744,143	1,853,730
Number of shares in issue	86,980,419	95,957,040
Net asset value per share	2,005.2p	1,931.8p

## 19. Reconciliation of net return on ordinary activities before finance costs and taxation to net cash outflow from operations before dividends and interest

	2017 £'000	2016 £'000
Net return on ordinary activities before finance costs and taxation	92,961	225,249
Less capital return on ordinary activities before finance costs and taxation	(40,147)	(172,042)
Scrip dividends received as income	(102)	(601)
Decrease/(increase) in accrued income and other debtors	318	(800)
Decrease in accrued expenses	(106)	(489)
Management fee charged to capital	(5,071)	(5,317)
Overseas withholding tax	(251)	(510)
Dividends received	(55,055)	(53,827)
Interest received	(944)	(840)
Realised (losses)/gains on foreign currency transactions	(30)	101
Net cash outflow from operations before dividends and interest	(8,427)	(9,076)

# Financial Statements – continued

## 20. Analysis of changes in net debt

	At 31st January 2016 £'000	Cash flow £'000	Other exchange movements £'000	Non cash movements £'000	At 31st January 2017 £'000
Cash at bank and in hand	519	578	(2)	—	1,095
Short term deposits	162,200	(125,000)	—	—	37,200
Cash equivalents: liquidity funds	99,925	—	(162)	—	99,763
<b>Total cash and cash equivalents</b>	<b>262,644</b>	<b>(124,422)</b>	<b>(164)</b>	<b>—</b>	<b>138,058</b>
Debentures falling due after more than five years	(177,479)	—	—	(97)	(177,576)
<b>Closing net funds/(debt)</b>	<b>85,165</b>	<b>(124,422)</b>	<b>(164)</b>	<b>(97)</b>	<b>(39,518)</b>

## 21. Contingent liabilities and capital commitments

At the balance sheet date there were no contingent liabilities or capital commitments (2016: same).

## 22. Related party transactions

Details of the management contract are set out in the Directors' Report on page 25. The management fee payable to the Manager for the year was £7,244,000 (2016: £7,596,000) of which £nil (2016: £nil) was outstanding at the year end.

During the year £118,000 (2016: £118,000) was payable to the Manager for the administration of savings scheme products, of which £8,000 (2016: £8,000) was outstanding at the year end.

Included in administration expenses in note 6 on page 49 are safe custody fees amounting to £27,000 (2016: £30,000) payable to JPMorgan Chase of which £4,000 (2016: £8,000) was outstanding at the year end.

During the year, brokerage commission on dealing transactions amounted to £101,000 (2016: £117,000) was payable to JPMorgan subsidiaries of which £nil (2016: £nil) was outstanding at the year end.

The Company also holds cash in JPMorgan Sterling Liquidity Fund, managed by JPMorgan. At the year end this was valued at £99.8 million (2016: £99.9 million). Income amounting to £494,000 (2016: £269,000) was receivable during the year of which £nil (2016: £nil) was outstanding at the year end.

Handling charges on dealing transactions amounting to £23,000 (2016: £19,000) were payable to JPMorgan Chase during the year of which £4,000 (2016: £3,000) was outstanding at the year end.

At the year end, total cash of £1,095,000 (2016: £519,000) was held with JPMorgan Chase. A net amount of interest of £nil (2016: £800) was receivable by the Company during the year from JPMorgan Chase of which £100 (2016: £nil) was outstanding at the year end.

Full details of Directors' remuneration and shareholdings can be found on page 33 and in note 6 on page 49.

## 23. Disclosures regarding financial instruments measured at fair value

The Company's financial instruments within the scope of FRS 102 that are held at fair value comprise its investment portfolio and derivative financial instruments.

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

**(1) The unadjusted quoted price in an active market for identical assets or liabilities that the entity can access at the measurement date**

The best evidence of fair value is a quoted price for an identical asset in an active market. Quoted in an active market in this context means quoted prices are readily and regularly available and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted price is usually the current bid price.

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

When quoted prices are unavailable, the price of a recent transaction for an identical asset provides evidence of fair value as long as there has not been a significant change in economic circumstances or a significant lapse of time since the transaction took place. If the entity can demonstrate that the last transaction price is not a good estimate of fair value (e.g. because it reflects the amount that an entity would receive or pay in a forced transaction, involuntary liquidation or distress sale), that price is adjusted.

## Financial Statements – continued

### (3) Inputs are unobservable (i.e. for which market data is unavailable) for the asset or liability

If the market for the asset is not active and recent transactions of an identical asset on their own are not a good estimate of fair value, an entity estimates the fair value by using a valuation technique. The objective of using a valuation technique is to estimate what the transaction price would have been on the measurement date in an arm's length exchange motivated by normal business considerations.

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

Details of the valuation techniques used by the Company are given in note 1(b) on page 46.

The following table sets out the fair value measurements using the FRS 102 hierarchy at 31st January.

	2017		2016	
	Assets £'000	Liabilities £'000	Assets £'000	Liabilities £'000
Level 1	1,783,525	—	1,772,744	—
Level 3 <sup>1</sup>	3,606	—	2,878	—
<b>Total</b>	<b>1,787,131</b>	<b>—</b>	<b>1,775,622</b>	<b>—</b>

<sup>1</sup>Consists only of the holding in unquoted stocks of Tennants Consolidated and International Ferro Metals.

There was no transfers between Level 1, 2 and 3 during the year (2016: none). A reconciliation of the fair value measurements using valuation techniques using non-observable data is set out below.

	2017		
	Equity Investments £'000	Fixed Interest Investment £'000	Total £'000
<b>Level 3</b>			
Opening balance	2,784	94	2,878
Change in fair value of unquoted investment during the year	728	—	728
Closing balance	3,512	94	3,606

	2016		
	Equity Investments £'000	Fixed Interest Investment £'000	Total £'000
<b>Level 3</b>			
Opening balance	2,795	94	2,889
Change in fair value of unquoted investment during the year	(11)	—	(11)
Closing balance	2,784	94	2,878

## 24. Financial instruments' exposure to risk and risk management policies

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

These financial risks include market risk (comprising interest rate risk and market price risk), liquidity risk and credit risk. The Directors' policy for managing these risks is set out below. The Company has no significant direct exposure to foreign exchange risk. A proportion of the dividends received by the Company are paid in currencies other than sterling. Therefore a significant movement in exchange rates could impact the portfolio yield, however the Board considers this to be a relatively low risk. The Company Secretary, in close co-operation with the Board and the Manager, co-ordinates the Company's risk management strategy.

# Financial Statements – continued

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

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 UK equity shares and other securities, which are held in accordance with the Company's investment objective;
- cash held within a liquidity fund;
- short term debtors, creditors and cash arising directly from its operations;
- a debenture issued by the Company, the purpose of which is to finance the Company's operations; and
- derivatives, the purpose of which is to effect changes in the level of the Company's gearing.

### (a) Market risk

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

#### (i) Interest rate risk

Interest rate movements may affect the level of income receivable on cash deposits, the liquidity fund and the interest payable on variable rate borrowings when interest rates are reset. There is no 'fair value' interest rate risk attached to the Company's fixed rate debenture in issue, as it is carried in the financial statements at amortised cost.

#### Management of interest rate risk

Liquidity and borrowings are managed with the aim of increasing returns to shareholders. The Company's gearing policy is to limit gearing within the range of 10% net cash to 20% geared where gearing is defined as investments expressed as a percentage of total net assets.

#### 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 Statement of Financial Position at amortised cost rather than fair value. Hence movement in interest rates will not affect equity but may have an impact on the share price and discount which is not likely to be material.

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

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

	2017 £'000	2016 £'000
Exposure to floating interest rates:		
Cash at bank and short term deposits	38,295	162,719
JPMorgan Sterling Liquidity Fund	99,763	99,925
<b>Total exposure</b>	<b>138,058</b>	<b>262,644</b>

Interest receivable on cash balances, or paid on overdrafts, is at a margin below or above LIBOR respectively (2016: same).

#### Interest rate sensitivity

The following table illustrates the sensitivity of the return after taxation for the year and net assets to a 1% (2016: 1%) increase or decrease in interest rates in regards to the Company's monetary financial assets and financial liabilities. This level of change is considered to be a reasonable illustration based on observation of current market conditions. The sensitivity analysis is based on the Company's monetary financial instruments held at the balance sheet date with all other variables held constant.

## Financial Statements – continued

	2017		2016	
	1% Increase in rate £'000	1% Decrease in rate £'000	1% Increase in rate £'000	1% Decrease in rate £'000
Statement of Comprehensive Income – return after taxation				
Revenue return	1,381	(1,381)	2,626	(2,626)
Total return after taxation	1,381	(1,381)	2,626	(2,626)
Net assets	1,381	(1,381)	2,626	(2,626)

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

### (ii) Other price risk

Other 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 other 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.

#### Other price risk exposure

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

	2017 £'000	2016 £'000
Investments held at fair value through profit or loss	1,787,131	1,775,622

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

#### Concentration of exposure to other price risk

An analysis of the Company's investments is given on pages 14 to 18. This shows that the majority of the investments' value is in the UK. Accordingly there is a concentration of exposure to that country. However it should be noted that an investment may not be entirely exposed to the economic conditions in its country of domicile or of listing.

#### Other price risk sensitivity

The following table illustrates the sensitivity of the return after taxation for the year and net assets to an increase or decrease of 10% (2016: 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, adjusting for changes in the management fee but with all other variables held constant.

	2017		2016	
	10% Increase in fair value £'000	10% Decrease in fair value £'000	10% Increase in fair value £'000	10% Decrease in fair value £'000
Statement of Comprehensive Income – return after taxation				
Revenue return	(268)	268	(266)	266
Capital return	178,088	(178,088)	176,941	(176,941)
Total return after taxation	177,820	(177,820)	176,675	(176,675)
Net assets	177,820	(177,820)	176,675	(176,675)

## Financial Statements – continued

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

#### (b) Liquidity risk

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

#### Management of the risk

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

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

#### Liquidity risk exposure

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

	2017			Total £'000
	Three months or less £'000	More than three months but not more than one year £'000	More than one year £'000	
<b>Creditors: amounts falling due within one year</b>				
Securities purchased awaiting settlement	2,261	—	—	2,261
Repurchase of the Company's own shares awaiting settlement	7,254	—	—	7,254
Other creditors and accruals	186	—	—	186
Debenture stock – interest <sup>1</sup>	5,441	5,441	—	10,882
<b>Creditors: amounts falling due after more than one year</b>				
Debenture stock – principal <sup>2</sup>	—	—	178,850	178,850
Debenture stock – interest <sup>1</sup>	—	—	136,306	136,306
	15,142	5,441	315,156	335,739
	2016			
	Three months or less £'000	More than three months but not more than one year £'000	More than one year £'000	Total £'000
<b>Creditors: amounts falling due within one year</b>				
Securities purchased awaiting settlement	8,198	—	—	8,198
Other creditors and accruals	292	—	—	292
Debenture stock – interest <sup>1</sup>	5,441	5,441	—	10,882
<b>Creditors: amounts falling due after more than one year</b>				
Debenture stock – principal <sup>2</sup>	—	—	178,850	178,850
Debenture stock – interest <sup>1</sup>	—	—	147,188	147,188
	13,931	5,441	326,038	345,410

<sup>1</sup>The liabilities shown above represent future contractual payments and therefore differ from the amounts shown in the statement of Financial Position.

<sup>2</sup>Includes £3,850,000 4.25% debenture stock which is irredeemable and secured by a floating charge over the assets of the Company.

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

## Financial Statements – continued

### (c) Credit risk

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

#### Management of credit risk

##### *Portfolio dealing*

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

##### *Cash and cash equivalents*

Counterparties are subject to regular credit analysis by the Manager and deposits can only be placed with counterparties that have been approved by JPMAM's Counterparty Risk Group. The Board regularly reviews the counterparties used by the Manager. At the year end a cash balance of £29.5 million was placed with BRED Banque Populaire and a cash balance of £7.7 million was placed with Crédit Agricole, in line with the Board's concentration guidelines. The JPMorgan Sterling Liquidity Fund has a AAA rating.

##### *Exposure to JPMorgan Chase*

JPMorgan Chase Bank is the custodian of the Company's assets. The custody agreement grants a general lien over the securities credited to the securities account. The Company's assets are segregated from JPMorgan Chase Bank's own trading assets and are therefore protected from creditors in the event that JPMorgan Chase Bank were to cease trading. However, no absolute guarantee can be given to investors on the protection of all of the assets of the Company.

#### Credit risk exposure

The amounts shown in the Statement of Financial Position under debtors and cash and cash equivalents represent the maximum exposure to credit risk at the current and comparative year ends.

### (d) Fair values of financial assets and financial liabilities

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

	Carrying value		Fair value	
	2017 £'m	2016 £'m	2017 £'m	2016 £'m
£175 million 6.125% debenture stock 25th February 2030	173.7	173.6	245.2	238.1
£3.85 million 4.25% perpetual debenture stock	3.9	3.9	5.7	4.4
	177.6	177.5	250.9	242.5

# Financial Statements – continued

## 25. Capital management policies and procedures

The Company's debt and capital structure comprises the following:

	2017 £'000	2016 £'000
<b>Debt</b>		
£175 million 6.125% debenture stock 25th February 2030	173,726	173,629
£3.85 million 4.25% perpetual debenture stock	3,850	3,850
	177,576	177,479
<b>Equity</b>		
Called up share capital	23,612	23,989
Reserves	1,720,531	1,829,741
	1,744,143	1,853,730
<b>Total debt and equity</b>	<b>1,921,719</b>	<b>2,031,209</b>

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 gearing policy is to operate within a range of 10% net cash to 20% geared in normal market conditions.

	2017 £'000	2016 £'000
Investments held at fair value through profit or loss	1,787,131	1,775,622
Net assets	1,744,143	1,853,730
Gearing/(net cash)	2.5%	(4.2)%

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 opportunity for issues of new shares, including issues from Treasury; and
- the level of dividend distributions in excess of that which is required to be distributed.

## 26. Subsequent events

The Directors have evaluated the period since the year end and have not noted any subsequent events.



# Regulatory Disclosures

## ALTERNATIVE INVESTMENT FUND MANAGERS DIRECTIVE ('AIFMD') DISCLOSURES (UNAUDITED)

### Leverage

For the purposes of the Alternative Investment Fund Managers Directive ('AIFMD'), leverage is any method which increases the Company's exposure, including the borrowing of cash and the use of derivatives. It is expressed as a ratio between the Company's exposure and its net asset value and is calculated on a gross and a commitment method in accordance with AIFMD. Under the gross method, exposure represents the sum of the Company's positions without taking into account any hedging and netting arrangements. Under the commitment method, exposure is calculated after certain hedging and netting positions are offset against each other.

### Alternative Investment Fund Managers — Leverage

The Company's maximum and actual leverage levels at 31st January 2017 are shown below:

	Gross Method	Commitment Method
Leverage Exposure		
Maximum limit	200%	200%
Actual	109%	110%

### JPMF Remuneration

The AIFMD requires certain disclosures to be made with regard to the remuneration policy of the Company's AIFM (the 'AIFM Remuneration Policy').

Details of JPMF's AIFM Remuneration Policy are disclosed on the Company's website at [www.mercantileit.co.uk](http://www.mercantileit.co.uk)

This disclosure has been prepared in accordance with the AIFMD, the European Commission Delegated Regulation supplementing the AIFMD, the 'Guidelines on Sound Remuneration Policies' under the AIFMD issued by the European Securities and Markets Authority and the Financial Conduct Authority Handbook (SYSC 19B: The AIFM Remuneration Code and FUND 3.3).

### JPMF Remuneration Policy

The current remuneration policy for the EMEA Global Investment business of J.P. Morgan can be found at <https://am.jpmorgan.com/gb/en/asset-management/gim/adv/legal/emea-remuneration-policy>. This policy includes details of the alignment with risk management, the financial and non-financial criteria used to evaluate performance and the measures adopted to avoid or manage conflicts of interest.

### JPMF Quantitative Disclosures

Disclosure in accordance with FUND 3.3.5, Article 22(2)e and 22(2)f of the AIFMD and Article 107 of the Delegated Regulation are disclosed on the Company's website at [www.mercantileit.co.uk](http://www.mercantileit.co.uk)

## SECURITIES FINANCING TRANSACTIONS REGULATION ('SFTR') DISCLOSURES (UNAUDITED)

The Company does not engage in Securities Financing Transactions (as defined in Article 3 of Regulation (EU) 2015/2365, securities financing transactions include repurchase transactions, securities or commodities lending and securities or commodities borrowing, buy-selling back transactions or sell-buy back transactions and margin lending transactions) or Total Return Swaps. Accordingly, disclosures required by Article 13 of the Regulation are not applicable for the year ended 31st January 2017.

# Shareholder Information

## Notice of Annual General Meeting

Notice is hereby given that the one hundred and thirty first Annual General Meeting of The Mercantile Investment Trust plc will be held at Trinity House, Tower Hill, London EC3N 4DH on Wednesday, 24th May 2017 at 12.00 noon for the following purposes:

1. To receive the Directors' Report, the Annual Accounts and the Auditors' Report for the year ended 31st January 2017.
2. To approve the Company's Remuneration Policy.
3. To approve the Directors' Remuneration Report for the year ended 31st January 2017.
4. To reappoint Angus Gordon Lennox as a Director of the Company.
5. To reappoint Sandy Nairn as a Director of the Company.
6. To reappoint Ian Russell as a Director of the Company.
7. To reappoint Helen James as a Director of the Company.
8. To reappoint Jeremy Tigue as a Director of the Company.
9. To reappoint Harry Morley as a Director of the Company.
10. To reappoint PricewaterhouseCoopers LLP as auditors to the Company and to authorise the Directors to determine their remuneration.

### Special Business:

To consider the following resolution:

#### Adoption of new Articles of Association – Special Resolution

11. THAT the Articles of Association produced to the meeting and initialled by the Chairman of the meeting for the purpose of identification be adopted as the new Articles of Association of the Company in the substitution for, and to the exclusion of, the existing Articles of Association with effect from the conclusion of the 2017 Annual General Meeting.

#### Authority to allot new shares – Ordinary Resolution

12. THAT the Directors of the Company be and they are hereby generally and unconditionally authorised, (in substitution of any authorities previously granted to the Directors), pursuant to and in accordance with Section 551 of the Companies Act 2006 (the 'Act') to exercise all the powers of the Company to allot shares in the Company and to grant rights to subscribe for, or to convert any security into, shares in the Company ('rights') up to an aggregate nominal amount of £1,064,544, representing approximately 5% of the Company's issued share capital as at the date of the passing of this resolution, provided that this authority shall expire at the conclusion of the Annual General Meeting of the Company held in 2018 unless renewed at a general meeting prior to such time, save

that the Company may before such expiry make offers or agreements which would or might require shares to be allotted or Rights to be granted after such expiry and so that the Directors of the Company may allot shares and grant Rights in pursuance of such offers or agreements as if the authority conferred hereby had not expired.

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

13. THAT subject to the passing of Resolution 12 set out above, the Directors of the Company be and they are hereby empowered pursuant to Sections 570 and 573 of the Act to allot equity securities (within the meaning of Section 560 of the Act) for cash pursuant to the authority conferred by Resolution 12 as if Section 561(1) of the Act did not apply to any such allotment, provided that this power shall be limited to the allotment of equity securities for cash up to an aggregate nominal amount of £1,064,544 representing approximately 5% of the issued share capital as at the date of the passing of this resolution at a price of not less than the net asset value per share and shall expire upon the expiry of the general authority conferred by Resolution 12 above, save that the Company may before such expiry make offers or agreements which would or might require equity securities to be allotted after such expiry and so that the Directors of the Company may allot equity securities in pursuance of such offers or agreements as if the power conferred hereby had not expired.

#### Authority to repurchase the Company's shares – Special Resolution

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

##### PROVIDED ALWAYS THAT

- (i) the maximum number of ordinary shares hereby authorised to be purchased shall be 12,781,006 or if less, that number of ordinary shares which is equal to 14.99% of the Company's issued share capital as at the date of the passing of this Resolution;
- (ii) the minimum price which may be paid for an ordinary share shall be 25p;
- (iii) the maximum price which may be paid for an ordinary share or unit shall be an amount equal to the highest of:
  - (a) 105% of the average of the middle market quotations for an ordinary share taken from and calculated by reference to the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the ordinary share is contracted to be purchased; or
  - (b) the price of the last independent trade; or
  - (c) the highest current independent bid;

## Shareholder Information – continued

- (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 23rd November 2018 unless the authority is renewed at the Company's Annual General Meeting in 2018 or at any other general meeting prior to such time; and
- (vi) the Company may make a contract to purchase ordinary shares under the authority hereby conferred prior to the expiry of such authority which contract will or may be executed wholly or partly after the expiry of such authority and may make a purchase of ordinary shares pursuant to any such contract.

### Approval of dividend policy – Ordinary Resolution

15. THAT the shareholders approve the Company's dividend policy to continue to pay four quarterly interim dividends, which in the year under review totalled 46.0 pence per share.

By order of the Board  
Jonathan Latter  
For and on behalf of  
JPMorgan Funds Limited,  
Company Secretary

13th April 2017

### Notes

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

1. A member entitled to attend and vote at the Meeting may appoint another person(s) (who need not be a member of the Company) to exercise all or any of his rights to attend, speak and vote at the Meeting. A member can appoint more than one proxy in relation to the Meeting, provided that each proxy is appointed to exercise the rights attaching to different shares held by him.
2. A proxy does not need to be a member of the Company but must attend the Meeting to represent you. Your proxy could be the Chairman, another director of the Company or another person who has agreed to attend to represent you. Details of how to appoint the Chairman or another person(s) as your proxy or proxies using the proxy form are set out in the notes to the proxy form. If a voting box on the proxy form is left blank, the proxy or proxies will exercise his/their discretion both as to how to vote and whether he/they abstain(s) from voting. Your proxy must attend the Meeting for your vote to count. Appointing a proxy or proxies does not preclude you from attending the Meeting and voting in person.
3. Any instrument appointing a proxy, to be valid, must be lodged in accordance with the instructions given on the proxy form, no later than 12.00 p.m. two business days prior to the Meeting (i.e. excluding weekends and bank holidays).
4. You may change your proxy instructions by returning a new proxy appointment. The deadline for receipt of proxy appointments also applies in relation to amended instructions. Any attempt to terminate or amend a proxy appointment received after the relevant deadline will be disregarded. Where two or more valid separate appointments of proxy are received in respect of the same share in respect of the same Meeting, the one which is last received (regardless of its date or the date of its signature) shall be treated as replacing and revoking the other or others as regards that share; if the Company is unable to determine which was last received, none of them shall be treated as valid in respect of that share.
5. To be entitled to attend and vote at the Meeting (and for the purpose of the determination by the Company of the number of votes they may cast), members must be entered on the Company's register of members as at 6.30 p.m. two business days prior to the Meeting (the 'specified time'). If the Meeting is adjourned to a time not more than 48 hours after the specified time applicable to the original Meeting, that time will also apply for the purpose of determining the entitlement of members to attend and vote (and for the purpose of determining the number of votes they may cast) at the adjourned Meeting. If however the Meeting is adjourned for a longer period then, to be so entitled, members must be entered on the Company's register of members as at 6.30 p.m. two business days prior to the adjourned Meeting or, if the Company gives notice of the adjourned Meeting, at the time specified in that notice. Changes to entries on the register after this time shall be disregarded in determining the rights of persons to attend or vote at the meeting or adjourned meeting.
6. Entry to the Meeting will be restricted to shareholders and their proxy or proxies, with guests admitted only by prior arrangement.

## Shareholder Information – continued

7. A corporation, which is a shareholder, may appoint an individual(s) to act as its representative(s) and to vote in person at the Meeting (see instructions given on the proxy form). In accordance with the provisions of the Companies Act 2006, each such representative(s) may exercise (on behalf of the corporation) the same powers as the corporation could exercise if it were an individual member of the Company, provided that they do not do so in relation to the same shares. It is therefore no longer necessary to nominate a designated corporate representative. Representatives should bring to the meeting evidence of their appointment, including any authority under which it is signed.
8. Members that satisfy the thresholds in Section 527 of the Companies Act 2006 can require the Company to publish a statement on its website setting out any matter relating to: (a) the audit of the Company's accounts (including the Auditors' report and the conduct of the audit) that are to be laid before the AGM; or (b) any circumstances connected with an Auditor of the Company ceasing to hold office since the previous AGM; which the members propose to raise at the meeting. The Company cannot require the members requesting the publication to pay its expenses. Any statement placed on the website must also be sent to the Company's Auditors no later than the time it makes its statement available on the website. The business which may be dealt with at the AGM includes any statement that the Company has been required to publish on its website pursuant to this right.
9. Pursuant to Section 319A of the Companies Act 2006, the Company must cause to be answered at the AGM any question relating to the business being dealt with at the AGM which is put by a member attending the meeting except in certain circumstances, including if it is undesirable in the interests of the Company or the good order of the meeting or if it would involve the disclosure of confidential information.
10. Under sections 338 and 338A of the 2006 Act, members meeting the threshold requirements in those sections have the right to require the Company: (i) to give, to members of the Company entitled to receive notice of the Meeting, notice of a resolution which those members intend to move (and which may properly be moved) at the Meeting; and/or (ii) to include in the business to be dealt with at the Meeting any matter (other than a proposed resolution) which may properly be included in the business at the Meeting. A resolution may properly be moved, or a matter properly included in the business unless: (a) (in the case of a resolution only) it would, if passed, be ineffective (whether by reason of any inconsistency with any enactment or the Company's constitution or otherwise); (b) it is defamatory of any person; or (c) it is frivolous or vexatious. A request made pursuant to this right may be in hard copy or electronic form, must identify the resolution of which notice is to be given or the matter to be included in the business, must be accompanied by a statement setting out the grounds for the request, must be authenticated by the person(s) making it and must be received by the Company not later than the date that is six clear weeks before the Meeting, and (in the case of a matter to be included in the business only) must be accompanied by a statement setting out the grounds for the request.
11. A copy of this notice has been sent for information only to persons who have been nominated by a member to enjoy information rights under Section 146 of the Companies Act 2006 (a 'Nominated Person'). The rights to appoint a proxy can not be exercised by a Nominated Person: they can only be exercised by the member. However, a Nominated Person may have a right under an agreement between him and the member by whom he was nominated to be appointed as a proxy for the Meeting or to have someone else so appointed. If a Nominated Person does not have such a right or does not wish to exercise it, he may have a right under such an agreement to give instructions to the member as to the exercise of voting rights.
12. In accordance with Section 311A of the Companies Act 2006, the contents of this notice of meeting, details of the total number of shares in respect of which members are entitled to exercise voting rights at the AGM, the total voting rights members are entitled to exercise at the AGM and, if applicable, any members' statements, members' resolutions or members' matters of business received by the Company after the date of this notice will be available on the Company's website [www.mercantileit.co.uk](http://www.mercantileit.co.uk).
13. The register of interests of the Directors and connected persons in the share capital of the Company and the Directors' letters of appointment are available for inspection at the Company's registered office during usual business hours on any weekday (Saturdays, Sundays and public holidays excepted). It will also be available for inspection at the Annual General Meeting. No Director has any contract of service with the Company.
14. You may not use any electronic address provided in this Notice of meeting to communicate with the Company for any purposes other than those expressly stated.
15. As an alternative to completing a hard copy Form of Proxy/Voting Instruction Form, you can appoint a proxy or proxies electronically by visiting [www.sharevote.co.uk](http://www.sharevote.co.uk). You will need your Voting ID, Task ID and Shareholder Reference Number (this is the series of numbers printed under your name on the Form of Proxy/Voting Instruction Form). Alternatively, if you have already registered with Equiniti Limited's online portfolio service, Shareview, you can submit your Form of Proxy at [www.shareview.co.uk](http://www.shareview.co.uk). Full instructions are given on both websites.
16. As at 5th April 2017 (being the latest business day prior to the publication of this Notice), the Company's issued share capital consists of 94,449,218 Ordinary shares (of which 9,285,667 are held in Treasury, representing 10.9% of the shares in issue), carrying one vote each. Therefore the total voting rights in the Company are 85,163,551.
17. A copy of the current articles of association of the Company and the proposed new articles of association of the Company will be available for inspection during normal business hours (Saturdays, Sundays and public holidays excepted) at the offices of JPMorgan Funds Limited, 60 Victoria Embankment, London EC4Y 0JP, from the date of the Annual Report in which this notice is included up until the close of the Annual General Meeting. Copies will also be available at Trinity House, Tower Hill, London EC3N 4DH, being the place of the Annual General Meeting, for 15 minutes prior to, and during, the meeting.

### 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.

# Shareholder Information – continued

## Appendix to Notice of Meeting

Resolution 11 seeks approval from shareholders to adopt new articles of association for the Company (the 'New Articles'). The principal changes proposed to be introduced in the New Articles and their effects are set out below.

### 1. The Alternative Investment Fund Managers Directive (2011/61/EU) ('AIFMD') and the Alternative Investment Fund Managers Regulations 2013 (SI 2013/1773) (the 'AIFM Regulations')

The Board is proposing to make amendments to the current articles of association of the Company (the 'Existing Articles') in response to the AIFMD and all applicable rules and regulations implementing that Directive. The proposed new provisions are as follows:

- 1.1. The Existing Articles will be amended to provide that the net asset value per share of the Company shall be calculated at least annually and be disclosed to shareholders from time to time in such manner as may be determined by the Board. The amendment will have no bearing on current practice and simply articulates the minimum requirements of the AIFM Regulations.
- 1.2. The AIFM Regulations require that prior to any new or existing investor making an investment in the Company certain prescribed information is to be made available to them. Therefore, the New Articles will include language with the effect that such information shall be made available to prospective and existing shareholders in such manner as may be determined by the Board from time to time (including, in certain cases, on the Company's website or by electronic notice).
- 1.3. The valuation of the Company's assets will be performed in accordance with prevailing accounting standards, in line with guidance from the Financial Conduct Authority. This reflects best practice and has no bearing on current practice and simply articulates the minimum requirements of the AIFM Regulations.
- 1.4. The Existing Articles will be amended to provide that the Company's annual report and accounts may be prepared either in accordance with generally acceptable accounting principles of the United Kingdom or such other international accounting standards as may be permitted under the law of England and Wales. The amendment will have no bearing on current practice and simply articulates the minimum requirements of the AIFM Regulations.

### 2. Removal of requirement for Directors to hold ordinary shares of the Company as a qualification requirement

The Existing Articles will be amended to remove the requirement that in order to qualify as a Director, a Director is required to hold (alone and not jointly with another) ordinary shares in the Company of the nominal amount of £125 or shares in the Company of any other class of the nominal amount of £500.

### 3. Increase in the cap on annual aggregate Directors' fees

- 3.1. The Existing Articles will be amended to provide that the aggregate fees that the Directors will be paid out of the funds of the Company by way of remuneration for their services as Directors will not exceed £400,000 per annum (or such larger sum as the Company may by ordinary resolution determine).
- 3.2. Associated with the calculation of the aggregate annual fees paid to Directors, the Existing Articles have been amended to clarify that certain expenses properly incurred by the Directors in connection with their attendance at relevant meetings and special remuneration paid to Directors in relation to the performance of services that the other Directors consider go beyond the ordinary duties of a Director, are to be excluded for the purposes of calculating such aggregate annual fees.

### 4. Investments

- 4.1. The Existing Articles have been amended to clarify the value of investment that the Directors may permit to be made in any one company or body. The amendment is primarily to provide clarification and the overall principle remains the same i.e. subject to certain exceptions, the Directors shall not make any investment in any one company or body with a value in excess of 3% of the gross assets of the Company at the time of investment save that the Directors may, in respect of up to a maximum of 40% of the gross assets of the Company at the time of investment, make an investment in any one company or body with a value of up to 8% of the gross assets of the Company at the time of investment. We have clarified that the relevant valuation will be one based on the Company's usual accounting policies and procedures.
- 4.2. In addition, the Existing Articles will be amended to provide that the investment restriction outlined above shall not apply to investments by the Company in certain money market funds.

# Shareholder Information – continued

## 5. Distributions out of capital reserves

The statutory rules governing investment trusts were amended in 2012. In particular, the rule which prohibited an investment trust from distributing any surplus arising from the realisation of its investments was repealed. In compliance with the previous statutory regime, the Company has provisions in the Existing Articles which expressly prohibit the distribution of any surplus arising from the realisation of any investment. In the light of the amended statutory rules, the Board no longer considers it appropriate to have such a prohibition in the Company's articles of association and therefore proposes that it is removed. The New Articles, if adopted, remove this prohibition.

The Board believes that the removal of this restriction will give the Company greater flexibility in the long term as it will enable the Company to make distributions from any surplus arising from the realisation of any investment. However, the Board has no intention of exercising this authority at the current time.

## 6. International tax regimes requiring the exchange of information

The Board is proposing to include provisions in the New Articles to provide the Company with the ability to require shareholders to co-operate in respect of the exchange of information to comply with the Company's international tax reporting obligations.

The Hiring Incentives to Restore Employment Act 2010 of the United States of America commonly known as the Foreign Account Tax Compliance Act and all associated regulations and official guidance ('FATCA') imposes a system of information reporting on certain entities including foreign financial institutions such as the Company following the enactment of the UK International Tax Compliance (United States of America) Regulations 2013 on 1st September 2013. These regulations have now been replaced by the International Tax Compliance Regulations 2015 (the 'Regulations').

The Existing Articles will be amended to provide the Company with the ability to require shareholders to co-operate with it in ensuring that the Company is able to comply with its obligations under the Regulations in order to avoid being deemed to be a 'Non-participating Financial Institution' for the purposes of FATCA and consequently having to pay withholding tax to the US Internal Revenue Service. The Existing Articles will also be amended to ensure that the Company will not be liable for any monies that become subject to a deduction or withholding relating to FATCA, as such liability would be to the detriment of shareholders as a whole.

The Regulations also include the automatic exchange of information regimes being brought in by the new tax regulation under the OECD (Organisation for Economic Co-operation and Development) Common Reporting Standard for Automatic Exchange of Financial Account Information (the 'Common Reporting Standard') which will require investment trust companies to provide personal information to HMRC on certain investors who purchase shares in investment trusts. As a result, the Company will have to provide information annually to the local tax authority on the tax residency of a number of non-UK based certified shareholders and corporate entities.

Therefore, the Existing Articles will also be amended in order to provide the Company with the ability to require shareholders to co-operate in respect of these broader obligations including its obligations under the OECD and FATCA.

## 7. Vacation of office by Directors

Finally, the Board is proposing to amend the provision in the Existing Articles that provides for automatic termination of a Director's appointment in circumstances where the Director has been suffering mental ill health and has been admitted to hospital in pursuance of an application for admission for treatment under the Mental Health Act 1983 or, in Scotland, an application for admission under the Mental Health (Scotland) Act 1984 or a court order has been made concerning a mental disorder for the Director's detention or for the appointment of a guardian or other person to exercise powers with respect to his property or affairs. This is in response to developments in mental health legislation and reflects the position in the model articles for public companies as set out in the Companies (Model Articles) Regulations 2008/3229.

# Shareholder Information – continued

## Glossary of Terms and Definitions

### Return on Net Assets

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

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

### Return to Shareholders

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

### Benchmark Return

Total return on the benchmark, on a closing-market value to closing-market value basis, assuming that all dividends received were reinvested, without transaction costs, into 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 'track' this index and consequently, there may be some divergence between the Company's performance and that of the benchmark.

### Ongoing Charges

The Ongoing Charges represent the Company's management fee and all other operating expenses excluding finance costs payable, expressed as a percentage of the average of the daily net assets during the year and is calculated in accordance with guidance issued by the Association of Investment Companies.

### Gearing/(Net Cash)

Gearing represents the excess amount above shareholders' funds of total investments, expressed as a percentage of the shareholders' funds. Previously gearing represented the excess amount above shareholders' funds of total assets expressed as a percentage of shareholders' funds. Total assets included total investments and net current assets/liabilities less cash/cash equivalents and excluding bank loans of less than one year. If the amount calculated is negative, this is shown as a 'net cash' position.

### Share Price Discount/Premium to Net Asset Value ('NAV') per share

If the share price of an investment trust is lower than the NAV per share, the shares are said to be trading at a discount. The discount

is shown as a percentage of the NAV per share. The opposite of a discount is a premium. It is more common for an investment trust's shares to trade at a discount than at a premium.

### Fair Value

The fair value of the Company's debentures is calculated using a discounted cash flow technique which applies the yield from a similarly dated gilt to the debentures issued by the Company and adds to that a margin based on the five year average for the AA Barclays Sterling Corporate Bond spread.

For the £175 million debenture, the Company takes the yield on 4.75% Treasury Gilt 07/12/2030. For the £3.85 million perpetual debenture, the Company applies the yield on 3.50% War Loan.

The margin applied on the five year average for the AA Barclays Sterling Corporate Bond spread at 31st January 2017 was 1.00%.

### Performance Attribution

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

### Performance Attribution Definitions:

#### Asset Allocation

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

#### Stock Selection

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

#### Cost of Gearing Effect

Measures the impact on relative performance arising from the cost of borrowings.

#### Cash Effect

Measures the impact on relative performance arising from holding cash balances.

#### Effect of Management Fee/Other Expenses

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

#### Interest Expense – cost of debenture

The payment of interest has a negative effect on relative performance.

#### Repurchase of shares

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

# Shareholder Information – continued

You can invest in a J.P. Morgan investment trust through the following;

## 1. Directly from J.P. Morgan

### Investment Account

The Company's shares are available in the J.P. Morgan Investment Account, which facilitates both regular monthly investments and occasional lump sum investments in the Company's ordinary shares. Shareholders who would like information on the Investment Account should call J.P. Morgan Asset Management free on 0800 20 40 20 or visit its website at [am.jpmorgan.co.uk/investor](http://am.jpmorgan.co.uk/investor)

### Stocks & Shares Individual Savings Accounts (ISA)

The Company's shares are eligible investments within a J.P. Morgan ISA. For the 2016/17 tax year, from 6th April 2016 and ending 5th April 2017, the total ISA allowance is £15,240. The shares are also available in a J.P. Morgan Junior ISA. Details are available from J.P. Morgan Asset Management free on 0800 20 40 20 or via its website at [am.jpmorgan.co.uk/investor](http://am.jpmorgan.co.uk/investor)

## 2. Via a third party provider

Third party providers include;

AJ Bell	Interactive Investor
Alliance Trust Savings	James Brearley
Barclays Stockbrokers	James Hay
Bestinvest	Selftrade
Charles Stanley Direct	TD Direct
FundsNetwork	The Share Centre
Hargreaves Lansdown	

Please note this list is not exhaustive and the availability of individual trusts may vary depending on the provider. These websites are third party sites and J.P. Morgan Asset Management does not endorse or recommend any. Please observe each site's privacy and cookie policies as well as their platform charges structure.

## 3. Through a professional adviser

Professional advisers are usually able to access the products of all the companies in the market and can help you find an investment that suits your individual circumstances. An adviser will let you know the fee for their service before you go ahead. You can find an adviser at [unbiased.co.uk](http://unbiased.co.uk)

You may also buy investment trusts through stockbrokers, wealth managers and banks.

To familiarise yourself with the Financial Conduct Authority (FCA) adviser charging and commission rules, visit [fca.org.uk](http://fca.org.uk)

## Financial Conduct Authority

### Beware of share fraud



In association with  
**icsa**  
Registrars  
Group

**Fraudsters use persuasive and high-pressure tactics to lure investors into scams. They may offer to sell shares that turn out to be worthless or non-existent, or to buy shares at an inflated price in return for an upfront payment. While high profits are promised, if you buy or sell shares in this way you will probably lose your money.**

#### How to avoid share fraud

- 1 Keep in mind that firms authorised by the FCA are unlikely to contact you out of the blue with an offer to buy or sell shares.
- 2 Do not get into a conversation, note the name of the person and firm contacting you and then end the call.
- 3 Check the Financial Services Register from [www.fca.org.uk](http://www.fca.org.uk) to see if the person and firm contacting you is authorised by the FCA.
- 4 Beware of fraudsters claiming to be from an authorised firm, copying its website or giving you false contact details.
- 5 Use the firm's contact details listed on the Register if you want to call it back.
- 6 Call the FCA on **0800 111 6768** if the firm does not have contact details on the Register or you are told they are out of date.
- 7 Search the list of unauthorised firms to avoid at [www.fca.org.uk/scams](http://www.fca.org.uk/scams).
- 8 Consider that if you buy or sell shares from an unauthorised firm you will not have access to the Financial Ombudsman Service or Financial Services Compensation Scheme.
- 9 Think about getting independent financial and professional advice before you hand over any money.
- 10 **Remember:** if it sounds too good to be true, it probably is!

#### Report a scam

If you are approached by fraudsters please tell the FCA using the share fraud reporting form at [www.fca.org.uk/scams](http://www.fca.org.uk/scams), where you can find out more about investment scams.

You can also call the FCA Consumer Helpline on **0800 111 6768**.

If you have already paid money to share fraudsters you should contact Action Fraud on **0300 123 2040**.

**5,000 people contact the Financial Conduct Authority about share fraud each year, with victims losing an average of £20,000**



# Information about the Company

## Financial Calendar

Financial year end	31st January
Final results announced	March/April
Half year end	31st July
Half year results announced	September
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
Interest on 6.125% debenture paid	25th February, 25th August
Annual General Meeting	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. In April 2008, the Company adopted its present name, The Mercantile Investment Trust plc.

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

## 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 Scotsman and on the JPMorgan internet site at [www.mercantileit.co.uk](http://www.mercantileit.co.uk), where the share price is updated every fifteen minutes during trading hours.

## Website

[www.mercantileit.co.uk](http://www.mercantileit.co.uk)

## Share Transactions

The Company's shares may be dealt in directly through a stockbroker or professional adviser acting on an investor's behalf. They may also be purchased and held through the J.P. Morgan Investment Account, J.P. Morgan ISA and J.P. Morgan Junior ISA. These products are all available on the online service at [jpmorgan.co.uk/online](http://jpmorgan.co.uk/online)

## Dividend Reinvestment Plan

The Company operates a dividend reinvestment plan. For further information please contact the Registrars (details below).

## Manager and Secretary

JPMorgan Funds Limited

## Company's Registered Office

60 Victoria Embankment  
London EC4Y 0JP  
Telephone number: 020 7742 4000

Please contact Juliet Dearlove for company secretarial and administrative matters.

## Depository

BNY Mellon Trust & Depository (UK) Limited  
BNY Mellon Centre  
160 Queen Victoria Street  
London EC4V 4LA

The Depository has appointed JPMorgan Chase Bank, N.A. as the Company's custodian.

## Registrars

Equiniti Limited  
Reference 1101  
Aspect House  
Spencer Way  
Lancing  
West Sussex BN99 6DA  
Telephone number: 0371 384 2329

Lines open 8.30 a.m. to 5.30 p.m. Monday to Friday. Calls to the helpline will cost no more than a national rate call to a 01 or 02 number. Callers from overseas should dial +44 121 415 0225.

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](http://www.shareview.co.uk).

## Independent Auditors

PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
7 More London Riverside  
London SE1 2RT

## Brokers

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

Winterflood Securities Limited  
The Atrium Building  
Cannon Bridge House  
London EC4R 2GA

## Savings Product Administrators

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



The Association of  
Investment Companies

A member of the AIC

J.P. Morgan Helpline  
Freephone 0800 20 40 20 or +44 (0)1268 444470  
Telephone lines are open Monday to Friday, 9 a.m. to 5.30 p.m.

Your telephone call may be recorded for your security

[www.mercantileit.co.uk](http://www.mercantileit.co.uk)