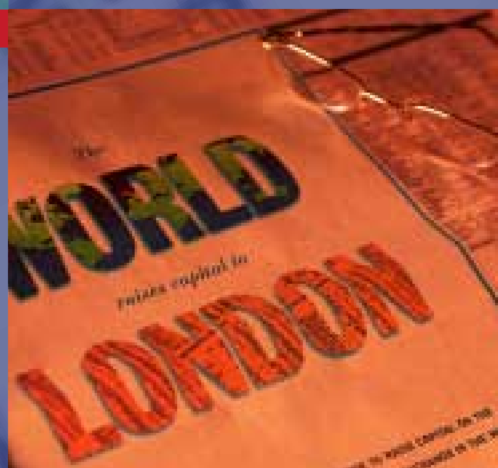

Major international newcomers


AIM market hits new records



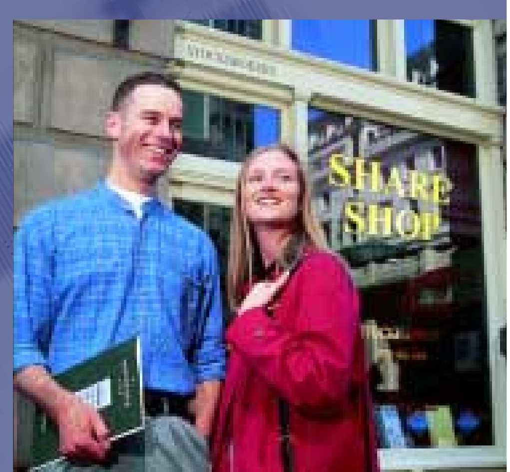
Companies raise over £62 billion

Financing the future


Electronic order book introduced for London

London **STOCK EXCHANGE**

Annual Report 1998



Private share ownership grows

London: The essential marketplace

Ideally positioned between the New York and Tokyo time zones, the London Stock Exchange plays a vital role in maintaining London's position as one of the world's leading financial centres.

Listing in London gives companies access to a deep and liquid market. As one of the leading centres for fund management, London is home to £1.4 trillion in managed funds, and firms based in the City manage some of the most geographically diverse portfolios in the world. Moreover, a significant number of international investment banks have chosen to base their main European investment banking and securities operations in London. Investors want the speed and certainty to deal that comes with a liquid and fair market and London has long been renowned for providing both.

Among its advantages, London has a balanced and effective regulatory regime, vast accumulated experience in banking and finance, and a well-established equity culture. This has led to a concentration of financial skills in securities sales and trading, banking, foreign exchange, corporate finance and asset management. And since the Exchange is both the UK's Listing Authority and a Recognised Investment Exchange, companies have to deal with only one regulatory body, easing access to listing on the London Stock Exchange.

Building on its reputation for integrity and transparency, the Exchange continues to adapt to the needs of its clients, both UK and international, into the next millennium.

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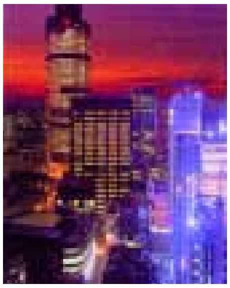


Financing the future By operating a portfolio of markets, the London Stock Exchange provides the infrastructure which enables companies and investors to prosper, as well as meeting the needs of our securities firms.

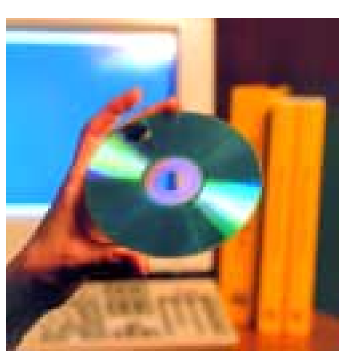
We are committed to developing products and services – supported by efficient technology – to meet the demands of a rapidly changing financial environment. Together, these are fundamental to meeting our goals of providing efficient and competitive markets to match the requirements of all our users.

8 Developing our markets

Our task is to ensure that we continue to win business for our markets and for London. During the year we introduced greater trading choice with an electronic order book and worked to promote our markets, both at home and overseas.

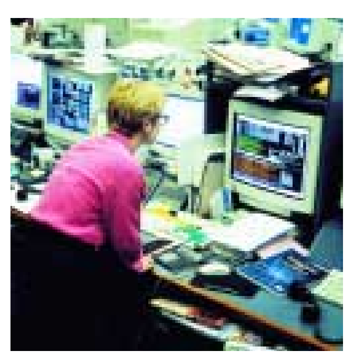
12 Regulating our markets

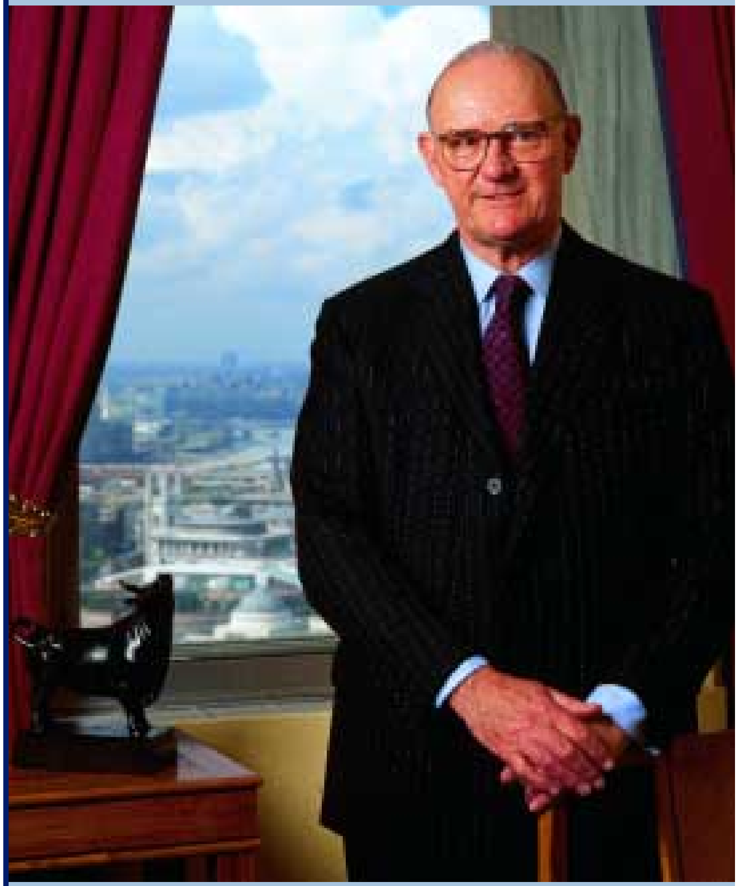
To maintain investor protection, as well as a fair and efficient marketplace for issuers, we keep our rules and procedures under regular review, remaining responsive to customers' needs and to changes in the business environment.



16 Delivering our markets

In delivering our services we aim for the best possible combination of responsiveness, reliability, functionality and cost. We are committed to providing a consistently high level of service to all our customers – whatever the conditions prevailing in the market.





John Kemp-Welch – Chairman, London Stock Exchange

The year 1997/8 will be remembered for buoyant, and in some cases, turbulent financial markets worldwide. London came through the year in good health, having successfully maintained and even strengthened its leading position in global finance. The Exchange played its part in this by providing efficient, well-regulated markets and by continuing to attract new business.

The Exchange's own markets had a significant year on several fronts.

At home

Last year was a record one for the UK equity markets. Turnover value rose by nearly 30 per cent, breaking through the £1,000 billion figure for the first time.

Exchange's electronic order-driven trading service. The launch in October of the new service by the Chancellor of the Exchequer marked the culmination of a long period of consultation and development and signalled another chapter in a process of reform that began in 1986 with Big Bang.

There was also considerable change during the year among the leading participants in the London market. New ownership of several major securities houses had the effect of making London even more international – a trend reflecting the depth of confidence worldwide in the future of London.

The change of government a year ago resulted in some far-reaching proposals for reform in the regulation of the UK

Chairman's statement

The Exchange's markets had a significant year on several fronts.

The vibrancy of the Exchange's markets was accompanied by a resurgence in merger activity, and by the introduction to our main market of some major companies, several of them as a result of UK demutualisations. As well as resulting in a very welcome expansion in private share ownership, the quality and standing of the demutualised companies enhanced the reputation of our marketplace.

A significant event during the year was the introduction of the

financial services sector and the Exchange is working closely with the new regulatory body, the Financial Services Authority.

In its capacity as Competent Authority for Listing, the Exchange has been able, through its Listing Rules, to help give effect in recent years to proposals to improve the standards of corporate governance of UK listed companies. The latest committee, under Sir Ronnie Hampel, concluded its work during the year and its Combined Code will be published as 'best practice' alongside our Listing Rules, following consultation with the market on associated rule changes.

International

On the international front, we continued our efforts to maintain the flow of new listings from countries all over the world. Our international marketing initiatives during the year included visits to China, India and Korea.

On a personal note, during my visit to India in December, I was especially pleased to meet the Indian finance minister, senior government officials and directors of both those companies already listed in London and of those considering a listing.

During the year we also received visits from government ministers, ambassadors and stock exchange representatives from a wide variety of overseas countries.

Committees

Following the significant change in the way our advisory committees are organised, I am pleased to say that the revised system enables the Exchange and its users to work more effectively together and it provides valuable advice on the development of policy.

I would also like to thank the members of the five main advisory committees, mentioned on page 21 of this Report, for the work they do and the advice they give us.

Board

Fields Wicker-Miurin left the Board in December 1997 and Richard Kilsby at the end of May. As director of Strategy and Finance and director of Market Services respectively they each made a considerable contribution to the Exchange at an important time in our development. We are very grateful to them.

Donald Brydon, Robert Metzler, Mark Radcliffe and Bernard Solomons are retiring from the Board at the conclusion of the Annual General Meeting. We thank them all for the significant contribution they have made to the Board and for the strong support they have given to the Exchange in recent years.

In addition to their membership of the Board each of them has given valuable time and experience to serving on important committees and we are very appreciative of all that they have contributed.

At the forthcoming AGM, we shall be recommending to shareholders that two new directors be appointed to the Board: Martin Wheatley, who is head of Markets Development and Marketing of the Exchange, and Simon Robertson, a Managing Director of Goldman Sachs.

Looking forward

While 1997/8 was a year of great activity in world markets, even more significant changes still lie ahead as global investment patterns continue to develop and particularly so in the light of the changes that EMU is likely to bring.

"Internationally our efforts were focused on maintaining the flow of new listings from countries all over the world."

The Exchange's preparations for EMU stepped up a gear during the year. With our advisory committees we are looking closely at changes in investment patterns and trading behaviour that are likely to result from EMU.

It is increasingly likely that the euro will presage a significant growth in equity-related business across Europe. We are determined to fulfil our role in ensuring that London is able to seize these opportunities. Good progress has been made.

Against this dynamic background, our competitive position will rely increasingly on our ability to deliver cost efficient services. This programme of work is in the hands of an effective and committed management team, working in close consultation with the market. This approach helps us to determine the right way forward and enables us to implement our plans efficiently and effectively.

Overall, London's future remains full of opportunity. Following the widespread and constructive changes we have implemented in recent years, I believe that the Exchange is well placed to play our part in that future.

John Kemp-Welch

John Kemp-Welch
Chairman,
London Stock Exchange

Chief Executive's review

The year's developments have strengthened our competitive position and provided a sound foundation for the longer term.

During 1997/8, we made significant progress across all our activities, meeting the targets we had set. These developments have strengthened the Exchange's competitive position, as well as providing a sound foundation for the longer term.

Our progress can be analysed under four main headings, details of which are given later in this Report. They are:

- Developing our markets – introducing greater choice for trading with the electronic order book, while lowering trading costs and working to promote our markets at home and overseas
- Regulating our markets – confirming our regulatory responsibility for listings and streamlining the processes involved in our regulation of both listings and trading
- Delivering our markets – maintaining a high level of reliability while enhancing our services to market users and publishing our plans for the Year 2000
- Managing our own business – ensuring the effectiveness of our cost-base and providing a further rebate to securities firms.

Developing our markets

The introduction of order-driven trading for FTSE 100 companies – a principal focus in the year – responded to the competitive needs of the market. This major change for the UK equity market has given London an advanced trading platform suitable for future developments.

Launching the order book

Having set out in January 1997 a timetable which aimed for delivery in October 1997, we undertook an intensive period of consultation, planning and preparation. Through the combined efforts of the entire market, and with valuable support and input from our Secondary Markets Committee, the order book was implemented on schedule on 20 October 1997.

During its first six months in operation, the electronic trading service (SETS) has proved robust under heavy use and in volatile markets, establishing itself as the market's main price formation mechanism and achieving a narrowing of average spreads between buying and selling prices.

However, we recognise that some further development is necessary for the new service to deliver in full the benefits it is designed to provide.

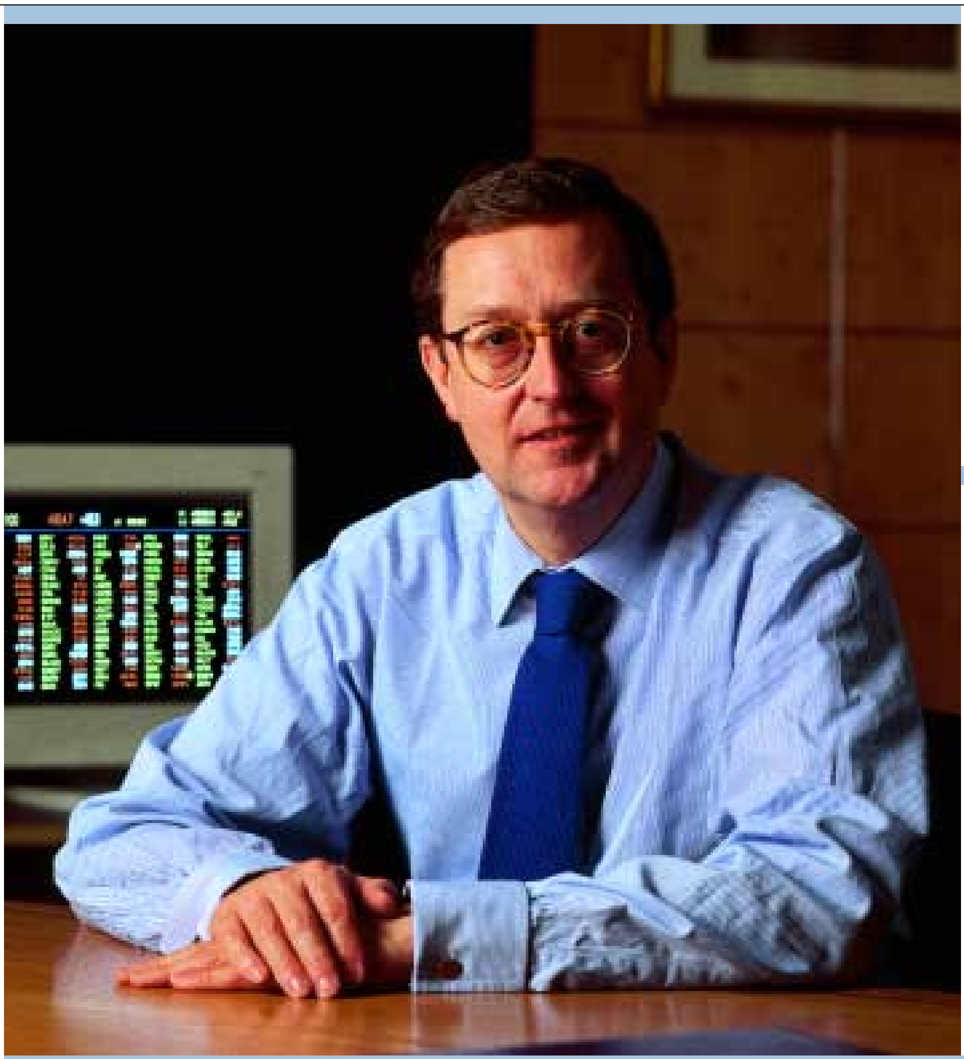
To this end, we have recently completed a major consultative exercise with market participants to review the performance of the order book. As a result of this work, we will be introducing a number of changes. We will continue to keep the operation of the order book under close review and will make further changes as required.

As part of our continuing commitment to providing cost-effective markets to our customers, a new competitive pricing structure was introduced at the time of the launch of SETS. The arrangements included significant reductions in the charges levied for trading in UK shares. At the same time, we continued to look to the needs of private investors, retaining a 25p minimum charge for our services and keeping the costs of larger trades to a maximum of £2.35.

Preparing for Economic and Monetary Union

The advent of Economic and Monetary Union (EMU) in January 1999 is clearly a significant event for the City of London. Although the UK will not be among the first wave of joiners, it is essential that we play our part to ensure that our securities markets are ready to benefit from the opportunities that EMU will bring and to lay the groundwork for potential UK participation in the future.

We have worked during the year to make sure that the Exchange and our markets are well prepared. Our trading



"It is essential that we play our part to ensure that our markets are ready to benefit from the opportunities that EMU will bring and to lay the groundwork for potential UK participation in the future."

Gavin Casey – Chief Executive, London Stock Exchange

platform, which already accounts in 36 currencies, can already accommodate euro-denominated securities and so gives us a sound base for the coming changes. There are also numerous detailed operational and regulatory changes which we continue to address in consultation with market participants.

Promoting our markets

We also strengthened the promotion of the Exchange and our services. In the UK we welcomed over 120 new companies to listing on the main market.

Meanwhile, a programme of international marketing visits ensured that the benefits of a London listing remained at the forefront of potential issuers' minds worldwide. We were pleased to welcome issues from several countries new to our markets, frequently in the form of depositary receipts (certificates showing ownership of shares usually listed on local exchanges).

AIM, our market for smaller and growing companies, developed further. During the year, we strengthened the regulations governing admission to AIM which continues to provide an effective way for smaller companies to raise funds for their growth. To date, over £1.7 billion has been raised by AIM companies.

On the private investor front, it was the busiest year since the privatisation programme of the 1980s. The demutualisations of several major building and insurance societies provided fresh impetus to the Exchange's work for private investors and the momentum is continuing this year with a national campaign – mounted jointly with a number of UK listed companies and securities firms to promote the benefits of equity investment.

Regulating our markets

Our task is to run efficient and orderly markets, where issuers can easily raise capital and investors feel confident to invest.

Primary markets

We were pleased to receive confirmation from the Government that the Exchange will continue in its statutory role of UK Competent Authority for Listing. The role was being looked at as part of the Government's review of financial regulation. The confirmation of our listing role is a welcome endorsement of the Exchange's work and we will continue to give companies a cost-effective and efficient means of listing.

The year also saw a streamlining of our listing processes, following a review of the service we offer to UK and international companies. The resulting reorganisation involved the implementation of new computer systems, with the result that handling of listing applications is now more efficient.

"On the private investor front, it was the busiest year since the privatisation programme of the 1980s."

▲ Supporting the promotion of wider share ownership – Gavin Casey at the Exchange-hosted final of ProShare's National Investment Programme for Schools and Colleges.

There is also greater access to help and advice, providing overall a better service for our customers.

Secondary markets

The Exchange is committed to maintaining high levels of protection for investors and ensuring the timely provision of trading and company information to the public. This was achieved over the year through the careful surveillance and supervision of our markets and, where appropriate, by carrying out specific investigations into potential cases of insider dealing and market manipulation for handover to the appropriate regulatory or prosecution body.

Delivering our markets

One of our key tasks is to ensure that our systems provide high quality support to the market. This is achieved by continuous co-operation, consultation and testing with key participants in the market.

Year 2000 compliance

As part of this commitment, we are working to make sure that our own trading and information services are tested for Year 2000 compliance. We are equally aware that the systems of our customers and suppliers must also be fully prepared and tested in order to provide a smooth transition to the new millennium.

CRESTCo co-operation

The Exchange worked closely with CRESTCo during the year to ensure the smooth transition of securities firms' transaction reporting, following the closure of the Exchange's own Talisman settlement service. We continue to work closely with CRESTCo on our respective day-to-day operations, as well as future developments.

Managing our own business

Our drive to increase efficiency and reduce overheads continued to bear fruit.

For the fifth successive year, the Exchange's overall costs fell, while services continued to be enhanced. Underlying operating costs showed a 21 per cent reduction on last year. At the same time, revenues were boosted by buoyant market conditions.

Securities firms' rebate

In the light of this performance, the Exchange has once again been able to return money to the securities firms that use its markets, through rebates on trading and membership fees. After the £16.6 million rebate, tax and interest, there was a surplus of £17.1 million which has been transferred to reserves to finance our continuing investment programme.

We have now largely completed the restructuring of our finances begun before the move of settlement functions from the Exchange. Costs will remain carefully controlled and we will continue to look for further efficiencies. We are now close to a sustainable financial platform for maintaining and improving our services, with sufficient flexibility to invest in our systems and our markets in the future.

Management and staff

One of the keys to our success is the cultivation of the right mix of staff with appropriate skills and experience. There have been some significant changes to the organisation during the year, including the appointment of a number of new managers to the Exchange's executive group. We are continuing a programme of promoting staff from within, where possible, and recruiting staff externally only when new skills are required. This strengthening of our team is already delivering results.

It has been a genuine pleasure to work with everybody in the Exchange over the year, including those who have now moved on. I would like to take this opportunity to thank them all personally for their great efforts on behalf of the Exchange's customers and shareholders.

The current agenda

The last year has seen us reach some significant milestones, but there is still a great deal to do.

In the coming year, our principal tasks are:

• to consolidate the operation of the order book so that the market can derive full benefit from the service

• to position our markets to take advantage of the immediate opportunities offered by the start of EMU, while continuing to develop our plans for our longer term future in Europe

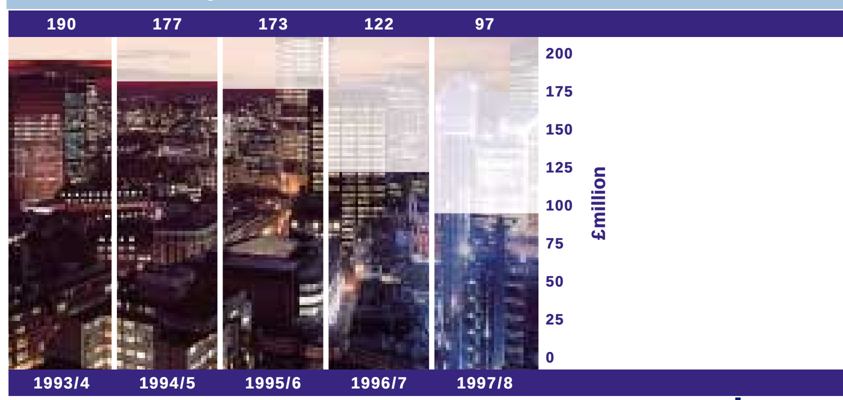
• to continue to tighten the conduct of our regulatory activities

• to carry forward our various marketing programmes, including those aimed at private investors and UK and international companies interested in joining our markets

• to continue to manage our business as effectively as possible, having regard to the needs of all market users and commensurate with our regulatory responsibilities.

"For the fifth successive year, the Exchange's overall costs fell, while services continued to be enhanced."

London Stock Exchange costs 1993/4 to 1997/8



This will undoubtedly be a major period of development and opportunity for London, its securities markets and for the Exchange. We look forward to all the challenges. We believe that the work we have carried out in the last two years, in particular, will stand us in good stead in the coming period.

Gavin Casey

Gavin Casey
Chief Executive,
London Stock Exchange

Developing our markets

Work continued throughout the year to develop the Exchange's markets on a number of fronts, including launching order book trading, meeting the challenge of EMU and promoting its markets both in the UK and internationally.

Chancellor of the Exchequer, Gordon Brown (left) and Gavin Casey, Chief Executive, London Stock Exchange – launching order book trading on 20 October 1997.

This year represented a landmark in the continuing development of the Exchange's markets. Highlights included the introduction of the electronic order book and significant advances in our preparations for Economic and Monetary Union (EMU).

These achievements took place against a background of buoyant, and sometimes volatile trading, with equity turnover at record levels, a marked increase in capital raising, indices at all-time highs and the creation of millions of new shareholders.

Order-driven trading

The order book – known as the Stock Exchange Electronic Trading Service (SETS) – was launched in October 1997, following the most comprehensive consultation exercise ever mounted by the Exchange. The system immediately proved its resilience, with its introduction coinciding with a prolonged period of turbulent markets worldwide, triggered by economic uncertainties in the Far East. The new system's performance underlined the value of the thorough testing and rehearsals undertaken by the market in the months preceding the launch (see case study on page 11).

On SETS, buy and sell orders entered on to the order book are matched electronically on-screen and are then executed against one another automatically – a step-change from the system of competing quotes and telephone trading. The order book at this time covers shares in the top 127 UK companies.

The performance and use of the order book in its first few months have confirmed its central role. Around 75 per cent of all trades are at the order book price – establishing it as the main pricing mechanism for the London equity market. Following its introduction, price formation has become more transparent, average spreads between buying and selling prices have narrowed substantially, and investors have benefited from a wider range of trading choices.

The pattern of trading on the order book continues to develop. In particular, we are seeing improvements to depth and spreads at the beginning and end of the trading day, as market participants become more familiar with the new way of working.

After the first six months' trading on the order book, the Exchange consulted its members and other market users on any changes which might be required.

Preparations for EMU

Another key focus of the year was preparing for EMU, as we worked closely with the users of our markets to ensure that we can benefit from the opportunities the single currency will bring.

The Exchange is already technically well prepared for the single currency. Since our trading platform caters for trading in many different currencies, converting to the listing and trading of euro-denominated securities will be relatively straightforward.

In June 1997, we published *Economic and Monetary Union: The Equity Markets*, outlining the steps necessary to prepare for EMU under a variety of different scenarios. Our proposals followed in a consultation document in February 1998. The issues on which we are seeking market participants' views include how to support trading in euros for UK stocks as well as trading in sterling.

As the largest European centre for equity trading and fund management, London stands to reap considerable benefits from the huge boost which monetary union will deliver to cross-border equity investment. Demand for equities is also likely to be raised by the continued development of the pension fund sector in Continental Europe. At the same time, EMU will alleviate currency risk and increase share price uniformity, leading to greater market efficiency. The resulting rise in liquidity and transparency should, in turn, encourage more companies to go public.

Primary markets

Listing activity by UK and international companies was buoyant during the year, with 124 UK companies and 39 overseas companies coming to the main market, and 90 companies joining AIM – taking the total number of companies quoted on our markets to 2,967. The money raised during 1997/8, including eurobonds, exceeded £62 billion, a rise of eight per cent. AIM continued to grow in size and maturity. By the end of March 1998, AIM had attracted 310 companies,

"As the largest European centre for equity trading and fund management, London stands to reap considerable benefits from the huge boost which EMU will deliver to cross-border equity investment."

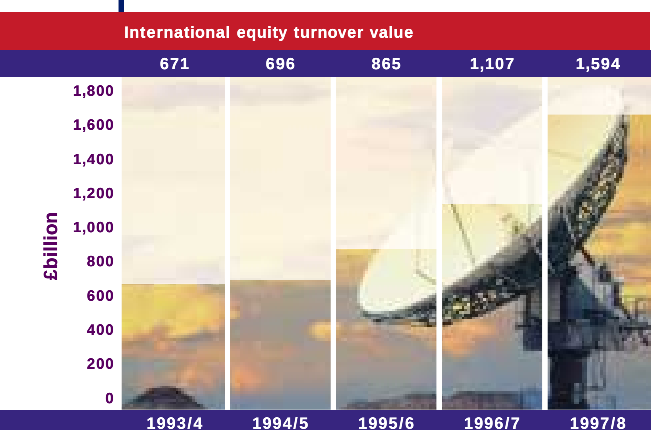
The Exchange published two documents outlining changes to equity markets as a result of EMU.

raising a total of £1.7 billion (including £553.9 million during 1997/8 alone). The gilt-edged market had a solid year, raising £26.6 billion for the UK Government.

Internationally, the 39 companies which chose a London listing raised a total of £2.5 billion.

Secondary markets

Trading activity reached record levels during 1997/8, with the value of UK equity turnover rising by 27 per cent to over £1,003 billion. The most active trading was in financial stocks, followed by service companies. International equity turnover rose even more strongly, up by 44 per cent to £1,593.5 billion, mostly in European equities. The AIM market enjoyed its most active trading year since its launch in 1995, with over six billion shares traded (a rise of almost seven per cent).



▲ International equity turnover rose strongly, up by 44 per cent to £1,593.5 billion.

During the year, a global depositary receipt issued by Indian telecommunications provider VSNL raised £227.7m.

Indices

New records were set by all the major UK share indices. The FTSE 100 index broke through the 5000 barrier for the first time, ending 1997/8 at 5932.2 – a rise of 38 per cent on the year – while the FTSE All Share index rose 32 per cent to 2781.6.

FTSE International, the indices company owned jointly by the Exchange and the Financial Times Limited, developed several new share indices both in the UK and overseas during the year. In the UK, FTSE launched three risk-weighted indices for private investors, and a new information technology index.

Overseas projects included the new FTSE-ASE index in Athens, and an agreement with the Amsterdam stock and options exchanges to take over calculation of the Eurotop 100 index, renamed the FTSE Eurotop 100. FTSE also developed the FTSE Eurotop 300, a new index covering Europe's 300 largest stocks.

UK marketing

A new Business Development Group was set up during the year to replace regional offices based in Belfast, Birmingham, Glasgow, Leeds, London, and Manchester. The new team of regional representatives reports directly to the London office and gives the Exchange the increased flexibility to place resources when and where they are needed.

This new structure was put to full use during the year as the Exchange kept market participants throughout the UK involved in the move to order book trading. We also launched a new customer magazine, *Exchange*, to keep all UK and international customers abreast of issues affecting the users of the London equity markets.

International initiatives

The Exchange's programme of overseas marketing continued throughout the year, ensuring that companies and investors worldwide are aware of London's strengths. High-level delegations conducted several promotional visits, with the primary objective of encouraging listings from emerging and fast-growing economies.

In June 1997, a team led by the Exchange's Deputy Chairman – in tandem with British Invisibles – visited South Korea, meeting a number of companies and signing a Memorandum of Understanding with the Seoul Stock Exchange. In November, the Exchange's Chief Executive participated in a sales drive in China, again with British Invisibles, and reinforced the Exchange's close relationship with Chinese regulators. And in December, the Exchange's Chairman visited India, to meet government authorities, potential issuers and London-listed companies in New Delhi and Mumbai (formerly Bombay). Other countries visited during the year included Bahrain, Jordan, Oman, Poland, Russia, South Africa and Ukraine.

The excellence of London's global reputation was underlined by the continuing expansion of its international listings base, with the first issuers from Bahrain, Jordan and Latvia coming to market. A global depositary receipt (GDR) issued by the Indian telecommunications provider VSNL in April 1997 raised £272.7 million – the largest amount so far with a GDR, and was followed by a further GDR from another Indian telecommunications company, MTNL. The listing in March 1997 of the first Chinese company on the Exchange, Beijing Datang Power, was followed by a second full listing from China, Jiangxi Copper Co, and a GDR from Zhejaing South East Electric Power Co.

Private share ownership

The year saw substantial expansion in private share ownership, due largely to the listing of several former building and insurance societies. The Exchange used the occasion of these high-profile flotations to provide the new shareholders created by the demutualisations with information about the share owning process.

Exchange initiatives included two new guides for private investors – *Share Ownership for All* and *Being a Shareholder* – and our Public Information telephone hot-line was strengthened to deal with the number of calls, which rocketed from their usual level of 1,000 to around 10,000 a week at the height of the demutualisations. We also continued to develop further links with private client brokers launching, in January 1998, a new regular newsletter for retail brokers called *Exchange Link*. We began detailed planning for a national promotion of the benefits of share investment, to be launched after the end of the financial year in conjunction with UK listed companies and our securities firms.

Case study: Building an electronic order book

In the 18 months prior to the launch of the order book (SETS), the Exchange worked with securities firms, information providers, listed companies and government officials – consulting on the shape and scope of the order book to ensure that everyone was prepared for the change.

Technical preparations for SETS involved over 40 'man' years and entailed around 350 staff across the Exchange. Technical and educational documents, focus groups and customer interviews supported firms up to the launch and beyond.

On the systems side, the Exchange worked closely with Andersen Consulting to build the technology for the new trading structure and to liaise with technical contacts across the market.

Communication during the period included three consultation documents, 17 technical guidance notes and 21 information sheets. General brochures were also produced for the public, including a guide for private investors.

Six weeks before the order book went live, weekend dress rehearsals gave traders hands-on experience and tested the systems thoroughly. More than 4,000 staff from 180 securities firms gave up their weekends to join the dress rehearsals, while Exchange staff monitored the systems and trading to ensure the order book was ready to go live.

Key features of the order book:

- over 75 per cent of all trades (on and off the book) are at the order book price
- order book share of total trading – up to 49 per cent by value (average 32 per cent)
- over 60 per cent of all eligible trades are conducted on SETS.

Consultation with market participants was key to the success of the project.

Exchange management monitored systems and trading.

The Exchange provided round-the-clock testing facilities, simulating real market conditions.

Weekend dress rehearsals gave traders hands-on experience before the launch.

Regulating our markets

Regulation is fundamental to investor protection and to the operation of fair and efficient equity markets.

Key to carrying out our regulatory responsibilities, is our commitment to maintain a strong framework of protection for investors as well as a fair and efficient marketplace for issuers.

This means keeping our rules and procedures under regular review so that we remain responsive to customers' needs and to changes in the corporate environment.

In the secondary markets, the Exchange's Integrated Monitoring and Surveillance System (IMAS) has continued to provide a reliable, real-time method of monitoring the markets.

Primary markets

The year has been a particularly active one in terms of regulatory developments. The Exchange's role as the UK Competent Authority for Listing was confirmed by the Government; a major exercise in streamlining our handling of listing enquiries and documents was completed; and there were several changes to the Exchange's Listing Rules, as well as a consultation exercise on the new Combined Code on Corporate Governance proposed by Sir Ronnie Hampel's Committee.

Listing authority re-confirmed

The efficiency of the Exchange in carrying out its listing functions was endorsed earlier this year when the Government confirmed its statutory role as UK Competent Authority for Listing. The announcement from the Treasury said that the Exchange is creating and enforcing listing rules in a way which both gives confidence to investors and also meets the commercial needs of users.

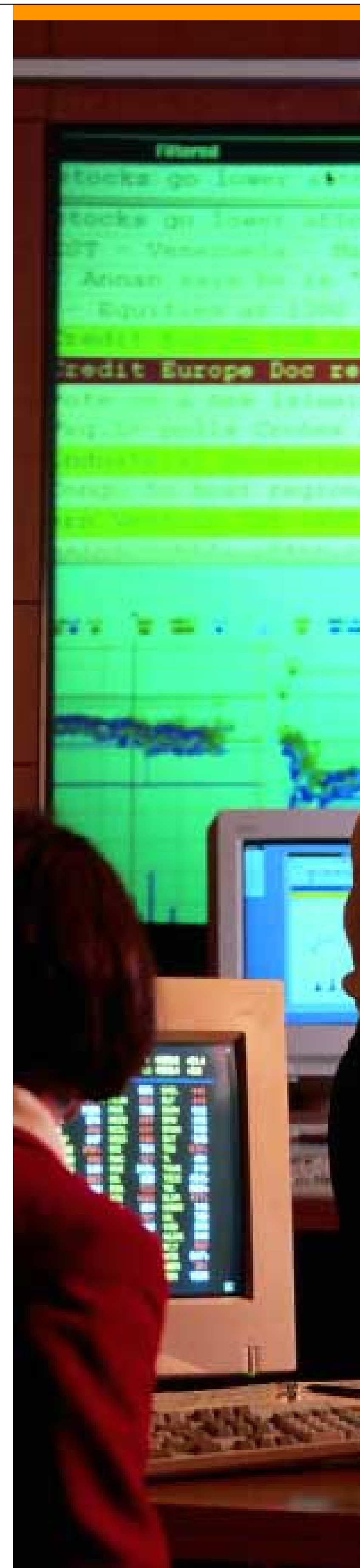
While this confirmation represents an endorsement of the Exchange's work in this area, we remain committed not only to maintaining current high standards, but to enhancing performance still further.

Processes streamlined

During 1997/8, we completed a major exercise to streamline our listing processes. This review, begun the previous year, is delivering significant increases in the efficiency of the service we offer to UK and international companies. All aspects of the exercise, including

"The London Stock Exchange is... creating and enforcing listing rules in a way which gives confidence to investors, while meeting the commercial needs of users."

Rt Hon Alistair Darling MP, Chief Secretary to the Treasury



IMAS – one of the world's most advanced systems for monitoring market activity.

substantial IT developments, were subject to extensive consultation to take into account the requirements of both companies coming to market and those already listed (see case study on page 14).

Changes to our Listing Rules

The Exchange announced a series of changes to the Listing Rules (the 'Yellow Book') aimed at benefiting investors and also companies joining the Exchange's markets. By simplifying the listing process, eliminating outdated regulations and making the rules more readily understandable, we are working to increase the international competitiveness of our markets.

The changes included lifting the existing restrictions on the use of summary documents and encouraging the use of more user-friendly and intelligible material for shareholders. The aim of achieving greater clarity was also served by a number of further changes, the most notable being the introduction of greater flexibility in the use of pro-forma financial information – a move which aligned the Exchange's requirements in this area more closely with companies' experience overseas.

Restrictions relating to profit forecasts and management continuity were also eased. In parallel with these changes, the Exchange's general updating process continued, with the removal from the

Case Study:
Project Lion – Improving the listing process

A major project to improve the processes and technology implemented by the Exchange's company listing function, was completed in February 1998.

Code-named Project Lion, its tasks were two-fold:

- to streamline the vast quantity of paper-based documents that accompany listing applications, and
- to boost the level of service provided to customers.

The systems introduced under Project Lion modernised the previous paper-based processes and provide faster, more effective handling of listing applications and all associated activities.

Among the practical improvements delivered by the review are new systems for case management – to identify precedents in previous listings, and for more efficient document tracking.

There is also greater access to help and advice for listed companies and their advisers through a dedicated help desk.

The Exchange's paper archive will be phased out as more and more company documents are stored electronically.

Developments in technology provide faster and more efficient handling of listing applications.

Listed companies now have greater access to advice through a dedicated help desk.

Listing Rules of regulations which duplicated statutory or accounting requirements.

AIM rules reinforced

During the year, the Exchange also clarified and reinforced the regulations governing admissions to AIM. Under the revised rules, companies coming to the market are required to identify anyone who has received shares or fees worth £10,000 or more in the previous 12 months.

Further changes included the requirement for companies and their nominated advisers to undertake regular reviews of the company's financial performance, and to notify the market of any material change against the forecasts published in its admission documents. The amended rules also placed greater responsibility on nominated advisers to satisfy themselves that a company was 'appropriate' for admission to AIM.

Hampel report

The final report of the Committee on Corporate Governance, chaired by Sir Ronnie Hampel, was published in January 1998. Following receipt from the committee of its Combined Code, which set out the Committee's principles and its own detailed recommendations, as well as those of the earlier Greenbury and Cadbury Committees, the Exchange embarked on a six-week consultation exercise involving companies, their advisers and other interested parties.

This process gave the opportunity for comment on any perceived ambiguities in the new Combined Code and for any clarification of wording. At the same time, it provided for consultation on the proposed inclusion in the Exchange's Listing Rules of a statement through which companies will disclose their compliance with the Combined Code.

The Code, which provides a clear statement of best practice in corporate governance, will sit alongside, but not form part of, the Exchange's Listing Rules. Following the consultation process, the final Code is expected to be published in mid-1998.

Secondary markets

In the secondary markets, the Exchange's Market Regulation and Enforcement department ensured that the operation of our markets was efficient and orderly throughout the year.

Monitoring and surveillance

We continued to maintain proper levels of protection for investors and ensured the timely provision of trading and company information to market participants. This was achieved by comprehensive real-time surveillance and supervision, carried out through the Exchange's Integrated Monitoring and Surveillance System (IMAS), one of the world's most advanced systems for monitoring market activity.

In particular, this involved identifying unusual trading activity and price movements, supervising market maker activities and detecting and investigating potential breaches of Exchange rules, cases of insider dealing and market manipulation.

During the year, the Market Regulation and Enforcement department carried out 111 detailed investigations into cases of potential insider dealing and market manipulation, resulting in 35 cases being referred to the Department of Trade and Industry for further investigation. In addition, cases were also referred, as necessary, to other exchanges and authorities such as the Financial Services Authority, the Serious Fraud Office and the US Securities and Exchange Commission.

Responding to market changes

The Exchange successfully responded to the regulatory challenges arising from the introduction of the new electronic order-driven trading service in October 1997 and continued to develop its regulatory techniques to meet such market developments.

The Exchange co-operated with CRESTCo on the restructuring of the transaction reporting regime which will improve the regulatory reporting of transactions. Also, in preparation for the introduction of the order book, we worked with CRESTCo to put in place a revised regime for the calculation and collection of stamp duty, to accommodate a new set of tax reliefs to fit the new market structure.

In addition, the Exchange's ongoing investment in technology has enhanced its monitoring and surveillance capabilities. In particular, during the year, the Exchange developed and implemented improvements to its Transaction Database System to assist in the monitoring of Exchange transactions reported to CREST, following the transfer of the last stocks from Talisman to CREST in April 1997.

Insider trading

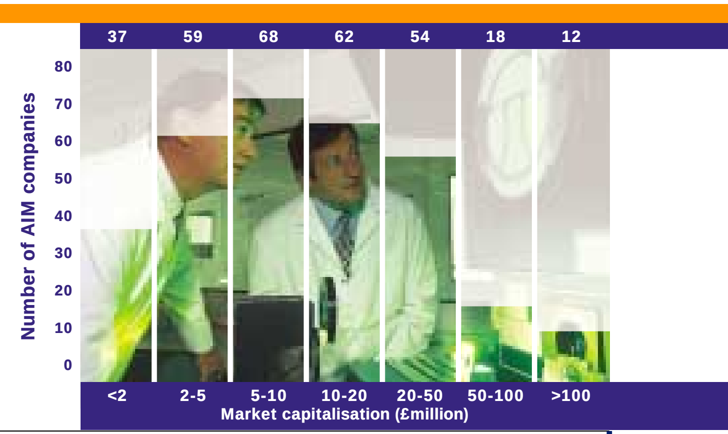
Throughout 1997/8, the Exchange worked closely with the UK Government and other regulatory bodies on developing new initiatives and guidelines on combatting insider trading.

As a result, changes to existing legislation were announced by the Government in May 1998, giving new civil powers of prosecution for cases of insider dealing and market manipulation. This reform, for which the Exchange has been pressing for some time, will increase the available sanctions in cases of insider dealing and enhance investor confidence in the markets. At the same time, the Exchange was given additional powers, in its role as Competent Authority for Listing, to fine companies in cases of breaches of the Listing Rules.

▼ The £4.5 million raised at issue on AIM by AorTech International plc has given the Lanarkshire-based company the flexibility to progress its cardiovascular research.

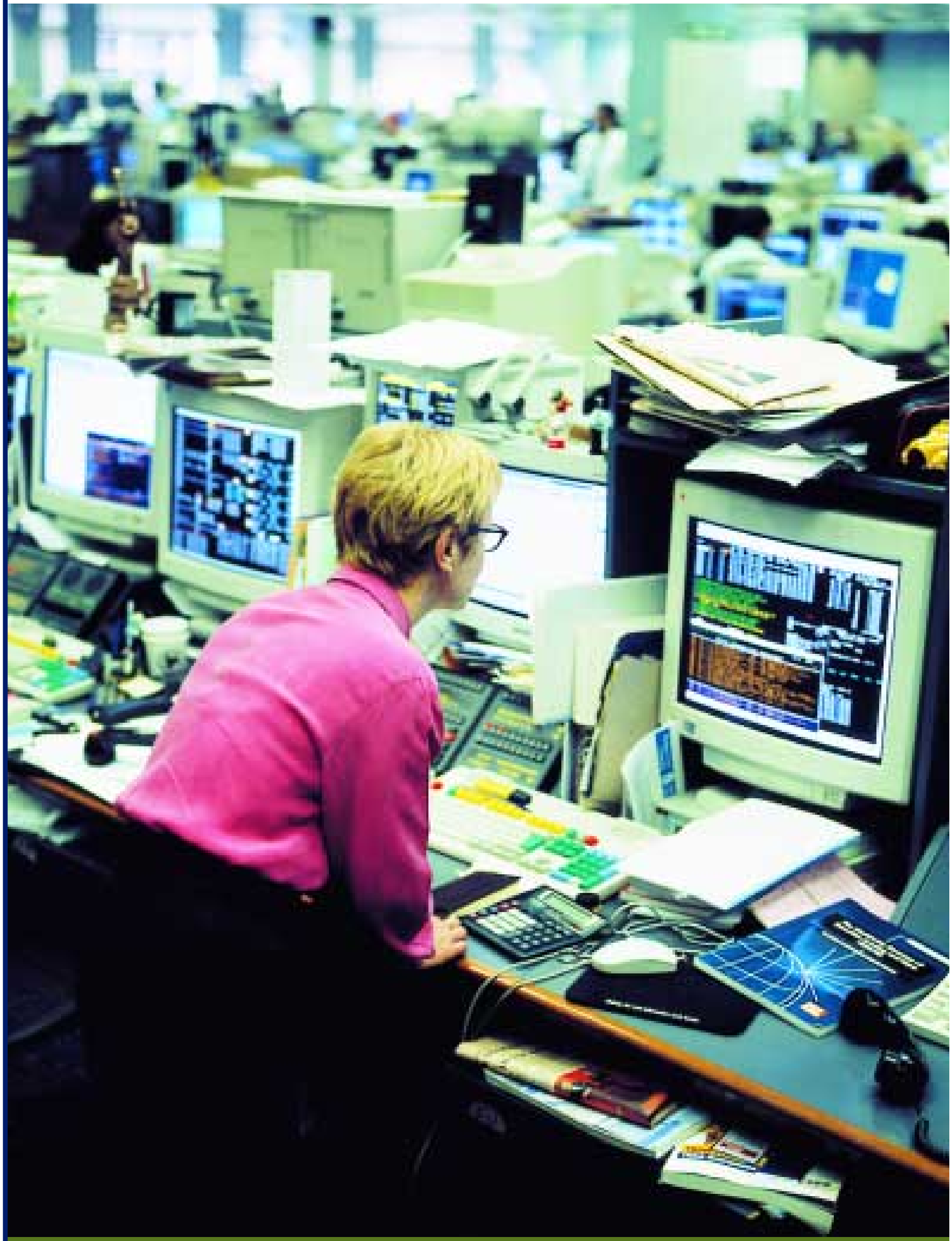
Pictured (from left to right): Eddie McDaid, managing director and Gordon Wright, chairman.

"During the year, the Exchange also clarified and reinforced the regulations governing admissions to AIM."



Delivering our markets

We delivered a consistent level of reliability and continued to develop and improve our services.



Around 75,000 terminals around the world display London Stock Exchange data.

During 1997/8, our systems and services maintained a high level of reliability, performing consistently well through a period of record volumes and substantial change.

We also continued to develop and improve the services we offer to all users of the London markets, aiming for the best possible combination of responsiveness, functionality and cost.

Information services

Providing accurate and timely information is a key Exchange activity on which our markets are based. The year saw an expansion in the distribution of this information through third party information vendors. During 1997, the number of screens showing Exchange data grew by 16 per cent to around 75,000 – of which 30 per cent are installed outside Europe. This increased distribution followed the restructuring of our information pricing in April 1997, which was designed to reduce many of the charges, increase value for money and, in part, to foster growth.

Lower charges for UK share trades

Also during the year we carried out our promised review of trading prices as part of our preparations for the implementation of the order book in October 1997. The review resulted in significant cuts in the charges levied for trading in UK shares, both on and off the order book.

For the new trading service it provided a cost-effective regime, with the average trade of £50,000 costing less than half the charge under the previous pricing system. At the same time, for trading outside the order book, the charge for an average £50,000 trade fell from £7.50 to £2.35. Special consideration was given to charges for smaller trades where the minimum charge of 25p was maintained, keeping rates at a very competitive level.

The new price structure took account of expected changes in trading patterns and volumes following the order book launch, and also reflected the Exchange's commitment to maintaining the competitiveness of its markets in a European and global context. A further factor behind the lower charges was the continuing success of the Exchange's drive to reduce its overheads.

Regulatory News Service

To develop further the speed and efficiency of the Regulatory News Service (RNS), we announced in April 1998 plans to take advantage of advances in communications technology. This involved appointing Informed Markets, a subsidiary of the electronic news provider, The Press Association (PA) to provide support services.

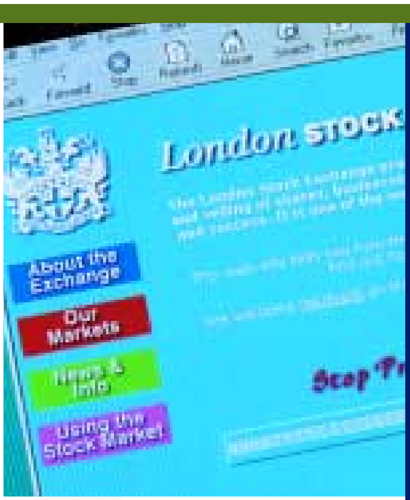
While management and control of this regulatory function remain firmly in the hands of the Exchange, it is clear that the benefits of developments in such a fast-moving electronic area can best be delivered by a company specialising in the field.

We plan to work with Informed Markets to introduce a broader range of electronic input mechanisms by the end of 1998, so that, while continuing to deliver the highest level of regulatory control, we can provide RNS customers with improved service levels via the best and most up-to-date technology.

Securities firms' access

A further advance in the services field during the year has been our work with British Telecommunications to develop the STX telephone service, through which securities firms gain instant access to Exchange services and support. BT will manage the current STX service through an outsourcing agreement and migrate it onto the BT FeatureNet network – a move which will in the future enable the Exchange to add new facilities and widen the range of services on offer.

"The number of screens showing London Stock Exchange data has grown to 75,000 worldwide."



▲ The Exchange's websites are a valuable resource for communicating with our customers.

Internet-based information services

During the year, we made increasing use of the Internet for both consultation and information purposes. The Exchange's website is now divided into two separate facilities – a 'corporate' site for general information about the Exchange and its markets, and a 'user' site for technical and practical issues.

The corporate website has proved a valuable resource for the Exchange in communicating with its wider audiences – ranging from institutions and listed companies, to private investors seeking advice on the buying and selling of shares, through hyper-links to more detailed information sources.

Old charge
Order book
Non-order book

▲ Our pricing review resulted in significant cuts in the charges levied for trading in UK shares.

Also during the year, the Exchange looked at providing possible avenues for a wide range of useful information including a 20-minute delayed share price, the previous night's closing price, company contact details, the headlines of any company announcements and the details of the last five trades in the shares.

The service, which will be introduced this year, will be particularly useful for private investors who are frequently avid users of the Internet as a data source.

The Exchange's 'user' site was a key resource in the technical preparation for SETS and won a major internet award, sponsored by the *Financial Times*. The award recognised uses of new media to reach business customers or to enhance distributor and dealer relationships. The site has been, and continues to be, used for consultation on technical preparations for EMU, Year 2000 and the Combined Code produced by the Hampel Committee on Corporate Governance.

Preparations for Year 2000

For some time, the issue of how the new millennium will affect computer systems has been a particular focus of concern for companies of all sizes. The Exchange itself has a clear programme of work

Case study:
Helping to meet the challenge of the Year 2000

Work to secure a smooth transition for equity markets at Year 2000 began during the year. A detailed set of arrangements was published by the Exchange in February 1998, designed to ensure the successful linking of customer systems with the Exchange's central trading and information systems.

It is intended that the Exchange's market-facing and internal systems will be tested for Year 2000 compliance by the end of 1998. Securities firms and other market participants will have to test that their systems which link to the Exchange are compliant by the middle of 1999.

Under the proposals, securities firms and customers are being offered two main services. The first is a mandatory testing service, designed to test the entry and receipt of information messages containing dates around the millennium. The second is an optional Year 2000 readiness service, which will help customers prepare their own systems for Year 2000.

to ensure that the market, regulatory and business support services are, where necessary, upgraded and fully tested for the requirements of Year 2000 (see case study on page 18).

However, on a wider scale, we are fully aware that it is vital to the operation of orderly markets and to the integrity and reputation of London equity trading, that millennium compliance issues do not cause disruption. This not only means that the Exchange's own systems must be tested for Year 2000 compliance, but also that they must continue to interconnect effectively with the systems of customers and suppliers.

With this requirement in mind, the Exchange published extensive plans in February 1998 for testing the successful linking of customers' systems with the Exchange's central trading and information services. The plans were developed in the light of feedback from the Exchange's customers and suppliers on the best approach to the Year 2000 issue and benefited from the experience of the comprehensive testing exercise conducted before the launch of SETS.

The nature of the Year 2000 issue clearly means that adherence to a strict timetable is crucial. The Exchange's objective is to make sure that its own market-facing and internal systems are fully compliant by the end of 1998. In turn, securities firms and other market participants must verify by mid-1999 that their systems successfully link with those of the Exchange.

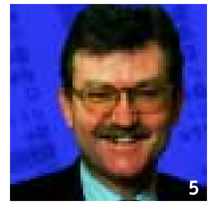
To help meet these deadlines, testing services will be available to market users for a 12 month period from October 1998, during which the services will be available every working day and (if necessary) one weekend in every three. This approach allows ample time for all parties' systems to be fully tested. We continue to work with the Bank of England, Financial Services Authority and other relevant organisations on all issues regarding Year 2000.

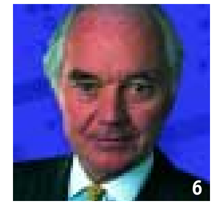
CRESTCo Co-operation

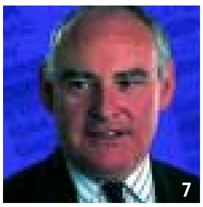
The Exchange has a close working relationship with CRESTCo. During the early part of the year, we worked together to complete the smooth transition from Talisman to the CREST settlement service. We also co-operated throughout the year on detailed operational and regulatory issues, as described on page 15.

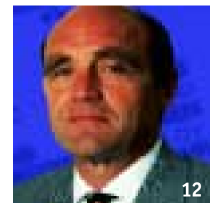
The Exchange's control centre works night and day to ensure orderly markets in the run up to the millennium.

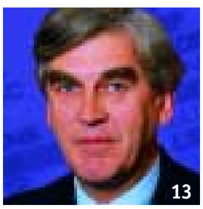
Board of directors

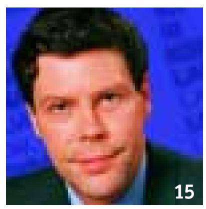












- • Member of the Audit Committee
- * Member of Management Committee
- ▲ Member of the Senior Appointments and Remuneration Committee

1. John Kemp-Welch 62
Chairman since July 1994. Formerly joint senior partner, Cazenove & Co. He is deputy chairman of the Financial Reporting Council, Chairman of The Scottish Eastern Investment Trust plc, a member of the Panel on Takeovers and Mergers, and a director of Royal & Sun Alliance Insurance Group plc, British Invisibles and The Savoy Hotel plc.

2. Gavin Casey 51 *
Chief Executive since August 1996. He is a chartered accountant and was previously Chief Operating Officer of Smith New Court (acquired by Merrill Lynch in 1995).

3. Ian Salter 55 ▲
Deputy Chairman since 1990. Director of SOCGEN Investment Management Ltd.

4. Gary J Allen, CBE, DL 53 •
Chief Executive, IMI plc, since 1986. He was appointed to IMI's Board in 1978, having joined the company in 1965. He is a non-executive director of NV Bekaert SA, Belgium and a member of the Council of the CBI.

5. Graham K Allen 47 •
Managing Director, ICI Investment Management Ltd. He joined ICI in 1974. He is Vice President of the NAPF. From 1996 to 1998 he was chairman of the NAPF Investment Committee, and also a member of the Panel on Takeovers and Mergers.

6. John Bond 56 ▲
Chairman of HSBC Holdings plc and director of The Hongkong and Shanghai Banking Corporation Ltd in Hong Kong and Chairman of Midland Bank plc. He is also a non-executive director of Orange plc.

7. Donald Brydon, OBE 52 ▲
Chairman and Chief Executive of AXA Investment Managers. He is a director of Allied Domecq plc and Nycomed Amersham. He has been Vice President of NAPF and Chairman of the Institutional Shareholders Committee.

8. Christine Dann 49 *
Director of Business Operations since March 1994. She managed the Birmingham Stock Exchange, transferring to London in 1983. She is a director of FTSE International Ltd and of CRESTCo Limited.

9. Richard Kilsby 47 *
Director of Market Services since September 1995. Formerly a managing director with Bankers Trust in the UK and USA. From 1988-1992 vice chairman of Charterhouse Bank.

10. Michael Marks 56 ▲
Executive Chairman, Merrill Lynch Europe, Middle East and Africa. Member of the Executive Management Committee of Merrill Lynch & Co. Inc. He is a member of NASD's International Markets Advisory Board.

11. Peter Meinertzhagen 52 ▲
Chairman, Hoare Govett Corporate Finance. He joined Hoare Govett in 1965 and is Chairman of The Hoare Govett Smaller Companies Index Investment Trusts.

12. Robert Metzler 60
A managing director of Morgan Stanley Securities since 1984 and Vice Chairman of Morgan Stanley & Co. International Limited.

13. Ian Plenderleith 54 •
Appointed Government Broker in 1989, he is an executive director of the Bank of England responsible for monetary stability (operations). At the Bank of England since 1965, he was seconded to the IMF in Washington DC and served on the Board of the European Investment Bank.

14. Mark Radcliffe, DL 60 •
Previously a director of the TI Group plc and Deputy Director General of the CBI. Chairman of METSEC PLC and SEC PLC. He is a member of the SFA Board.

15. Hector Sants 42
Vice Chairman of UBS Ltd until 1998, responsible for UBS' worldwide equity operations. From September 1998 he will become joint Chairman of D.L.J. Europe and Global Head of International Equities.

16. Nigel Sherlock, DL, 58
Chairman of Wise Speke Ltd, having formerly been a partner of Wise Speke & Co from 1969-87. A deputy chairman of APCIMS, a member of the Securities Institute and an associate member of the Institute of Investment Management and Research.

17. Bernard Solomons 53 •
Previously Chairman of Allied Provincial Securities plc and deputy chairman of Greig Middleton & Co Ltd. He is a non-executive director of Britannia Smaller Companies Trust plc, Allied London Properties plc, Edinburgh Income Trust plc and the Scottish Amicable.

Management Committee
In addition to Board members (marked with an asterisk) the following comprise the Exchange's Management Committee:

Allan Cameron
Paul Geradine
Jonathan Howell
Claire Mascall
Colvin Rae
Keith Robinson
Martin Wheatley

Committee reports

The Committee system enables the Exchange and market practitioners to work together closely. The following is a review of the year by the Exchange's Committees.

Primary Markets Committee

This committee provides practitioner advice on policy matters relating to primary markets, including rule changes for both the main market (Official List) and AIM.

Particular input was given by committee members in relation to the Exchange's consultation on Amendment 11 of the Listing Rules. The committee also reviewed the public consultation document which was issued by the Exchange following receipt of the Combined Code on Corporate Governance, published by the Hampel Committee.

A particular focus of the year was a review of the special needs of smaller companies. A separate working group was established to report to the committee on this issue and will present its findings and recommendations in the near future.

Secondary Markets Committee

The committee, which provides practitioner advice on a wide range of secondary market issues, played a major part in the development of the new electronic trading service (SETS), offering support and guidance on all aspects of the order book, including the rules, arrangements for retail investors and non-FTSE companies.

The committee also advised on the new pricing structure introduced by the Exchange in conjunction with the order book.

A further key area of consideration was Economic and Monetary Union (EMU) and its effect on the equity markets. The committee advised on the issues arising from monetary union and on the content of the Exchange's EMU consultative document issued in February 1998.

Listed Companies Advisory Committee

The committee considered a wide range of major policy issues as they affect listed companies. These included the work of the Hampel Committee on Corporate Governance, where the committee focused particularly on differentiation between small and large companies, on the structure of boards and the conduct of AGMs.

The committee also looked at corporate governance rights for private investors, as well as advising on amendments to the Listing Rules.

In preparation for EMU, the committee considered the potential impact on listed companies, in particular the question of currency of trading until the UK might join.

Institutional Investors Advisory Committee

The committee provided important investor views on the Exchange's thinking on trading market issues, in particular the operation of SETS, where the committee commented throughout the year and advised on matters such as closing prices, spreads and year-end prices.

On EMU the IIAC was heavily involved in the debate over the way forward and contributed to the pool of ideas, particularly with regard to the movements of investment funds into euros and the implications of mixed portfolios in the euro environment.

The committee also advised on changes to the Listing Rules and to the application of the Combined Code on Corporate Governance issued by the Hampel Committee.

Private Investors' Advisory Committee

In its role as adviser on matters related to wider share ownership, the committee helped guide the Exchange in its move to encourage equity participation, taking forward key recommendations from the Weinberg Committee.

The committee addressed private investor governance rights, as well as practical options related to new issues. It also made a significant contribution to the Inland Revenue consultation on Individual Savings Accounts (ISA).

A key area of the committee's work was to advise on the Exchange's promotional work in this area, which included new publications and presentations, and the development of an industry-wide investment campaign.

Financial review – managing our finances

The financial performance of the Exchange has been sound during a year of significant change. At the year's close, staff numbers were 30 per cent lower than a year ago and operating costs were down by 21 per cent, more than 50 per cent lower than five years ago. Although settlement operations have now ceased, income from other sources increased over the previous year. We were able, therefore, to return £16.6 million to our members in the form of a rebate.

We removed a significant part of our cost base following the closure of Talisman in April 1997 and further restructuring has prepared the Exchange for the future opportunities which are now on our agenda. Our cost base is below the target we set two years ago. The pricing for a number of services has been reviewed and reductions made to tariffs for both trading and information services.

Income

Gross income for the year was £143.3 million, 4.5 per cent above last year (after taking into account the loss of settlement) in spite of the lower prices for trading and information services referred to above. We have benefited from increased sales of our data around the world and market volumes have been buoyant. Listing activity increased with a higher level of new issues. Income from property lettings has also grown with the successful letting of surplus space as the Exchange's requirements have been reduced.

The rebate of £16.6 million to our members is based on trading charges and, in this exceptional year, a full refund of the membership fee. This is in recognition of the strong financial performance over the past year and to mark our commitment to returning funds to members when the financial position allows, while maintaining sufficient resources to meet future investment needs.

Costs

For the fifth successive year, costs have been reduced with operating costs at £96.7 million, 21 per cent down on last year. Staff costs are part of this reduction, with a saving of £6.6 million on last year and these are now lower than at any time over the last 10 years. Staff numbers at the year end were 529 (221 lower than a year ago). Staff costs include bonus payments which have been introduced for all staff who perform well against objectives set for the year. This provides a motivation for staff which has helped the Exchange meet its business objectives.

Provisions

The Exchange is undertaking significant work in preparation for Year 2000 and EMU. Work on these projects is covered in more detail in earlier sections of this report. We are providing market testing services to securities firms as well as modifying our own systems where necessary. The accounts include provision for the cost of these projects, reflecting a charge in the year of £16.5 million.

The provisions made in previous years covered the restructuring of the Exchange, where work is proceeding as planned. Some further rationalisation will take place in the coming year, including the recently announced new arrangements for the Regulatory News Service and the STX service. The rationalisation of settlement operations is now complete and £3.1 million is released to the Revenue Account. This is a saving from the original provision as the careful management of the migration to CREST resulted in lower trading losses than initially provided.

Final results

Net interest receivable increased to £7.3 million (1997, £7.1 million) and our contribution from FTSE International was unchanged at £0.3 million. This resulted in a surplus before tax of £24.1 million compared with £25.3 million in the previous year. After tax of £7.0 million, we are transferring £17.1 million to reserves for future investment, the same amount as last year.

Balance sheet and cash flow

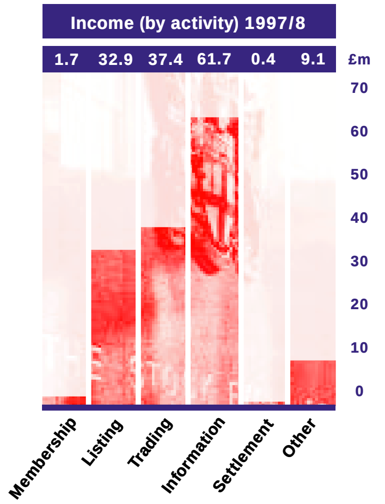
Cash flow for the year was positive with the inflow from operating activities exceeding the requirements for taxation and capital investment. The only long term debt is a £30 million debenture which is repayable in 2016.

Accounting developments

The new accounting standard for Associates and Joint Ventures FRS 9 has been adopted this year. Our joint venture company, FTSE International Limited, which is owned jointly with the Financial Times, is an important part of our business although our share of profits and net assets is not material in comparison with the Exchange's results. We have, therefore, included the detailed disclosure requirements in the notes to the financial statements.

Going concern

After making appropriate enquiries, the directors have a reasonable expectation, at the time of approving the financial statements, that the Company has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.



Corporate governance

Corporate governance

The Exchange continues to be committed to the principle of improved and strengthened corporate governance arrangements. The Combined Code on Corporate Governance, prepared by the Hampel Committee, will be published in mid-1998. The Exchange complies with the main recommendations of the Hampel Committee and intends to comply with the principles of the Combined Code in the coming year when the final text has been agreed.

For the year ended 31 March 1998, the Exchange's Board is satisfied that it has complied throughout the year with the Code of Best Practice published by the Cadbury Committee.

Board of directors

The Board, at 31 March 1998, comprised the Chairman, Deputy Chairman, Chief Executive, two executive and 12 non-executive directors. The non-executives represent various aspects of the Exchange's membership, but also include six independent directors. Directors categorised as independent are those who are not an employee or partner of an Exchange member firm.

Board committees

The committees of the Board which are concerned with the governance of the Exchange are detailed below and the directors who serve on these committees are indicated on page 20.

The **Management Committee** is chaired by the Chief Executive and comprises the principal executives of the Exchange. The Management Committee has the responsibility of managing the day-to-day business operations of the Exchange and to report regularly to the Board on those activities.

The **Audit Committee** is chaired by G J Allen, an independent director, and comprises four other non-executive directors. It meets at least twice a year, normally with the external auditors, to consider the audit plan, the interim and annual results, as well as any matters raised by the auditors. It reviews the adequacy and effectiveness of accounting systems and internal financial control. It also monitors the efficiency and independence of the internal audit function. The Committee reviews the Company's financial statements and makes recommendations regarding their approval by the Board as a whole.

The **Senior Appointments and Remuneration Committee** is chaired by J R H Bond, an independent director, and currently comprises four other non-executive directors. The report from this committee is set out on page 24.

Internal financial control

The directors are responsible for the Company's system of internal financial control. Such a system can provide only reasonable and not absolute assurance against material misstatement or loss. Internal financial controls are continually being developed, refined and communicated across the organisation. The directors, through the Audit Committee, have reviewed the effectiveness of the Company's system of internal financial control and are committed to its continual improvement. The framework of internal financial control is described under the following headings:

Delegation of authority – There are clearly defined matters which are reserved for Board approval only. The Board has delegated specific authorities to the Chief Executive and the Management Committee.

Financial reporting process – An annual budget is reviewed in detail by the Management Committee and is approved by the Board. Monthly financial reports compare actual performance with the annual budget and management action is taken where variances arise. Revised forecasts are prepared as required during the year.

Audit Committee – Reports from internal and external auditors on aspects of internal control are reviewed by the Audit Committee and appropriate action taken, where necessary. No material weaknesses have been identified over the past year.

Finance manual – Key procedures and controls for authorisation, reporting and investment appraisal are set out in a finance manual. This is reviewed and kept up-to-date to meet changing business needs.

Risk management – The operation of effective risk management is the responsibility of all line managers. This is kept under review by Internal Audit.

Going concern

As explained in the Financial Review on page 22, the directors continue to adopt the going concern basis in preparing the accounts.

Audit review

The Company's auditors have reported to the Board that in their opinion the directors' statements above on internal financial control and on going concern, included in the Financial Review on page 22, provide the disclosures required by the Listing Rules. The statements are consistent with the information of which the auditors are aware from their audit work on the financial statements. The above statement on corporate governance appropriately reflects the Company's compliance with the other paragraphs of the Code specified by the Listing Rules for review by the auditors. The auditors have not carried out the additional work necessary to, and do not, express any opinion on the effectiveness of either the Group's system of internal financial control or its corporate governance procedures, nor the ability of the Company to continue in operational existence.

Report of the Senior Appointments and Remuneration Committee

This report has been prepared in accordance with the recommendations made in the Code of Best Practice published by the Study Group on Directors' Remuneration (the 'Greenbury Committee').

Membership and terms of reference

The committee currently comprises five non-executive directors who are appointed by the Board. The committee members are shown on page 20. The committee meets as required to:

- review and present recommendations to the Board regarding the appointment, remuneration and conditions of service of the Chairman, Chief Executive and executive directors
- perform the function of a Nomination Committee for the appointment of directors
- review the remuneration of non-executive directors

(Each of the above is ratified by the whole Board)

- monitor the remuneration and conditions of service of members of the Management Committee who are not directors.

In the areas covered by this committee the members of it do not have any personal financial interests nor any potential conflicts arising from cross-directorships. The members do not have any day-to-day involvement in running the Company.

The committee has access to professional advice both from internal sources and external consultants. This advice includes relevant market data to assess the levels of remuneration.

The committee's terms of reference are approved by the Board.

Remuneration policy

The Exchange's remuneration policy is designed to attract, retain and motivate senior executives of a high calibre through a remuneration package which is competitive and representative of best practice.

All executive directors have one-year rolling service contracts with the Company.

Executive directors are allowed to accept up to two appointments as non-executive directors of other companies with the prior formal approval of this committee. Approval will only be given where the appointment does not present a conflict of interest with the Exchange's activities and the wider exposure gained will be beneficial to the development of the individual. The fees for these appointments will normally be paid to the Exchange.

Executive directors' rewards

The executive directors' remuneration package has four elements: base salary, benefits in kind, annual performance bonus and pension benefits.

Base salaries are reviewed annually taking into account market comparisons for similar roles, together with the performance of the individual.

Benefits in kind provided to executive directors are principally a company car allowance and private health care arrangements. Within the disclosures of individual director's remuneration, included in note 4 to the financial statements, benefits in kind represent the amounts assessable to income tax in respect of the benefits provided.

The annual performance bonus is a non-pensionable cash payment for achieving targets set each year. These targets are linked to the performance against objectives for the director and the organisation.

Pension benefits are also part of the remuneration package. Executive directors may join the Company pension scheme which offers Inland Revenue approved retirement benefits on final salary. The core benefit, which is non-contributory, comprises a pension accrual rate of $^1/_{60}$th of final basic salary for each year of service (up to a limit of $^2/_3$rds of final base salary). Alternatively, executive directors may elect to have a payment of $22^1/_2$ per cent of their base salary paid into an appropriate vehicle for pension according to their individual circumstances.

The amounts paid for pension arrangement are shown for each director in note 4 to the financial statements. The note also includes details in respect of the director who is a member of the Company defined benefit scheme. The information provided is the increase in accrued benefit and the accumulated pension at the end of the year and the transfer value of the increase in accrued benefit during the year.

Non-executive directors' fees

The standard fee for non-executive directors is currently £12,500 per annum as approved by the Board. An additional amount is paid to the Deputy Chairman, as shown in the accounts, in relation to the further activities which he carries out for the Company in his non-executive role.

Compliance

The constitution and operation of the committee is in compliance with Section A of the best practice provisions annexed to the Listing Rules and derived from the Code of Best Practice issued by the Study Group on Directors' Remuneration (the 'Greenbury Report').

The committee also confirms that full consideration has been given to the best practice provisions set out in Section B, annexed to the Listing Rules, in framing its remuneration policy for executive directors.

Details of directors' remuneration are set out on page 32, in note 4 to the financial statements.

John Bond
Chairman of the Senior Appointments and Remuneration Committee

Directors' report

The directors have pleasure in presenting their annual report to shareholders, together with the financial statements for the year ended 31 March 1998.

The Exchange was originally constituted by Deeds of Settlement dated 27 March 1802 and 31 December 1875. It was incorporated under the Companies Act 1985 as a private limited company on 19 November 1986 under the name of The International Stock Exchange of the United Kingdom and the Republic of Ireland Limited and has since changed its name to London Stock Exchange Limited ('the Exchange').

Directors

The directors of the Company at 31 March 1998 are shown on page 20.

S P Cooke died on 26 May 1997.

R A Barfield and M Kaneko resigned on 10 July 1997 and F Wicker-Miurin resigned on 31 December 1997. R P Kilsby has resigned with effect from 31 May 1998.

P R Meinertzhagen was appointed as a director on 22 May 1997.

Under the Articles of Association of the Company, D H Brydon, M H J Radcliffe and B Solomons will retire by rotation at the Annual General Meeting and do not seek re-appointment. R Metzler will retire from office at the same time. J Kemp-Welch and I Plenderleith will retire by rotation and offer themselves for re-election.

The share interests of the directors are shown in note 23 to the financial statements. No company in the Group was, during or at the end of the financial year, party to any contract of significance in which any director was materially interested.

Corporate governance

The Exchange's corporate governance statement is set out on page 23.

Membership

The number of member firms as at 31 March 1998 was 302 (1997, 312).

Interests in share capital

14,084 (1997, 14,072) 'B' shares are held by The Stock Exchange (Holdings) Limited as the share trustee in accordance with the Company's Articles of Association.

The directors are not aware of any person who is beneficially interested in three per cent or more of the issued share capital of the Company.

Principal activities and results

The principal activities of the Exchange and its subsidiaries are the organisation and regulation of markets in securities, the provision of associated information services and the admission of securities to listing which are regarded as a single class of business.

The surplus of the Group on ordinary activities before taxation for the year ended 31 March 1998 was £24.1 million compared with a surplus of £25.3 million in 1997. The premium of £1.46 million on redemption of 146 'A' shares has been deducted from the capital redemption reserve.

The business and systems developments and future developments of the Company are described more fully in the Chairman's statement and the Chief Executive's review on pages 2 to 7, and the Financial review on page 22.

Tangible assets

All freehold properties were revalued at 31 March 1997 and are included in the financial statements at the revalued amounts less depreciation. In the opinion of the directors, the market value of freehold properties at 31 March 1998 exceeded book value by approximately £16 million.

Employment

All new employees undergo an induction programme which includes training on health and safety. A range of training and development programmes is available for staff to develop their skills and knowledge. The Exchange encourages and assists the employment, training and retention of disabled people. Where changes to working practices or structure affect staff, they are consulted and given the appropriate support.

All employees are provided with information on matters of concern to them in their work, through regular briefing meetings and internal publications.

Donations

During the year the Exchange gave £103,000 (1997, £113,000) to charitable organisations. No donations were made to political organisations.

Supplier payment policy

The Exchange's policy with suppliers is to agree payment terms when business transactions are agreed and to make payments in accordance with those terms when goods have been satisfactorily supplied. At 31 March 1998 the average number of days credit from suppliers to the Company was 24.

Auditors

A resolution to reappoint Coopers & Lybrand as the Company's auditors will be proposed at the Annual General Meeting.

By Order of the Board
K O Robinson
Secretary
28 May 1998

Directors' responsibility for the financial statements

The following statement, which should be read in conjunction with the report of the auditors set out below, is made with a view to distinguishing for shareholders the respective responsibilities of the directors and of the auditors in relation to the financial statements.

The directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and the Group as at the end of the financial year and of the surplus or deficit for the financial year.

The directors consider that in preparing the financial statements on pages 27 to 43 the Group has used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, and that all applicable accounting standards have been followed.

The directors have responsibility for ensuring that the Group keeps accounting records which disclose with reasonable accuracy the financial position of the Group and which enable them to ensure that the financial statements comply with the Companies Act 1985.

The directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Report of the auditors

To the shareholders of London Stock Exchange Limited.

We have audited the financial statements on pages 27 to 43.

Respective responsibilities of directors and auditors

As described above, the Company's directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

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

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group at 31 March 1998 and of the surplus, total recognised gains and cash flows of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Coopers & Lybrand
Chartered Accountants and Registered Auditors
London
28 May 1998

Accounting policies

1. Basis of accounting and consolidation

The financial statements are prepared in accordance with applicable UK accounting standards under the historical cost convention modified by the revaluation of certain fixed assets. The consolidated financial statements include the accounts of all subsidiaries, although none was actively trading during the year. As permitted by section 230 of the Companies Act 1985, the holding company's revenue account has not been included in these financial statements.

2. Joint ventures

The Group's share of profits, less losses, of joint ventures is included in the consolidated revenue account and the Group's share of their net assets is included in the consolidated balance sheet. In view of the lack of materiality in relation to the Exchange's business, the Group's share of turnover, gross assets and gross liabilities underlying the net equity amount, as required by FRS 9 for Associates and Joint Ventures, is included in the notes to the accounts.

3. Tangible assets and depreciation

a) Freehold properties

Freehold properties, including related fixed plant, are revalued periodically by external chartered surveyors and included in the financial statements at the revalued amounts.

Freehold buildings and related fixed plant are depreciated, based on cost or valuation at the beginning of the year plus subsequent additions, over their estimated economic lives. The estimated economic lives of properties range from 15 to 50 years, the estimated useful lives of fixed plant range from 5 to 20 years.

b) Leasehold properties

Leasehold improvements are included at cost and depreciated over the period of the lease or economic life as appropriate.

c) Plant and equipment

Plant and equipment is stated at cost and is depreciated on a straight line basis over the estimated useful lives of the assets, which are mainly in the range from 3 to 5 years.

d) Leased plant and equipment

Plant and equipment leased from finance houses for effectively the whole of the useful lives of the assets are treated in the financial statements as tangible assets and the amount due to the lessors over the remainder of the leases, excluding an amount representing future finance charges, is included as a liability. The cost of leased plant and equipment is depreciated on a straight line basis over the lease period.

e) Service equipment

Computer and communications equipment acquired in respect of services in operation is stated at cost and depreciated on a straight line basis over the estimated useful lives ranging from 3 to 5 years.

4. Operating leases

Rental costs for operating leases are charged in the accounts as incurred. Provision is made in the accounts for lease commitments, less income from sub-letting, for properties which are surplus to business requirements.

5. Income

Income represents the total amount receivable for the provision of goods and services, excluding value added tax.

6. Pension costs

The pension costs are assessed in accordance with the advice of an independent actuary. The accounting cost for providing pensions is charged over the period during which the Company benefits from the services of employees. The cost is calculated so as to produce a substantially level percentage of the current and future pensionable payroll. Further details of the Company's pension scheme and the basis upon which the charge to the revenue account is determined are set out in note 21 to the financial statements.

7. Development costs

Expenditure on the development or enhancement of services is charged as an operating cost as incurred.

8. Deferred taxation

Provision for deferred taxation is made using the liability method except where, in the opinion of the directors, a liability or recovery is unlikely to arise in the foreseeable future.

Group revenue account

Year ended 31 March 1998

Continuing operations	Notes	**1998 £000**	1997 £000
Gross income			
Listing, trading, information and other services		**142,853**	136,703
Settlement		**418**	55,042
Total		**143,271**	191,745
Rebate		**(16,600)**	(10,000)
Net income after rebate	1	**126,671**	181,745
Operating costs	2	**(96,687)**	(122,392)
Operating surplus		**29,984**	59,353
Provision for Year 2000 and EMU modifications	5	**(16,523)**	(1,750)
Provisions for restructuring and SETS	6	**3,070**	(39,750)
Share of profits of joint venture	10	**274**	309
Net interest receivable	7	**7,255**	7,096
Surplus on ordinary activities before taxation		**24,060**	25,258
Taxation on surplus on ordinary activities	8	**(6,980)**	(8,164)
Surplus for the financial year transferred to reserves		**17,080**	17,094

Statement of total recognised gains and losses

	1998	1997
Surplus for the financial year	**17,080**	17,094
Other recognised gains and losses for the year:		
Unrealised surplus on the revaluation of tangible assets	**–**	21,094
Total recognised gains for the year	**17,080**	38,188

Note of historical cost profits and losses

	Notes	**1998**	1997
Surplus on ordinary activities before taxation		**24,060**	25,258
Difference between historical cost depreciation charge and the actual depreciation charge for the year calculated on the revalued amount	17	**1,910**	1,309
Historical cost surplus on ordinary activities before taxation		**25,970**	26,567
Historical cost surplus retained after taxation		**18,990**	18,403

Balance sheets

31 March 1998

	Notes	Group 1998 £000	Group 1997 £000	Company 1998 £000	Company 1997 £000
Fixed assets					
Tangible assets	9	**105,027**	111,149	**105,027**	111,149
Investments	10	**605**	595	**410**	463
		105,632	111,744	**105,437**	111,612
Current assets					
Debtors: due within one year					
General	11	**25,615**	26,315	**25,615**	26,315
Settlement	11	**–**	3,990	**–**	3,990
Deferred tax: due after more than one year	12	**11,404**	15,259	**11,404**	15,259
Investments – term deposits with banks		**177,350**	167,000	**177,350**	167,000
Cash at bank:					
General		**7,423**	7,427	**7,423**	7,427
Settlement		**–**	3,425	**–**	3,425
		221,792	223,416	**221,792**	223,416
Creditors: due within one year					
General	13	**49,122**	54,324	**49,141**	54,495
Settlement	13	**–**	7,415	**–**	7,415
		49,122	61,739	**49,141**	61,910
Net current assets		**172,670**	161,677	**172,651**	161,506
Total assets less current liabilities		**278,302**	273,421	**278,088**	273,118
Creditors: due after more than one year	14	**30,000**	30,000	**30,000**	30,000
Provisions for liabilities and charges	15	**65,584**	76,323	**65,584**	76,323
Net assets		**182,718**	167,098	**182,504**	166,795
Capital and reserves					
Called up share capital	16	**1**	1	**1**	1
Reserves:					
Revaluation	17	**54,460**	56,370	**54,460**	56,370
Capital redemption	17	**36,290**	37,750	**36,290**	37,750
Revenue	17	**91,967**	72,977	**91,753**	72,674
Total shareholders' funds		**182,718**	167,098	**182,504**	166,795
Analysed between:					
Equity shareholders' funds	17	**146,428**	129,348	**146,214**	129,045
Non-equity shareholders' funds	17	**36,290**	37,750	**36,290**	37,750
		182,718	167,098	**182,504**	166,795

The financial statements on pages 27 to 43 were approved by the Board on 28 May 1998 and signed on its behalf by:

Gavin Casey Chief Executive
Christine Dann Director of Business Operations

Group cash flow statement

Year ended 31 March 1998

	Notes	1998 £000	1997 £000
Net cash inflow from continuing operating activities	19(i)	**28,183**	72,389
Returns on investments and servicing of finance			
Interest received		**11,831**	11,899
Interest paid		**(3,059)**	(3,106)
Net cash inflow from returns on investments and servicing of finance		**8,772**	8,793
Taxation			
Corporation tax paid		**(14,712)**	(10,295)
Capital expenditure			
Payments to acquire tangible fixed assets		**(9,635)**	(6,196)
Receipts from sale of tangible fixed assets		**1,056**	318
Net cash outflow from capital expenditure		**(8,579)**	(5,878)
Net cash inflow before use of liquid resources and financing		**13,664**	65,009
Management of liquid resources			
Increase in term deposits	19(ii)	**(10,350)**	(102,000)
Financing			
Redemption of 'A' shares		**(1,460)**	(1,320)
Increase/(decrease) in cash in the year	19(ii)	**1,854**	(38,311)

Notes to the financial statements

1. Income	1998 £000	1997 £000
Analysis of income:		
Membership fees	**1,726**	1,660
Listing	**32,948**	30,248
Trading	**37,380**	37,254
Information services	**61,673**	60,371
Settlement services	**418**	55,042
Other income	**9,126**	7,170
Gross income	**143,271**	191,745
Rebate	**(16,600)**	(10,000)
Net income after rebate	**126,671**	181,745

The rebate is payable to member firms in 1998 based on income received during the year from trading services and annual membership fees. The rebate in 1997 was based on income received from trading and settlement services.

2. Operating costs		
Operating costs include:		
Depreciation of tangible assets	**14,720**	18,253
Operating lease rentals – properties	**5,203**	5,212
– plant and machinery	**–**	27
Auditors' remuneration	**112**	198
Other fees payable to Coopers & Lybrand (see note i)	**389**	202
Fees payable to the Financial Services Authority	**1,286**	1,230

Notes

i) Other fees payable to Coopers & Lybrand, the Company's auditors, are primarily in respect of taxation, pensions, actuarial and consulting services.

ii) The revenue account includes £2,474,000 (1997, £2,443,000) for the operating costs of the Regulatory News Service. Total income for this service for the year ended 31 March 1998 was £506,000 (1997, £586,000).

3. Employees	1998	1997
Employees of the Group and their employment costs are summarised below.		
The number of employees was:		
At the year end	**529**	750
Average for the year	**573**	872
Staff costs during the year amounted to:	**£000**	£000
Wages and salaries	**22,451**	26,732
Social security costs	**2,275**	2,768
Other pension costs	**1,524**	3,359
Total	**26,250**	32,859

4. Directors' emoluments

The report of the Senior Appointments and Remuneration Committee on directors' remuneration is on page 24.

	1998				1997				**1998**	1997
	Salary* £	Performance Bonus** £	Benefits £	**Total £**	Salary* £	Performance Bonus** £	Benefits £	Total £	**Pensions (Note i) £**	Pensions (Note i) £
Chairman										
J Kemp-Welch	250,000	–	3,113	**253,113**	196,603	–	2,692	199,295	**–**	–
Chief Executive										
G F Casey (in 1997 from 5 August 1996)	307,250	160,000	9,421	**476,671**	187,775	55,528	5,615	248,918	**66,600**	40,774
Executive directors										
C L Dann (note i)	200,000	120,000	11,316	**331,316**	179,000	98,230	11,181	288,411	**–**	–
R P Kilsby	209,000	120,000	697	**329,697**	185,444	99,430	6,968	291,842	**–**	–
pension provision (note i)	45,000			**45,000**	40,882			40,882		
F Wicker-Miurin resigned 31 December 1997	131,692	51,000	10,400	**193,092**	171,200	98,230	13,404	282,834	**29,625**	39,500
G E Vardey resigned 31 March 1997	–	–	–	**–**	189,700	81,030	4,518	275,248	**–**	30,000
	1,142,942	451,000	34,947	**1,628,889**	1,150,604	432,448	44,378	1,627,430	**96,225**	110,274
Adjustment to bonus payments for period to 31 March 1997, see note below**				**100,000**				–		
Compensation for contractual commitment										
F Wicker-Miurin				**167,696**				–		
G E Vardey				**–**				129,000		
Total emoluments for chairman and executive directors				**1,896,585**				1,756,430	**96,225**	110,274

*The salary figures above include a car allowance where this is provided in cash rather than the provision of a car which is shown as a benefit in kind.
**The arrangements for the bonus scheme are explained in the report of the Senior Appointments and Remuneration Committee on page 24. The bonus scheme was changed in 1997/8 to run for the financial year to 31 March rather than the calendar year to 31 December. An additional bonus is payable to GF Casey (£40,000), CL Dann (£30,000) and RP Kilsby (£30,000) for the period 1 January 1997 to 31 March 1997, to cover the change in bonus year.

		1998 Total £	1997 Total £	**1998 Pensions £**	1997 Pensions £
Non-executive directors' fees					
Directors in office throughout both years					
I G Salter – deputy chairman		**25,000**	22,500	**–**	–
G J Allen		**12,500**	12,500	**–**	–
G K Allen		**12,500**	12,500	**–**	–
J R H Bond		**12,500**	12,500	**–**	–
D H Brydon		**12,500**	12,500	**–**	–
M J P Marks		**12,500**	12,500	**–**	–
R A Metzler		**12,500**	12,500	**–**	–
I Plenderleith		**12,500**	16,087	**–**	–
M J H Radcliffe		**12,500**	12,500	**–**	–
N Sherlock		**12,500**	12,500	**–**	–
B Solomons		**12,500**	12,500	**–**	–
Directors who did not hold office for the whole of the two financial years					
R A Barfield	until 10 July 1997	**3,125**	12,500	**–**	–
S P Cooke	until 26 May 1997	**1,932**	13,433	**–**	–
M Kaneko	until 10 July 1997	**3,125**	12,500	**–**	–
P Meinertzhagen	from 22 May 1997	**10,759**	–	**–**	–
H W H Sants	from 5 December 1996	**12,500**	4,050	**–**	–
H N Verey	until 16 October 1996	**–**	6,764	**–**	–
Total non-executive directors' fees (note ii)		**181,441**	200,334	**–**	–
Total directors' emoluments		**2,078,026**	1,956,764	**96,225**	110,274

4. Directors' emoluments (continued)

Notes

i) Pensions

The Company provided additional emoluments to R P Kilsby of £45,000 (1997, £40,882) to apply towards his pension arrangements. No separate pension contributions are made.

Mrs C L Dann is a member of the Company's defined benefit scheme. The increase in the accrued benefit during the year was £8,727 (1997, £5,756), and the accumulated accrued pension at the end of the year was £78,768 (1997, £67,513). The transfer value of the increase in her accrued benefit during the year was £124,000 (1997, £52,100).

The Company made payments into senior executive defined contribution pension schemes for G F Casey and Mrs F Wicker-Miurin.

ii) Non-executive directors' fees

Fees paid directly to the employer companies of non-executive directors were £125,191, representing 12 directors (1997, £156,584, representing 14 directors).

iii) Waiver of emoluments

None of the directors waived emoluments during 1997 or 1998.

5. Provision for Year 2000 and EMU modifications

	1998 £000	1997 £000
Provision for Year 2000 and EMU modifications	**16,523**	1,750
Taxation	**(5,122)**	(577)

The provision is for the costs of preparing the Exchange's systems, and also to provide market testing services to member firms and customers in readiness for the Year 2000. The provision also covers the modifications required for EMU.

6. Provisions for restructuring and SETS

Changes to the Exchange's trading systems and support to the market to implement the Stock Exchange Electronic Trading Service (SETS)	**–**	18,000
Redundancy and restructuring costs	**–**	9,850
Increase in provision for leasehold properties	**–**	11,900
Rationalisation of settlement operations – release of surplus provision	**(3,070)**	–
Total (decrease)/increase in provisions	**(3,070)**	39,750
Taxation	**952**	(9,191)

Expenditure incurred to date is shown in note 15. The release of the surplus provision for rationalisation of settlement operations is mainly due to lower trading losses, compared with the sum provided, following careful management of the migration to CREST.

7. Interest

	1998 £000	1997 £000
Interest receivable:		
Bank deposits	**12,020**	12,025
Other	**553**	405
	12,573	12,430
Interest payable:		
On bank and other loans repayable after five years	**(3,038)**	(3,038)
Other interest	**(14)**	(75)
Interest on discounted provision for leasehold properties (see note 15)	**(2,266)**	(2,221)
	(5,318)	(5,334)
Net interest receivable	**7,255**	7,096

8. Taxation

Corporation tax for the year at 31% (1997, 33%)	**4,871**	17,126
Deferred taxation (see note 12)	**2,236**	(3,660)
Adjustment for previous years:		
Corporation tax	**(1,816)**	(6,094)
Deferred taxation	**1,619**	688
Joint venture	**70**	104
Taxation charge	**6,980**	8,164

The adjustments for previous years for corporation tax are in respect of assessments now agreed or in discussion with the Inland Revenue.

9. Tangible assets	Land and buildings Freehold £000	Leasehold £000	Plant and equipment £000	Service equipment £000	Total £000
GROUP & COMPANY					
Cost or valuation:					
1 April 1997	153,400	4,787	13,944	54,581	226,712
Additions	647	–	1,792	7,196	9,635
Disposals	(7,231)	(95)	(4,150)	(16,120)	(27,596)
31 March 1998	**146,816**	**4,692**	**11,586**	**45,657**	**208,751**
Depreciation:					
1 April 1997	61,420	4,787	10,443	38,913	115,563
Provision for the year	5,028	–	2,028	7,664	14,720
Disposals	(6,648)	(95)	(3,721)	(16,095)	(26,559)
31 March 1998	**59,800**	**4,692**	**8,750**	**30,482**	**103,724**
Net book values:					
31 March 1998	**87,016**	**–**	**2,836**	**15,175**	**105,027**
1 April 1997	91,980	–	3,501	15,668	111,149
Net book values at 31 March 1998 are analysed as follows:					
Valuations	86,378	–	–	–	86,378
Cost less depreciation	638	–	2,836	15,175	18,649
	87,016	**–**	**2,836**	**15,175**	**105,027**

Notes

i) Freehold land and buildings include freehold properties and the associated fixed plant. All freehold properties were revalued as at 31 March 1997 by DTZ Debenham Thorpe, International Property Advisors, in accordance with the RICS Appraisal and Valuation Manual. The Directors reviewed the valuations at 31 March 1997 and were of the opinion that the total value of freehold properties amounted to £91,980,000 based on the Existing Use Value or Open Market Value as appropriate.

ii) Based on historical cost at 31 March 1998, the aggregate cost of Group tangible assets was £169,269,000 (1997, £187,230,000) and the aggregate depreciation was £118,702,000 (1997, £132,451,000).

10. Fixed asset investments

	Joint venture note (i) £000	Subsidiary undertakings Shares note (ii) £000	Loans £000	Other note (iii) £000	Total £000
These represent investments in subsidiary and joint venture undertakings and other investments made by the Company.					
a) GROUP					
Cost:					
1 April 1997	**205**	**–**	**–**	**390**	**595**
Share of retained profit	**10**	**–**	**–**	**–**	**10**
31 March 1998	**215**	**–**	**–**	**390**	**605**
b) COMPANY					
Cost:					
1 April 1997	**–**	**73**	**–**	**390**	**463**
Repayment of share capital	**–**	**(48)**	**–**	**–**	**(48)**
Exchange loss	**–**	**(5)**	**–**	**–**	**(5)**
31 March 1998	**–**	**20**	**–**	**390**	**410**

Notes

(i) Joint venture

The Company owns 50 per cent of the 100 £1 issued equity shares in FTSE International Limited, a company which distributes financial information. FTSE International Limited is a joint venture owned together with The Financial Times Limited, a subsidiary of Pearson plc, and is incorporated in Great Britain. The Company is entitled, under a shareholders agreement, to receive royalties from FTSE International Limited. At 31 March 1998, the Company was owed £258,000 by FTSE International Limited (1997, £110,000 was owed to FTSE International Limited). The Group investment of £215,000 shown above represents the Exchange's share of the joint venture's net assets as at 31 December 1997.

The Company's share of the joint venture company is:	Year to 31 December 1997 £000	13.5 months to 31 December 1996 £000
50% share of:		
Turnover	**2,993**	2,184
Operating profit	**249**	297
Interest receivable	**25**	12
Gross assets	**1,584**	955
Gross liabilities	**1,369**	750

In view of the lack of materiality, the above figures are provided in this note rather than in the primary statements.

The following amounts were receivable from FTSE International Limited during the year:	1998 £000	1997 £000
Royalties	**1,924**	1,487
Facilities management and other data services	**237**	164
Rent and service charges	**83**	69
Other miscellaneous charges	**2**	23
Dividend for the year ended 31 December 1997	**194**	–
	2,440	1,743

(ii) Subsidiary undertakings

The Company holds directly or indirectly 100 per cent of the ordinary shares, being the only class of shares in issue, of all its subsidiaries, none of which has actively traded during the year. A full list of subsidiaries will be annexed to the next annual return of the Company.

(iii) Other investment

The other investment of £390,000 represents the cost of the Company's 3.2 per cent interest in unlisted redeemable fixed interest shares in CRESTCo Limited.

11. Debtors: due within one year

	Group		Company	
	1998 £000	1997 £000	**1998 £000**	1997 £000
Trade debtors – General	**9,596**	10,070	**9,596**	10,070
– Settlement	**–**	3,990	**–**	3,990
Amounts owed by joint venture	**258**	–	**258**	–
Other debtors	**718**	623	**718**	623
Prepayments and accrued income	**15,043**	15,622	**15,043**	15,622
	25,615	30,305	**25,615**	30,305
Representing:				
General	**25,615**	26,315	**25,615**	26,315
Settlement	**–**	3,990	**–**	3,990
	25,615	30,305	**25,615**	30,305

12. Deferred taxation: due after more than one year

	£000
1 April 1997	15,259
Charge to revenue account during the year	(3,855)
31 March 1998	**11,404**

The deferred taxation balance is in respect of timing differences which are expected to reverse within the foreseeable future and comprises:

	1998 £000	1997 £000
Tax allowances available in excess of related depreciation	**2,355**	3,201
Other timing differences	**9,049**	12,058
	11,404	15,259
Potential deferred taxation assets, not recognised in these accounts, comprise:		
Tax allowances in excess of related depreciation	**3,543**	9,651
Other timing differences	**9,981**	8,148
	13,524	17,799

The disposal of properties at the revalued amount would not give rise to a tax liability.

13. Creditors: due within one year

	Group 1998 £000	Group 1997 £000	Company 1998 £000	Company 1997 £000
Bank overdraft	**–**	1,858	**–**	1,858
Trade creditors – General	**5,292**	4,154	**5,292**	4,154
– Settlement	**–**	7,415	**–**	7,415
Amounts owed to subsidiary undertakings	**–**	–	**19**	210
Amounts owed to joint venture	**–**	110	**–**	110
Corporation tax	**4,633**	16,290	**4,633**	16,251
Other taxation and social security	**2,410**	3,840	**2,410**	3,840
Other creditors	**3,486**	3,050	**3,486**	3,050
Accruals and deferred income	**33,301**	25,022	**33,301**	25,022
	49,122	61,739	**49,141**	61,910
Representing:				
General	**49,122**	54,324	**49,141**	54,495
Settlement	**–**	7,415	**–**	7,415
	49,122	61,739	**49,141**	61,910

The liability at 31 March 1997 in respect of settlement arose from the functions of the Company as the principal responsible for the central clearing house for the settlement of transactions in securities and the collection of stamp duty. The total liability was matched by debtors and cash.

14. Creditors: due after more than one year

	1998 £000	1997 £000
Repayable in five years or more – otherwise than by instalments		
10 1/8 per cent Mortgage Debenture Stock 2016	**30,000**	30,000

The 10 1/8 per cent Mortgage Debenture Stock 2016 is secured by a mortgage on the freehold site and buildings known as The Stock Exchange, London. The Company may purchase and cancel any of the stock at any time and except in so far as previously purchased or redeemed and cancelled, the stock will be redeemed at par on 1 November 2016. Earlier redemption of the stock in certain circumstances could be at an amount above par.

15. Provisions for liabilities and charges	Pensions note (i) £000	Property note (ii) £000	Rationalisation note (iii) £000	Year 2000 & EMU note (iv) £000	SETS note (v) £000	Total £000
1 April 1997	1,942	37,524	20,322	1,750	14,785	76,323
Utilised during the year	(198)	(3,354)	(11,948)	(921)	(10,037)	(26,458)
Interest on discounted provision	–	2,266	–	–	–	2,266
Provided (released) in the year (see notes 5 & 6)	–	–	(3,070)	16,523	–	13,453
31 March 1998	**1,744**	**36,436**	**5,304**	**17,352**	**4,748**	**65,584**

Notes

i) The pensions provision represents a pension surplus which arose in 1990 and is being released to the revenue account over the expected remaining service lives of scheme members in accordance with the accounting policy for pension costs.

ii) The property provision represents the estimated net present value of future costs for lease rentals less the expected receipts from sub-letting for those properties which are surplus to business requirements.

iii) The rationalisation provision represents the estimated costs for the rationalisation of settlement operations (see note 6) and further redundancy and restructuring costs.

iv) The provision for Year 2000 and EMU covers the costs of preparing the Exchange's systems and also to provide market testing services to member firms and customers in readiness for the Year 2000. The provision also covers the modifications required for EMU.

v) The SETS provision represents the estimated costs for changes to the Exchange's trading systems and support to the market for implementation and subsequent modification as required for the Stock Exchange Electronic Trading Service (SETS) (see note 6).

16. Share capital	**1998 £000**	1997 £000
The authorised share capital comprises 5,601 'A' shares and 14,399 'B' shares of 5p each.		
Issued, called up and fully paid		
3,629 'A' shares of 5p (1997, 3,775 shares)		
14,399 'B' shares of 5p (1997, 14,399 shares)	**1**	1

Each 'A' share of 5p shall be redeemed at a price of £10,000 (i) in the case of a shareholder being a natural person, not earlier than attaining 60 years of age or on death or insolvency, or (ii) in the case of a shareholder who is not a natural person, on 31 December 2026.

The shares are non-voting and have a preferential right to be redeemed on a winding up. The premium on these redemptions is charged to the capital redemption reserve.

If the shares are redeemed when the shareholder reaches the age of 60, they would be redeemed as follows:

Redemption period	**1998 No of shares**	1997 No of shares
Within 5 years	**1,256**	945
Between 5 and 10 years	**1,047**	1,109
Between 10 and 15 years	**595**	789
Between 15 and 20 years	**419**	462
After 20 years	**312**	470
	3,629	3,775

17. Reserves

	Group			Company		
	Revaluation £000	Capital redemption £000	Revenue £000	Revaluation £000	Capital redemption £000	Revenue £000
1 April 1997	56,370	37,750	72,977	56,370	37,750	72,674
Surplus for the financial year	–	–	17,080	–	–	17,169
Premium paid to 'A' shareholders (see note 16)	–	(1,460)	–	–	(1,460)	–
Transfer, representing the amount in the current year by which the depreciation charge for revalued assets exceeds the historic cost depreciation	(1,910)	–	1,910	(1,910)	–	1,910
31 March 1998	**54,460**	**36,290**	**91,967**	**54,460**	**36,290**	**91,753**

The Exchange's Articles of Association provide that the revenue reserves of the Exchange are not distributable to members except with regard to the redemption of the 'A' shares or in case of the dissolution of the Company. This provision may be amended by special resolution.

Equity shareholders' funds on the balance sheet comprise the issued share capital of 'B' shares together with the revaluation and revenue reserves. Non-equity shareholders' funds comprise the issued share capital of 'A' shares and the capital redemption reserve.

As explained in note 16, the 'A' shares have preferential rights to be redeemed on a winding up.

18. Reconciliation of movements in shareholders' funds

	1998 £000	1997 £000
Surplus for the financial year	**17,080**	17,094
Redemption of 'A' shares	**(1,460)**	(1,320)
Unrealised surplus on the revaluation of tangible assets	**–**	21,094
Net addition to shareholders' funds	**15,620**	36,868
Opening shareholders' funds	**167,098**	130,230
Closing shareholders' funds	**182,718**	167,098

19. Notes to the Group cash flow statement

	1998 £000	1997 £000
i) Analysis of continuing operating activities		
Operating surplus	**29,984**	59,353
Depreciation of tangible assets	**14,720**	18,253
Profit on disposal of tangible assets	**(19)**	(129)
Decrease in debtors	**1,086**	2,657
Increase in creditors	**8,870**	7,793
Expenditure relating to exceptional items	**(26,458)**	(15,538)
Net cash inflow from continuing operating activities	**28,183**	72,389

Changes in debtors and creditors exclude those relating to settlement as these, together with the changes in settlement cash balances, do not give rise to a movement in net current assets.

	1998 £000	1997 £000
ii) Reconciliation of net cash flow to movement in net funds		
Increase/(decrease) in cash in the year	**1,854**	(38,311)
Increase in liquid resources	**10,350**	102,000
Change in net funds	**12,204**	63,689
Net funds at 1 April 1997	**142,569**	78,880
Net funds at 31 March 1998	**154,773**	142,569

iii) Analysis of changes in net funds	At 1 April 1997 £000	Cash Flows £000	**At 31 March 1998 £000**
Cash in hand and at bank	7,427	(4)	**7,423**
Bank overdrafts	(1,858)	1,858	**–**
	5,569	1,854	**7,423**
Debt due after more than one year	(30,000)	–	**(30,000)**
Current asset investments	167,000	10,350	**177,350**
Total net funds	142,569	12,204	**154,773**

20. Commitments	1998 £000	1997 £000
Contracted capital commitments not provided for in the accounts	**1,270**	5,667

The contracted commitments were mainly in respect of building refurbishment and computing facilities.

Financial commitments under property operating leases at 31 March 1998 for payments in the year to 31 March 1999 are as follows:

Leases expiring – in one year	**51**	168
– between two and five years	**237**	200
– in five years or more	**4,811**	4,862
	5,099	5,230

21. Pension costs

The Company operates a non-contributory pension plan providing benefits based on final pensionable pay. The assets of the plan are held separately from those of the Company and the funds are managed, on behalf of the trustee, by Schroder Investment Management Limited. Pension costs are charged to the revenue account so as to spread the costs of pensions over employees' working lives with the Company. The pension costs are determined by an independent qualified actuary on the basis of regular valuations now using the attained age method. With effect from 31 March 1997 the Exchange decided to improve the guaranteed level of pension increases from 3 per cent a year to be in line with price inflation subject to a maximum of 5 per cent and a minimum of 3 per cent a year.

The most recent actuarial valuation was carried out at 31 March 1997. The assumptions which have the most significant effect on the results of the valuation are those relating to the rate of return on investments and the rates of increase in pensionable pay and pensions. The principal assumptions for the March 1997 valuation were that over the long term (i) the annual rate of return on equity investments would be 2 per cent above the real return on the Government's RPI-linked gilts, (ii) the increase in pensionable pay would be two per cent above inflation and (iii) pension increases would be in line with inflation. Contributions to the pension plan are made in accordance with advice given by an independent qualified actuary. These were paid at a rate of 16 per cent of pensionable payroll up to 31 August 1997 and, following the results of the recent actuarial valuation, no further contributions were paid for the remainder of the financial year (1997, 16 per cent).

In addition to the Company's contributions to the pension plan, the Company matches certain additional voluntary contributions by employees; in the year to 31 March 1998 the cost of this match amounted to £208,000 (1997, £274,000).

As an alternative to being members of the pension plan, employees may opt for a personal pension. The Company will make contributions to these personal pensions instead of its contribution to the main plan. In the year to 31 March 1998 the cost of these contributions amounted to £509,000 (1997, £532,000).

The total pension charge for the year was £1,524,000 (1997, £3,359,000).

The actuarial valuation at 31 March 1997 showed that the market value of the plan's main assets was £115,000,000, excluding investments valued at £6,400,000 bought with members' additional voluntary contributions and with matching contributions from the Exchange. The actuarial value of the main assets represented 135 per cent of the value of benefits that had accrued to the members, after allowing for expected future increases in earnings. Following the valuation, and following advice from the plan's actuary, the Exchange ceased contributions to the plan for the time being. The Exchange and the plan trustee will keep the funding position of the plan under review.

22. Transactions with related parties

During the financial year, no contracts of significance were entered into by the Company or any of its subsidiaries in which the Directors had a material interest.

FTSE International Limited
Details of transactions with FTSE International are included in note 10.

ProShare (UK) Limited
During 1997, three of the Company's directors were non-executive directors of ProShare (UK) Limited although for various reasons they have since resigned. The Exchange continues to support the work of ProShare both through a contribution and joint co-operation on specified projects. The Company provided property space to ProShare (UK) Limited for a charge of £59,000 (1997, £55,000). The Company also makes a contribution to the annual expenditure of ProShare (UK) Limited. The contribution during the year was £350,000 (1997, £400,000).

23. Share interests of directors

The following directors were each the beneficial owner of one 'A' share of the Company as at 1 April 1997 or at subsequent appointment and at 31 March 1998:

G F Casey	I G Salter
J Kemp-Welch	H W H Sants
M J P Marks	N Sherlock
P R Meinertzhagen	B Solomons

There have been no changes in the above interests since 31 March 1998.

During the year no director or member of a director's immediate family was granted or exercised any right to subscribe for shares in or debentures of the Company or any other body corporate in the Group.

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