

M&G Group P.L.C. Annual Report & Accounts 1997

Registered Number 633480



M&G

M&G Group P.L.C., an independent company listed on the London Stock Exchange, was established as an investment management company in 1931 and was the UK's first unit trust provider. We market investments to the public through a wide range of unit trusts, Personal Equity Plans, investment trusts and unit-linked life and pension policies. We also provide investment management services to company pension funds, charities and other institutional clients. The Group now has £18.1 billion under management and over 750,000 customers.

M&G has a distinctive investment philosophy based on a reluctance to follow fashion, a bottom-up approach to stock selection and a long-term view of investment and performance. We manage funds which, collectively, hold over 5% of the share capital of some 250 companies and we take our responsibilities as a large shareholder very seriously. We believe strongly that we should have a constructive dialogue with the management of companies in which we have a significant interest. We always vote on company resolutions but are wary of imposing rigid rules, believing that every situation must be considered in the light of each company's particular circumstances.

Good performance, marketed imaginatively and supported by efficient and accessible service, will deliver strong long-term earnings and dividend growth to our shareholders.

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Financial Highlights

for the year ended 30th September 1997

| | 1997 | 1996 | % Change | |
|---------------------------------|------------------|---------|----------|----|
| Profit before tax | £67.4m | £64.5m* | 4 | |
| Earnings per share | 61.9p | 59.2p† | 5 | |
| Final dividend per share | 24.0p | 20.0p | 20 | |
| Dividend per share for the year | 40.0p | 36.0p | 11 | |
| Net assets per share | £4.15 | £3.68 | 13 | |
| Funds managed by M&G | £18.1bn | £15.6bn | 16 | |
| FTSE All-Share Index | – period end | 2,455 | 1,945 | 26 |
| | – period average | 2,136 | 1,842 | 16 |
| Retail Prices Index | – period end | 159.3 | 153.8 | 4 |

*The 1996 profit before tax before exceptional items was £72.1m.

†The 1996 earnings per share before exceptional items was 66.2p.

Financial Calendar

Group Year End
30th September 1997

Annual General Meeting
14th January 1998

Payment of Final Dividend
15th January 1998

Announcement of Interim Results
7th May 1998

Payment of Interim Dividend
2nd July 1998

Dear Shareholder,

Pre-tax profits have risen from £64.5 million to £67.4 million, an increase of 4%, and earnings per share have increased by 5% from 59.2p to 61.9p. However, the previous year's results included £7.6 million of exceptional costs and before these expenses, profit before tax and earnings per share were £72.1 million and 66.2p respectively.

We have increased the final dividend from 20p to 24p, bringing the total for the year to 40p, an increase of 11%. This is a measure of our confidence in the Group's prospects and is well covered by the year's earnings. The Group's net assets increased to £310 million, equivalent to £4.15 per share.

Funds under management have risen over the year from £15.6 billion to £18.1 billion, an increase of 16%.

For much of the year our fund performance did not match the growth in the FTSE All-Share Index. This had an impact on both annual and initial fee revenue. Growth in funds under management, on which our annual fee income depends, was held back both by the relative underperformance of our funds and a consequent increase in redemptions. Sales of new products were also affected and this reduced the level of initial fee income.

The rise in marketing expenditure of £8 million was due to two factors. We spent £2 million on television advertising, commissioned to maintain our brand strength in the face of increased competitive pressure in the industry. This was a highly successful exercise, more than trebling M&G's name awareness among our target

market. We also saw a 26% increase in costs relating to no initial charge products. This rise reflects the continuing success we have had in selling Managed Income Fund and Corporate Bond Fund PEPs.

Administration expenses at £54 million were 8% higher than the figure for last year, excluding exceptional items. This year we started to adapt our IT systems to cope with the year 2000 and the expenses include £1.6 million of our expected £5 million total spend on this project. If the expenditure on year 2000 and our fund changes is stripped out, the underlying increase in administration costs is under 3%.

It has been a difficult year for our UK equity unit trusts as our traditional investment philosophy is to seek undervalued and often unfashionable or unpopular shares. While this approach has been successful over long periods, for much of the past year the growth in the FTSE All-Share Index was essentially accounted for by just a handful of very large banking, pharmaceutical and oil company shares. At the same time smaller and medium-sized companies were largely ignored and companies with a high yield remained relatively undervalued. It is encouraging that the real value in smaller and medium-sized companies is now beginning to be realised, and since August we have seen a sharp upturn in our fund performance.

It has been a year of positive change for M&G. Michael McLintock took over as Chief Executive of the Group in February and under his direction the management

a sharp upturn in fund performance

team has undertaken several major initiatives that will stand the Group in excellent stead for the future.


- We have made a number of key management appointments across the business to strengthen the existing team.
- We have completed a review of M&G's unit trust range and our proposals were approved overwhelmingly by unitholders. The UK fund range now offers a much clearer and more relevant choice of funds to investors.
- M&G attracted over 10,000 new investors by agreeing to hold building society windfall shares in a PEP. We hope that over time these customers will be persuaded to invest in other M&G products.
- M&G launched a new defined contribution pension product into the institutional market and has had encouraging success in selling this product.

Michael McIntock's review and outlook, which follows, gives more details on these points.

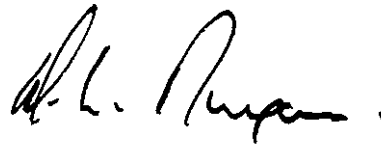
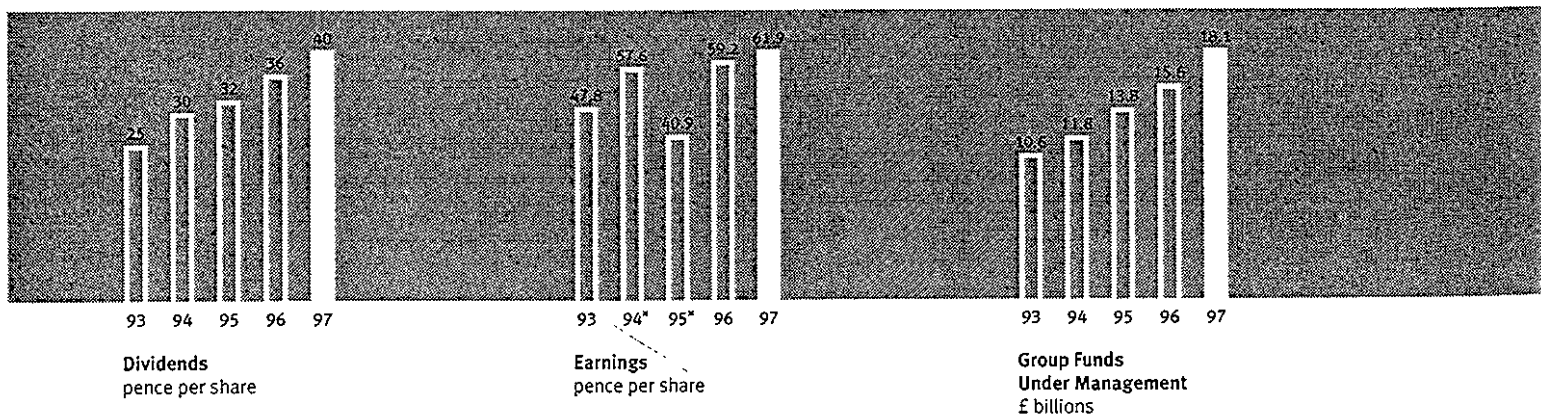
This year saw the new Labour Government come to power. In Labour's first budget the Chancellor announced that the existing regime of Personal Equity Plans (PEPs) and Tax Exempt Saving Schemes (TESSAs) would be replaced in 1999 by a new tax-favoured savings vehicle, the Individual Savings Account (ISA). It is presently unclear what form the ISA will take, but M&G has put proposals to the Government which stress that, if confidence in Government-sponsored savings initiatives is to be

fostered, existing PEP and TESSA savers who have built up significant investments over the long term should not be penalised by the introduction of this new savings vehicle.

We are encouraged by the Government's determination to provide a workable solution for the nation's pension provision. The idea of stakeholder pensions will encourage individuals to take more responsibility for their own standard of living in retirement. As with ISAs it is too early to know exactly what form the new pensions vehicle will take but we believe that the pensions and investment markets, previously distinct from each other and served by two different sets of product providers, are gradually converging into a single savings market. Those companies with a reputation for good long-term investment performance supported by accessible, efficient service and a strong retail brand have the best chance of succeeding as this market emerges. M&G fits these criteria as well as any of its current or likely competitors. The new management team is keenly aware of the opportunity open to the Group and it is with confidence I predict that M&G will be one of the winners as the single savings market becomes a reality.



David Morgan
Chairman, 26th November 1997

As advised to shareholders on 27th March 1996, the results are prepared on the 'modified statutory solvency' basis. *The figures for 1994 and 1995 have been restated on this basis for comparative purposes.

The Directors

Non-Executive

D L Morgan

(Non-Executive Chairman and member of the Remuneration Committee). Age 63. Joined M&G in 1972 from E D Sassoon.

J S Fairbairn DL

(Non-Executive, and a member of the Remuneration Committee). Age 63. Joined the Board in 1974. An executive with M&G, 1961-1989, and Joint Deputy Chairman, 1979-1989. Chairman of the Esmée Fairbairn Charitable Trust since 1988, Chairman of the Unit Trust Association, 1989-1991, and Deputy Chairman of Lautro, 1986-1989.

H R Collum

(Non-Executive, Chairman of the Audit Committee and a member of the Remuneration Committee). Age 57. Joined the Board in 1992. Executive Vice President and Chief Financial Officer of SmithKline Beecham plc, a non-executive director of Safeway plc and was a member of the Cadbury Committee on the Financial Aspects of Corporate Governance.

A G Down

(Non-Executive, and a member of the Audit and Remuneration Committees). Age 59. Joined the Board in 1980. A Trustee of the Esmée Fairbairn Charitable Trust, and a director of several other companies.

R D Kent

(Non-Executive, Chairman of the Remuneration Committee and a member of the Audit Committee). Age 50. Joined the Board in 1995. Managing Director of Close Brothers Group plc. Non-executive director of Wessex Water plc and English and Scottish Investors plc.

E C S Macpherson

(Non-Executive, and a member of the Remuneration Committee). Age 55. Joined the Board in August 1996. Formerly Chief Executive of 3i Group plc.

Executive

M G A McIntock
(Group Chief Executive). Age 36.
Joined M&G in 1992 from
Barings.

V P Bazalgette
(Managing Director of M&G
Investment Management).
Age 46. Joined M&G in 1996
from LGT Asset Management.

P A Emms
(Group Marketing and Sales
Director). Age 48. Joined M&G
in 1992 having previously worked
at Allied Dunbar plc.

M Lewis
(Administration and Information
Technology Director). Age 41.
Joined M&G in 1996 from Chase
Manhattan Bank. He was
appointed to the Board
in February 1997.

R S Hughes
(Vice Chairman of M&G
Investment Management).
Age 40. Joined M&G in 1986
from Derbyshire County Council.

D K Watson
(Finance Director). Age 38.
Chartered Accountant. Joined
M&G in 1994 from NatWest
Securities.

Other Officers

A J Ashplant
(Head of Legal and Compliance).
Age 43. Barrister-at-Law. Joined
M&G in 1983 from Craigmyle &
Company, having previously
practised at the Bar.

S H Henton
(Company Secretary). Age 58.
Fellow of the Institute of
Chartered Secretaries and
Administrators. Joined M&G
in 1996 from Amersham
International plc.

L J Scrine
(Group Actuary). Age 39. Fellow
of the Institute of Actuaries.
Joined M&G in 1982 from
Commercial Union.

"M&G is staffed by able and motivated individuals who share a common energy and determination to see the Group succeed."

Michael McIntuck
Chief Executive

Chief Executive's Review and Outlook

Since I took over as Chief Executive in February, the main focus of my attention has been in two areas: to recruit talented individuals to expand the management team across the business, and to update our fund range. Whilst these have been the most high profile changes, this has been a year of intense activity and change across the whole Group.

People

Our future success depends upon the quality of the people in the business and over the past year we have made a number of key appointments. To the main board we welcomed Vivian Bazalgette in November, as Managing Director of M&G Investment Management, and Martin Lewis in February, as Director of IT and Administration. In the investment department we have, amongst others, appointed a new head of our UK equity funds; a new head of our smaller companies team; a new head of corporate analysis who will take special responsibility for corporate developments affecting companies in which we have large stakes; and new institutional and fixed interest fund managers. We have also appointed key people in direct marketing and administration, reflecting the need to focus more of our efforts on the service we can offer to existing and prospective customers, as well as in finance and IT. Everywhere the new arrivals have brought with them fresh perspectives from which the Group is benefiting.

Fund Changes

In March, we initiated a review of our UK range of unit trust funds. This was something that had not been done in M&G's 66-year history and was overdue. In some cases the fund objectives required updating, in others the

activity and change

The Updated Fund Range

| Old name | New name | Purpose |
|-------------------|-----------------------|-------------------------------------|
| Extra Yield | Extra Income | 50% yield premium to FTSE All-Share |
| Dividend | Dividend | 33% yield premium to FTSE All-Share |
| High Income | Income | 15% yield premium to FTSE All-Share |
| General | Blue Chip | Beat FTSE 100 |
| Second General | UK Equity | Beat FTSE All-Share |
| Smaller Companies | Smaller Companies | Beat HGSC Index* |
| Compound Growth | UK Growth | Growth |
| Recovery | Recovery | Recovery |
| Capital | Capital | Special Situations |
| Midland & General | British Opportunities | British Economy |
| Managed Income | Managed Income | Mixed asset fund of funds |

*Hoare Govett Smaller Companies Index

We wrote to over 500,000 M&G unitholders and 20,000 IFAs with details of our fund changes.

Chief Executive's Review and Outlook

differences between funds were unclear, and in one or two instances fund objectives had become inappropriate. The purpose of the review was to ensure that the fund range was entirely relevant for today's economic conditions and to introduce greater variety into our range of products, so giving more choice to our investors.

The key changes are in three areas:

- i) We are going to reduce the number of income funds from four to three and, by revising the objectives, offer a wider range of yield targets.
- ii) We have targeted two of our existing general funds to outperform key indices:
 - The M&G Blue Chip Fund (formerly M&G General Trust Fund) now aims to outperform the FTSE 100 Index.
 - The M&G UK Equity Fund (formerly the M&G Second General Trust Fund) invests across the UK stockmarket with the aim of beating the FTSE All-Share Index.
- iii) Among the capital growth funds the key change was to the M&G British Opportunities Fund (formerly the M&G Midland & General Trust Fund) which will become a more diversified fund investing in companies whose turnover originates mainly in the UK.

We communicated these changes to IFAs by means of a Roadshow this autumn. Over a two week period we

made presentations in London, Birmingham, Manchester, Leeds, Glasgow, Edinburgh, Belfast, Bristol, and Southampton, and the reception everywhere was extremely positive.

To date, the proposals have been overwhelmingly approved by unitholders. We are now much better placed to meet the needs of existing and new customers whatever the stage in the economic cycle.

To date,
M&G investors
have voted
overwhelmingly
in favour of our
fund changes

Our fund managers look after £18 billion on behalf of over 750,000 customers.

Vivian Bazalgette joined the Group as Managing Director of M&G Investment Management.

Investment Performance

UK Equity Investment

Over the year the FTSE All-Share Index rose by 26%, but this figure masks the highly unusual buying patterns that have dominated the UK market. For much of this year relatively few of the largest companies accounted for most of the rise, whilst investors tended to ignore the shares of smaller and medium-sized companies. In addition, the prevalence of special dividends over the past two years and fears about the new Government's attitude towards dividend taxation sharply reduced the demand for income shares. For the ten months to July 1997 the FTSE 100 Index grew by 24%, while the Mid 250 Index, which represents the medium-sized companies, grew by just 2% and the Hoare Govett Smaller Companies Index was unchanged. During this period the relative performance of M&G's UK equity unit trusts was badly affected by these distinctive patterns as we have tended to invest our portfolios with an emphasis on smaller and medium-sized companies or those which have a higher than average yield.

The period from August onwards saw markedly different buying behaviour in the UK stockmarket. The strength of the UK economy improved the appeal of smaller and medium-sized companies, and this, combined with the strong rise already seen in the FTSE 100 Index, made the popular large company shares look comparatively

expensive. As a result there was a strong improvement by smaller and medium-sized companies. In the final quarter of our year the M&G Recovery Fund was 6th out of the 156 funds in its sector and the M&G Dividend Fund was 2nd out of the 91 funds in its sector. The scale of the improvement affected figures for the six months as well; over the six months to the end of September, 8 of our 13 UK equity funds were above average in their sectors and I am pleased to report that the improving trend continued in October. A particular highlight of our investment performance was that our most popular PEP fund, the M&G Managed Income Fund, was 2nd out of the 80 funds in its sector over the year to the end of September. Our longer term performance figures remain strong; over five years 69% of our unit trusts by weight were above average in their sectors and over ten years 77% were above average.

Fixed Interest Investment

Our fixed interest funds continue to maintain their formidable performance, underlining their outstanding longer term record. This success was confirmed by the team jointly winning the "Express and Investment Week Fixed Income Fund Manager of the Year" award. Over the year, M&G Charibond was 1st out of the 14 funds in its sector, M&G Treasury Fund was 2nd out of 27 funds in its sector, M&G Gilt and Fixed Interest Fund was 5th out of 34 funds in its sector and M&G Corporate Bond Fund was 10th out of 72 funds in its sector.

| Funds Under Management | 1993 £m | 1994 £m | 1995 £m | 1996 £m | 1997 £m |
|---|---------------|---------------|---------------|---------------|---------------|
| Unit Trusts | 5,554 | 5,819 | 6,278 | 6,339 | 6,836 |
| Investment Trusts | 377 | 389 | 449 | 576 | 629 |
| PEPs | 880 | 1,407 | 2,013 | 2,639 | 3,273 |
| Life and Pensions | 2,143 | 2,384 | 2,651 | 2,845 | 3,164 |
| Institutional | 3,340 | 3,781 | 4,589 | 5,475 | 6,786 |
| Total Funds | 12,294 | 13,780 | 15,980 | 17,874 | 20,688 |
| Less adjustment to eliminate double counting* | (1,736) | (1,984) | (2,191) | (2,320) | (2,584) |
| Total Funds excluding double counting | 10,558 | 11,796 | 13,789 | 15,554 | 18,104 |

*The double counting is principally due to unit trust holdings by life and pension funds

We invest in every major stockmarket in the world.

Chief Executive's Review and Outlook

Overseas Equity Investment

The performance of our overseas funds was generally reasonable and, in certain areas, extremely good. The M&G American Recovery Fund was the top performing fund among the 117 unit trusts in its sector over one year and our specialist funds, M&G Australasian Fund and M&G Commodity Fund, both retained their leading positions in their respective sectors. The M&G European Smaller Companies Fund, launched in September 1996, completed its maiden year as the best performer in its category; it attracted a considerable following from investors and established a strong position in a growing niche market. Stockmarkets in Asia, which were both turbulent and difficult, proved unrewarding for investors but two of our core Asian funds, M&G South East Asia Fund and M&G Japan Smaller Companies Fund, produced results which compared favourably with others in their sector.

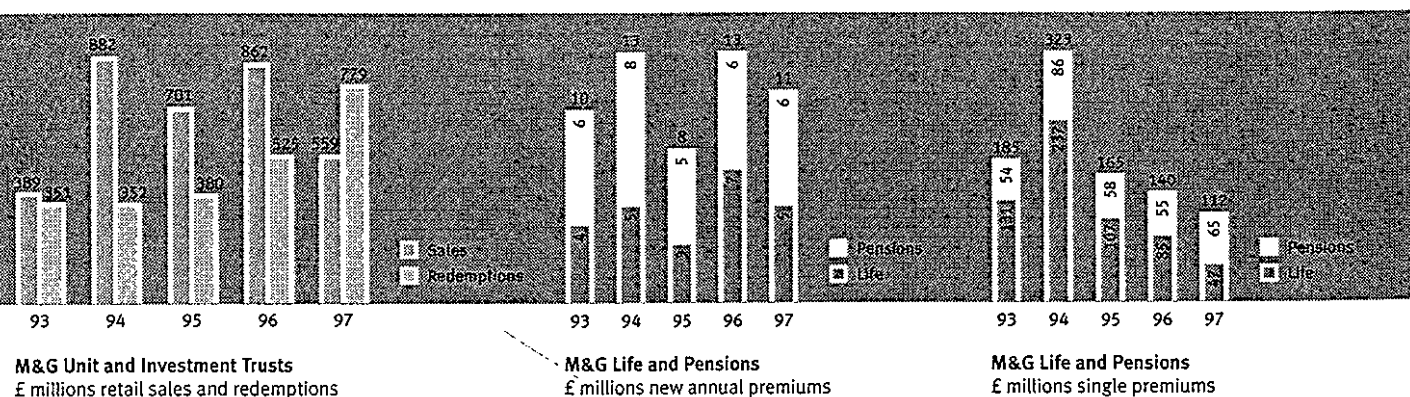
Institutional Investment

Over the course of the year, the funds managed by our institutional desk outperformed the sector average, as measured by the CAPS Median. M&G topped the table in the recent Financial Times survey of the performance over five years of leading managers of balanced segregated funds.

Retail Operations

The relative underperformance of our UK equity unit trusts for much of the year has overshadowed the Group's retail operations with the result that sales have been disappointing. Sales of unit trusts were down by 26% from £690 million to £511 million, while redemptions increased by 32% from £525 million to £693 million. The launch of the M&G High Income Investment Trust raised £20 million of additional funds against £156 million from the M&G Equity Investment Trust in the previous year. Excluding windfall shares, net PEP sales were £210 million compared to £554 million last year, whilst main register unit trusts saw an outflow of £347 million, up from £238 million last year. More encouragingly, however, the early indications are that our fund reorganisation proposals are having a positive effect on the level of net sales.

We opened a net 42,743 new PEP accounts, bringing the total to 519,372. This was helped by attracting £78 million of windfall shares from investors wishing to shelter them within the M&G PEP. Our success was partly due to our systems flexibility which allowed us to hold the individual shares within our PEP. Many of our competitors could only help customers who were willing to exchange their shares for units. We received over 10,000 windfall applications from investors who were



“We are pleased to see the recent performance of M&G improving. We have always felt comfortable recommending M&G and valued their long experience in the investment field.”

Amondo Davidson

Partner, Bolder Meenan, Independent Financial Advisers

Chief Executive's Review and Outlook

new to M&G and we hope that over time many of these people will invest further with us.

The M&G Corporate Bond Fund has consistently been one of the top performing funds in its sector since launch in April 1994. It has been an enormous success and has now grown to £597 million. Since the launch of the first of our no-load funds, the Managed Income Fund PEP, in February 1993, the total value of our three no initial charge funds has risen to £2.38 billion.

Following the significant increase in sales of regular premium life and pension products recorded last year, new regular life and pension premiums for the year fell from £13 million to £11 million.

Single premium life sales fell from £85 million to £47 million. This was in part due to the popularity of offshore unit-linked bonds. We believe that, despite their superficial appeal, these products generally offer poor value to customers and are now to be looked at by the Inland Revenue as part of their review of possible tax avoidance. During the year ahead we will be working hard to emphasise the relative merits of straightforward onshore UK equity investment. Our sales of single premium pensions rose from £55 million to £65 million, recording their second highest level ever.

Awareness amongst the public of the need to save and invest is growing all the time. This has been given particular stimulus by building society windfalls, which have resulted in the creation of many thousands of new investors, and by media comment about the "pensions timebomb" and the need for individuals to be financially self-sufficient. The challenge for the major unit trust providers is to convert this awareness into actual investment by presenting relevant products in an interesting way that stimulates response. We have been looking at the way in which we communicate with investors and we will be adapting our advertising style to become more accessible to a wider range of potential customers whilst building on the brand recognition and goodwill that we have developed over 66 years.

Independent Financial Advisers (IFAs) continue to account for half our sales of investment products and virtually all our sales of life and pensions products. The changes we make to our communications should help IFAs to sell M&G products. We are also working to improve the quality and timeliness of information we send them. Electronic trading, together with on-line enquiries and information, will become increasingly important to this distribution channel and we are at the forefront of industry developments in this area.

Our top performing Corporate Bond PEP has over 48,000 investors.

M&G manages pension funds for many large companies.

We take around 15,000 phone calls from customers a week.

| Number of Accounts | 1993 | 1994 | 1995 | 1996 | 1997 |
|------------------------|------------------|------------------|------------------|------------------|------------------|
| Unit Trusts | 637,564 | 748,933 | 815,954 | 849,401 | 831,166 |
| Investment Trusts | 59,873 | 58,116 | 57,877 | 86,017 | 88,817 |
| Windfall Shares | - | - | - | - | 25,816 |
| Life Policies | 289,264 | 323,555 | 315,960 | 304,118 | 277,332 |
| Pension Policies | 61,042 | 63,716 | 64,426 | 62,544 | 61,124 |
| Total* | 1,047,743 | 1,194,320 | 1,254,217 | 1,302,080 | 1,284,255 |
| Includes PEP accounts* | 194,076 | 304,757 | 389,732 | 476,629 | 519,372 |

| Retail Sales During the Year | | 1996 £m | 1997 £m |
|---|----------|------------|------------|
| Unit and Investment Trusts | | | |
| Gross Sales | | 862 | 559 |
| Redemptions | | (525) | (779) |
| Net Sales | | 337 | (220) |
| Windfall Shares | | - | 78 |
| PEP Gross Sales included within the above | | 656 | 487 |
| Life and Pension Policies | | | |
| Single Premiums | Life | 85 | 47 |
| | Pensions | 55 | 65 |
| New Annual Premiums | Life | 7 | 5 |
| | Pensions | 6 | 6 |
| Total Annual Premiums in Force (as at end of period) | | 80 | 80 |

Institutional Operations

The institutional side of our business has had a good year. Portfolios managed for pension funds and other institutional clients have grown by 24% from £5.5 billion last year to £6.8 billion and fees generated amounted to £9.7 million, a rise of 12%. We have won £229 million from new clients in the course of the year, on the back of an excellent long-term performance record which was recognised by the Financial Times, as already mentioned.

In March, we launched a new range of products designed for the rapidly expanding defined contribution market and have already attracted new clients to this service. This market is likely to grow strongly in the future as employers look to transfer ultimate responsibility for pension provision to employees. Although the market for defined contribution provision is already competitive and will become more so, M&G is particularly well placed, due to the unusual combination of our excellent long-term institutional investment record – defined contribution mandates are awarded on an institutional basis – and our high brand recognition amongst the public, which particularly appeals to employers seeking to encourage the greatest involvement by employees.

M&G – Top of the
Financial Times
five year performance
table for institutional
fund management

Chief Executive's Review and Outlook

Administration and Information Technology

Our Customer Services Centre has again experienced a record number of contacts with customers this year, up a further 22% over last year. Much of this increase was explained by the introduction of income tax self-assessment, enquiries ahead of the general election and the mass allocation of windfall shares.

In July, we upgraded the call centre technology and increased the number of staff. We have set demanding response and service standards and are determined to deliver continuing improvements in this area.

During the summer, M&G started to take building society windfall shares into PEP accounts. The Group was first in the industry to announce this capability and although we had only 11 weeks before the first share certificates arrived, new systems were quickly put in place and we processed over 29,000 applications without delay. The flexibility and strength of our systems have been at the heart of our success. These will again be of importance with the imminent introduction of ISAs.

The upgrades to our PEP and life bond processing capability were installed in January and proved their worth by enabling us to handle the tax year-end peak without temporary staff for the first time. For these products, we have been able to more than halve

the time it takes our staff to learn how to operate the new system.

Significant benefits are also coming from the investment in our customer database. The improved information increasingly allows us to send customers more relevant and tailored information which should help to increase sales and encourage longer retention of funds.

Our plan to amend our systems to make them Year 2000 compliant moved into full swing during the year. We remain on target to be ready before the end of 1998.

M&G received over
29,000 windfall
applications, 10,000
of which came from
new investors

The development of our database enables us to give customers more up-to-date and helpful information by phone and post.

This year, M&G accepted building society windfall shares into the M&G PEP.

"I have invested with M&G since 1986. What makes M&G special is the helpful and friendly service I have received in dealing with my investments – M&G is a company with a human face."

Miss Barbara Mackinnon
M&G Unitholder

Chief Executive's Review and Outlook

Conclusion

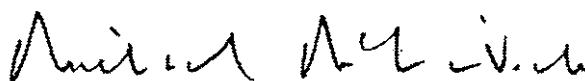
In the face of a difficult sales environment caused by below-average performance by a number of our UK equity funds, we have initiated change where we felt this to be necessary whilst recognising and building on the inherent strengths of the business. The improvement in UK fund performance now puts us in a good position to build on these developments to reverse the net redemptions we have seen over the year and take the business forward.

The immediate sales outlook is clouded by the volatility we have started to see in financial markets, and by the replacement of the existing PEP regime in 1999 with Individual Savings Accounts whose precise form is as yet unclear. Inevitably this introduces a higher element of uncertainty to our immediate prospects.

Over the medium and longer term, however, the dynamics for the fund management industry, and especially retail fund management, continue to look extremely favourable. Economic growth will produce an expanding pool of wealth for investment whilst the pensions and investment markets are likely to converge

as growing numbers of individuals save for their retirement. There are many businesses competing to share in this growth but M&G, with its strength of brand, investment heritage and unique position straddling the investment and pensions markets, is well placed to succeed.

Ultimately, however, the key ingredient that will determine whether or not we are one of the winners will be the quality of the people we employ, and here I have particular grounds for optimism. In all parts of our business M&G is staffed by able and motivated individuals who share a common energy and determination to see the Group succeed. With good people everything is possible and the team we have now assembled, both its long-standing members and those more recently joined, makes the future a promising one.



Michael McLintock
Group Chief Executive, 26th November 1997



Electronic communications will be an increasingly important means of communicating with customers and IFAs.

Our literature is being improved to become more accessible to a wider range of audiences.

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Consolidated Profit and Loss Account

| For the years ended 30th September | Note | 1997 £'000 | 1996 £'000 |
|--|------|---------------|---------------|
| Revenue | 1,2 | 152,231 | 146,604 |
| Marketing and commission expenditure | 3 | 46,276 | 38,255 |
| Administrative expenditure | 3,4 | 54,016 | 57,614 |
| Operating profit for the Group from continuing operations | 2 | 51,939 | 50,735 |
| Interest receivable and investment income | 7 | 15,419 | 13,762 |
| Profit before tax | 3 | 67,358 | 64,497 |
| Tax | 8 | 21,144 | 20,361 |
| Profit after tax attributable to shareholders | 9 | 46,214 | 44,136 |
| Dividends | 10 | 29,938 | 26,878 |
| Retained profit for the year | | 16,276 | 17,258 |
| Earnings per ordinary share of 25p | 10 | 61.9p | 59.2p |
| Earnings per ordinary share of 25p before exceptional items | 10 | 61.9p | 66.2p |

Statement of Total Recognised Gains and Losses

| | | |
|--|---------------|---------------|
| Profit after tax attributable to shareholders | 46,214 | 44,136 |
| Change in value of investments, after tax | 17,753 | (1,766) |
| Total recognised gains relating to the year | 63,967 | 42,370 |

The notes on pages 22 to 38 form an integral part of these accounts.

Consolidated Balance Sheet

| as at 30th September | Note | 1997 £'000 | 1996 £'000 |
|--|------|------------------|------------------|
| Employment of Capital | | | |
| Fixed assets | | | |
| Tangible fixed assets | 11 | 30,200 | 30,248 |
| Investments | 12 | 290,742 | 260,782 |
| Net assurance assets held to match unit-linked liabilities | 13 | 3,316,983 | 2,743,946 |
| Total fixed assets | | 3,637,925 | 3,034,976 |
| Current assets | | | |
| Stock | | 7,664 | 21,871 |
| Debtors due after more than one year | 14 | 24,609 | 27,036 |
| Debtors due within one year | 14 | 50,316 | 48,489 |
| Total debtors | | 74,925 | 75,525 |
| Investments | 12 | 36,629 | 18,950 |
| Cash at bank | 20 | 51,869 | 55,282 |
| Total current assets | | 171,087 | 171,628 |
| Creditors | | | |
| Amounts falling due within one year | 15 | 105,223 | 121,027 |
| Net current assets | | 65,864 | 50,601 |
| Total assets less current liabilities | | 3,703,789 | 3,085,577 |
| Creditors | | | |
| Amounts falling due after more than one year | 15 | 49,469 | 44,749 |
| Provision for liabilities and charges | | | |
| Provision for unit-linked liabilities | 13 | 3,316,983 | 2,743,946 |
| Deferred tax | 16 | 26,933 | 22,635 |
| Total capital employed | | 310,404 | 274,247 |

Equity Shareholders' Funds

| | | | |
|---|----|----------------|----------------|
| Capital and reserves | | | |
| Called up share capital | 17 | 18,717 | 18,643 |
| Share premium account | 18 | 6,744 | 4,690 |
| Revaluation reserve | 18 | 71,566 | 61,938 |
| Capital redemption reserve | 18 | 1,241 | 1,241 |
| Profit and loss account | 18 | 212,136 | 187,735 |
| Total equity shareholders' funds | | 310,404 | 274,247 |

Approved by the Board of Directors and signed on its behalf by:-

M G A McLintock

Directors

D K Watson

26th November 1997

The notes on pages 22 to 38 form an integral part of these accounts.

Reconciliation of Movements in Shareholders' Funds

for the Group and Parent Company

| for the years ended 30th September | Note | 1997 £'000 | 1996 £'000 |
|---|------|---------------|---------------|
| Profit after tax attributable to shareholders | | 46,214 | 44,136 |
| Dividends | | 29,938 | 26,878 |
| Retained profit for the year | | 16,276 | 17,258 |
| Other recognised gains and losses | | 17,753 | (1,766) |
| New share capital issued | 17 | 74 | 60 |
| Share premium on shares issued | | 2,054 | 1,340 |
| Shares redeemed | | - | (56) |
| Premium paid on purchase of own shares | | - | (2,596) |
| Net addition to equity shareholders' funds | | 36,157 | 14,240 |
| Opening equity shareholders' funds | | 274,247 | 260,007 |
| Closing equity shareholders' funds | | 310,404 | 274,247 |

Cash Flow Statement

| | Note | 1997 £'000 | Restated 1996 £'000 |
|--|------|---------------|---------------------------|
| Cash flow from operating activities | 20 | 50,795 | 65,065 |
| Returns on investments and servicing of finance | | | |
| Interest and investment income received (net of tax) | | 12,555 | 11,474 |
| Tax | | | |
| Corporation tax paid (including ACT) | | (18,456) | (17,419) |
| Capital expenditure and financial investment | | | |
| Purchases of tangible fixed assets | | (4,266) | (5,203) |
| Sales of tangible fixed assets | | 428 | 963 |
| Net cash outflow from capital expenditure and financial investment | | (3,838) | (4,240) |
| Equity dividends paid | | (26,882) | (25,386) |
| Cash inflow before use of liquid resources and financing | | 14,174 | 29,494 |
| Management of liquid resources | | | |
| Purchase of listed and unlisted liquid investments | | (54,532) | (83,137) |
| Sale of listed and unlisted liquid investments | | 34,817 | 57,153 |
| Net cash outflow from management of liquid resources | | (19,715) | (25,984) |
| Financing | | | |
| Issue of ordinary share capital | | 2,128 | 1,400 |
| Purchase of own shares | | - | (2,652) |
| Net cash inflow/(outflow) from financing | | 2,128 | (1,252) |
| (Decrease)/increase in cash in the period | 20 | (3,413) | 2,258 |

The notes on pages 22 to 38 form an integral part of these accounts.

Company Balance Sheet

as at 30th September

| | Note | 1997 £'000 | 1996 £'000 |
|--|------|----------------|----------------|
| Employment of Capital | | | |
| Fixed assets | | | |
| Investments | 12 | 272,667 | 238,700 |
| Current assets | | | |
| Amounts owed by subsidiary undertakings | | 57,246 | 52,863 |
| Sundry debtors | | 99 | 72 |
| Total debtors | | 57,345 | 52,935 |
| Cash at bank | | 4 | 72 |
| Total current assets | | 57,349 | 53,007 |
| Creditors – amounts falling due within one year | | | |
| Dividend | | 17,970 | 14,914 |
| Advance corporation tax | | 1,571 | 2,474 |
| Sundry creditors | | 71 | 72 |
| Total creditors | | 19,612 | 17,460 |
| Net current assets | | 37,737 | 35,547 |
| Total capital employed | | 310,404 | 274,247 |

Equity Shareholders' Funds

| | | | |
|---|----|----------------|----------------|
| Capital and reserves | | | |
| Called up share capital | 17 | 18,717 | 18,643 |
| Share premium account | 19 | 6,744 | 4,690 |
| Revaluation reserve | 19 | 258,956 | 224,989 |
| Capital redemption reserve | 19 | 1,241 | 1,241 |
| Profit and loss account | 19 | 24,746 | 24,684 |
| Total equity shareholders' funds | | 310,404 | 274,247 |

Approved by the Board of Directors and signed on its behalf by:-

M G A McLintock

D K Watson

26th November 1997

The notes on pages 22 to 38 form an integral part of these accounts.

Notes to the Accounts

30th September 1997

Accounting Policies

These accounts have been prepared in accordance with the historical cost convention, as modified by the revaluation of the Group's investments, and in accordance with applicable accounting standards. The principal accounting policies which the Directors have adopted within that convention are set out below. The Group has adopted FRS1 cash flow statements (revised) and has adjusted the comparatives in the cash flow statement to reflect the provisions of the new standard.

- (a) **Basis of consolidation:** The consolidated accounts incorporate the accounts of the Company and its subsidiary undertakings, all of which make up their accounts at the same date.
- (b) **Assurance activities:** These have been accounted for using the 'modified statutory solvency' basis of accounting. The results from this have been consolidated by analysing them on the same basis as those of the rest of the business as the essence of these activities is similar to the unit and investment trust business.
- The 'net assurance assets held to match unit-linked liabilities' are the net assets of the assurance long-term life fund that are held to meet the liabilities to policyholders invested in unit-linked assurance products. Other assurance assets and liabilities have been consolidated on a line by line basis within the balance sheet.
- (c) **Deferred tax:** Full provision is made at the current rate where, in the opinion of the Directors, it is probable that a liability to corporation tax may arise in the future from the allocation of items to different periods for tax and for accounting purposes. Deferred tax is also provided on the surplus of the balance sheet values over the tax base cost of investments where it is probable that a liability to corporation tax will arise in the foreseeable future.
- (d) **Depreciation of tangible fixed assets:** Tangible fixed assets are capitalised and stated at cost less depreciation which is calculated to write down the cost of the assets to residual value over their expected useful lives as follows:-

| | |
|------------------------|--------------------------|
| Freehold buildings | 50 years straight-line |
| Computer equipment | 3-5 years straight-line |
| Equipment and fittings | 3-10 years straight-line |
| Motor vehicles | 25% reducing balance |

Freehold land is not depreciated.

(e) **Investments:**

Fixed assets: Listed investments are stated at the middle-market values prevailing at the balance sheet date. Unlisted investments are included at Directors' valuation. Leasehold property is stated at professional valuation. The overall surplus of balance sheet values over original cost is credited to the revaluation reserve. Realised gains and losses on disposals of investments, calculated by reference to original cost less attributable tax, are transferred from the revaluation reserve to the profit and loss account as a movement on reserves.

Current assets: Listed investments are included at the lower of cost and middle-market values ruling at the balance sheet date.

- (f) **Investment income:** Dividends on equities and distributions on unit trusts are included when the investments are quoted ex-dividend. Income on fixed interest investments is accrued on a daily basis after making appropriate adjustments for purchases and sales.
- (g) **Stock of units:** Stock of units is valued at the lower of cost and market value.
- (h) **Investments in subsidiary undertakings:** The investments in subsidiary undertakings are stated at an amount equal to the book value of the underlying net assets of the subsidiary undertakings at the balance sheet date. The unrealised surplus arising is credited to the revaluation reserve in the accounts of the Company. No provision is made for deferred tax in respect of the unrealised surplus.
- (i) **Pension contributions:** Contributions to the pension scheme are charged to the profit and loss account so as to spread the cost of pensions over the employees' service lives. The Actuary of the pension scheme undertakes a valuation of the scheme every three years, as a result of which he recommends the level of contributions that should be paid to the scheme so as to secure the benefits set out in the scheme rules.
- (j) **Deferral of acquisition costs:** Acquisition costs which are directly attributable to no-load unit and investment trust products and assurance products are deferred and charged against future profits. The rate of amortisation of the deferred acquisition cost asset is consistent with a prudent assessment of the expected pattern of receipt of the future revenue margins over the period the relevant contracts are expected to remain in force.
- (k) **Operating leases:** Operating lease costs are charged to the profit and loss account on a straight-line basis over the term of the lease.

Notes to the Accounts
30th September 1997

| | | 1997 | | 1996 | |
|---|---|----------------|---------|----------------|---------|
| | | £'000 | £'000 | £'000 | £'000 |
| 1 | Revenue | | | | |
| | Annual management fees from: | | | | |
| | Unit and investment trusts | 82,466 | | 74,101 | |
| | Institutional clients | 9,733 | | 8,657 | |
| | Assurance funds: | | | | |
| | Renewal and annual unit-linked charges | 46,239 | | 46,077 | |
| | Non-linked business charges | 4,006 | | 3,714 | |
| | | | 142,444 | | 132,549 |
| | Initial charges arising on sales of: | | | | |
| | Unit and investment trusts | 6,037 | | 9,731 | |
| | Assurance funds | 3,750 | | 4,324 | |
| | | | 9,787 | | 14,055 |
| | Total revenue | 152,231 | | 146,604 | |

Revenue arises principally from the management of unit and investment trusts, assurance funds and client portfolios. Annual management fees are charged to the unit and investment trusts and assurance funds.

| | | 1997 | 1996 |
|---|---|----------------|----------------|
| | | £'000 | £'000 |
| 2 | Segmental information | | |
| | Analysis by class of business is as follows: | | |
| | Revenue | | |
| | Unit and investment trusts | 88,503 | 83,832 |
| | Institutional clients | 9,733 | 8,657 |
| | Assurance funds | 53,995 | 54,115 |
| | Total | 152,231 | 146,604 |
| | All revenue arises from activities within the United Kingdom. | | |
| | Pre-tax operating profit | | |
| | Unit and investment trusts | 25,892 | 28,433 |
| | Institutional clients | 6,824 | 5,461 |
| | Assurance funds | 19,223 | 16,841 |
| | Total | 51,939 | 50,735 |
| | Net assets | | |
| | Unit and investment trusts | 154,413 | 145,555 |
| | Institutional clients | 26,009 | 18,979 |
| | Assurance funds | 129,982 | 109,713 |
| | Total | 310,404 | 274,247 |

Net assets represent the assets held to meet the capital and solvency requirements of each business.

Funds under management by activity are shown on page 9.

Notes to the Accounts
30th September 1997

| | | 1997 £'000 | 1996 £'000 |
|---|---|---------------|---------------|
| 3 | Profit before tax is stated after charging these expenses against operating profit | | |
| | Depreciation of fixed assets | 3,922 | 4,680 |
| | Fees paid to KPMG Audit Plc and its associates | | |
| | Audit | 168 | 150 |
| | Review of restatement | – | 20 |
| | Regulatory | 19 | 18 |
| | Other | 239 | 74 |
| | Non audit | 258 | 112 |
| | Amounts payable under operating leases | | |
| | Plant and machinery | 30 | 76 |
| | Other | 1,673 | 1,832 |
| | Marketing and commissions expenditure | | |
| | Marketing and commission costs incurred | 27,970 | 33,741 |
| | Marketing and sales overheads | 9,870 | 9,349 |
| | Less: deferred acquisition costs | (14,841) | (23,621) |
| | | 22,999 | 19,469 |
| | Amortisation of acquisition costs | 18,060 | 14,318 |
| | Renewal commission | 5,217 | 4,468 |
| | | 46,276 | 38,255 |
| The required disclosures in relation to staff costs and Directors are given within notes 5 and 6 on pages 25 to 30. | | | |
| 4 | Exceptional items | | |
| | Administrative expenditure of the Group includes the following exceptional items | | |
| | Expenditure relating to the review and reorganisation of the Group's administrative processes | – | 7,632 |

Notes to the Accounts
30th September 1997

| | | 1997 £'000 | 1996 £'000 |
|-------------|--|---------------|---------------|
| 5 Employees | Staff costs, including Directors' emoluments, consist of: | | |
| | Salaries and executive bonus scheme | 25,662 | 22,074 |
| | Social Security costs | 2,437 | 2,106 |
| | Pension costs | 2,504 | 2,174 |
| | Redundancy costs | 358 | 956 |
| | Total staff costs | 30,961 | 27,310 |

The average number of staff, including Directors, employed by the Group during the year was 845 (1996 – 789).

As regards remuneration, all employees of the Group

(a) receive a salary which is based on their relevant experience, responsibility and market value based on external consultant surveys and discussions with competitors operating within the same industry or geographical area;

(b) can participate in the M&G Pension Scheme, if they work at least 12 hours per week. This provides for a pension of two-thirds of basic annual salary upon retiring from active service at Normal Retirement Age after a minimum of 30 years of service. The pension is reduced if pensionable service is less than 30 years or if early retirement is permitted. The Normal Retirement Age is 65, but select members (being members of the Executive Committee of M&G Group P.L.C. or Directors of M&G Investment Management Ltd) may retire at 60 without loss of benefit. Contributions (currently – employer 13%; employee 3%) are based upon recommendations from the Group's Actuaries, Aon Consulting. All members of the pension scheme benefit from cover in respect of retirements due to ill-health and their next of kin receive four times their final salary should they die whilst employed by the Company.

For certain employees who joined the scheme after 1st June 1989 and who are subject to the earnings limit in calculating benefits under the scheme, the Group operates an arrangement to provide them with the pension benefits they would have otherwise obtained and the accounts include a full provision for these amounts;

(c) are invited to participate in the M&G Group Profit Sharing Scheme and the M&G 1992 Savings-Related Share Option Scheme (SAYE) if they work at least 12 hours per week and after they have been employed by the Company for three years and one year respectively. These schemes are designed to encourage employees to participate in the progress of the Group by becoming shareholders.

Under the M&G Group Profit Sharing Scheme, shares are appropriated to each eligible employee to a total value equal to 10% of basic salary for the tax year, or the preceding tax year, whichever is greater, subject to an upper limit equal to the lower of i) £8,000 and ii) such amount as may be determined by the Directors. These amounts are reduced proportionately if the total value of shares appropriated in any year would otherwise exceed 5% of the Group's UK-generated pre-tax profits.

The basis of the 1992 SAYE Scheme is that members make monthly contributions under an approved SAYE contract for five years. On maturity, members may request the return of their contributions and will receive a bonus equal to that number of monthly contributions stated in the Sharesave prospectus relating to the particular SAYE contract. They can then decide whether or not they wish to acquire shares in M&G Group P.L.C. with all or part of the money up to the maximum number of shares and at the price stipulated at the start of the contract ("the exercise price"). The exercise price can be set at a discount of up to 20% of the market price prevailing when the scheme is operated each year;

(d) can obtain private health care cover paid for by the Company;

(e) are employed under service contracts terminable at one month's notice by the employee or employer. Notice by the employer will be greater where statutory employment provisions apply.

Notes to the Accounts

30th September 1997

5 Employees (continued)

In addition

- (f) Certain **Directors and senior executives** in the Group receive the above benefits as well as
- (i) being entitled to join the Profit Sharing and SAYE schemes without having served the three year and one year qualification period, respectively;
 - (ii) a company car. Two car schemes are operated by the Group, one of which includes reimbursement of all fuel costs and the other of which reimburses the fuel costs for business mileage only;
 - (iii) bonuses determined according to individual and Group performance and with reference to bonus levels in relevant comparator companies;
 - (iv) annual grants of executive share options made to encourage them to identify their interests with those of the shareholders. These options are awarded for performance and progression through the management structure subject to a holding limit not exceeding the greater of four times annual remuneration and £100,000;
 - (v) being employed under service contracts terminable at three months' notice by the employee or employer (other than Directors who are normally employed under rolling one-year contracts of service).
- (g) For certain **sales and marketing staff** the Group operates bonus schemes to reward performance against specific targets.

6 Report of the Remuneration Committee

The remuneration committee have elected to present their report within the main body of the accounts since they believe that it is appropriate that the remuneration of the Directors of the Company be considered in the context of the results of the Group and the remuneration arrangements for the Company's employees.

The Remuneration Committee ("the Committee") is responsible for determining the remuneration policy for executive Directors and senior executives. The members of the Committee are the non-executive Directors chaired by R D Kent. The Chief Executive is normally invited to attend meetings except where his own remuneration is considered. The Committee has access to external advisers and also takes advice from the Group's Human Resources department.

This report sets out the Company's remuneration policy as determined by the Committee and disclosures on Directors' and senior executives' remuneration. In framing the remuneration policy full account has been taken of Section B of the best practice provisions annexed to the listing rules of the London Stock Exchange.

1. Executive Remuneration Policy

The Group believes that continuing success is critically dependent upon the recruitment and retention of high quality staff for all its business operations. In determining the remuneration policy for the executive Directors and senior executives, the Committee has taken advice from independent consultants and has considered the need to offer competitive basic salaries together with a significant element of performance-related benefits designed to reward both individual and business performance and to ensure that executives' interests are aligned with those of shareholders.

In determining the remuneration of individual executive Directors and senior executives, the Committee obtained survey data and advice from independent consultants on the composition and level of remuneration for equivalent roles in relevant comparator investment management companies. Additionally, the Committee took account of remuneration levels throughout the Group.

Notes to the Accounts

30th September 1997

6 Report of the Remuneration Committee (continued)

2. Base Salary and Benefits

The Committee sets the base salary of each executive Director after taking account of individual performance and comparison with external data.

The principal benefits provided for each Director are a fully expensed car, health insurance, membership of the M&G Group Pension Scheme and participation in the M&G Group Profit Sharing Scheme.

3. Annual Performance Related Bonus

The executive Directors and certain senior executives are eligible for an annual performance related bonus payment related to the results of the Group and their individual performance and contribution.

4. Share Option Schemes

(a) Executive Share Option Schemes

The Group operates both Revenue approved and unapproved executive share option schemes. The total cumulative value of options unexercised at any point in time is subject to an upper limit of four times annual remuneration. Options are normally granted in tranches so that, typically, employees will not reach their maximum entitlement until after a period of three to four years. Options issued under these schemes may be exercised between three and ten years after the date of grant, subject to meeting specified performance criteria.

(b) Savings-Related Option Schemes

The executive Directors, as well as all eligible employees, are entitled to participate in the M&G 1992 Savings-Related Share Option Scheme.

5. Directors' Contracts

The executive Directors are employed under rolling one-year contracts of service, with the exception of V P Bazalgette who joined the Group on a two-year contract reducing to a rolling one-year contract after his first year of employment.

With regard to early termination of Directors' service contracts the Company has regard to the circumstances of each case, the fact that Directors are under a duty to mitigate their loss and the fact that continuing Directors are normally entitled to no more than 12 months' notice.

The non-executive Directors each receive fees, but do not have contracts of service nor do they participate in the bonus and share option scheme arrangements and their service is not pensionable. Non-executive Directors appointed since 1st January 1992 have been engaged for specific terms, usually of four years, which may be renewed for a further three years. Non-executive Directors appointed before 1st January 1992 do not have a specified term of office.

6. Directors' Emoluments

Total emoluments of the Directors, including compensation for loss of office, were as follows:

| | 1997 £'000 | 1996 £'000 |
|---|---------------|---------------|
| Emoluments of executive Directors | 1,454 | 1,408 |
| Bonus payments | 375 | 871 |
| Compensation payments for loss of emoluments on joining the Group | 93 | — |
| Compensation for loss of office | — | 466 |
| Relocation payment | 31 | — |
| Gains made on the exercise of share options | 558 | 703 |
| Sub-total | 2,511 | 3,448 |
| Fees of non-executive Directors | 186 | 166 |
| Total emoluments, gains and compensation for loss of office | 2,697 | 3,614 |

Retirement benefits are accruing to six (1996 – six) Directors under a defined benefit scheme.

Notes to the Accounts

30th September 1997

6 Report of the
Remuneration Committee
(continued)

Emoluments of the individual Directors for their services as Directors were as follows:

| | Salary and Fees £'000 | Bonus £'000 | Other Benefits £'000 | Total 1997 £'000 | Total 1996 £'000 | Long-term share option incentives ^f 1997 £'000 | 1996 £'000 |
|-------------------------------------|-----------------------------|----------------|----------------------------|------------------------|------------------------|---|---------------|
| Current Directors | | | | | | | |
| V P Bazalgette ^Q | 182 | 150 | 114 | 446 | - | - | - |
| H R Collum | 29 | - | - | 29 | 24 | - | - |
| A G Down | 25 | - | - | 25 | 21 | - | - |
| P A Emms | 180 | 30 | 19 | 229 | 314 | - | - |
| J S Fairbairn | 21 | - | - | 21 | 18 | - | - |
| R S Hughes | 194 | - | 21 | 215 | 364 | 11 | - |
| R D Kent | 25 | - | - | 25 | 15 | - | - |
| M Lewis [†] | 179 | 65 | 47 | 291 | - | - | - |
| M G A McIntock [#] | 246 | 100 | 17 | 363 | 360 | - | - |
| E C S Macpherson | 21 | - | - | 21 | 2 | - | - |
| D L Morgan (Chairman) ^{*^} | 145 | - | 13 | 158 | 528 | 429 | - |
| D K Watson | 154 | 30 | 17 | 201 | 210 | - | - |
| Former Directors | | | | | | | |
| R A Brooks | - | - | - | - | 7 | - | - |
| H J Haden | 79 | - | 14 | 93 | 247 | 118 | - |
| Sir David Money-Coutts | 22 | - | - | 22 | 60 | - | - |
| A J Oddie | - | - | - | - | 400 | - | 91 |
| A P Shearer | - | - | - | - | 322 | - | 612 |
| E B O Sherlock | - | - | - | - | 19 | - | - |
| | 1,502 | 375 | 262 | 2,139 | 2,911 | 558 | 703 |

^f Notional gains made on Executive and Savings-Related share options exercised during the year. These represent the difference between the price of options exercised and the value of the shares on the dates the options were exercised.

* Highest paid Director.

^Q The emoluments shown for V P Bazalgette are from the commencement of his employment on 17th October 1996 to the year end. He was appointed to the Board on 27th November 1996. Included within other benefits is a payment of £92,784 made to V P Bazalgette in respect of benefits foregone on leaving his former employer.

[†] The emoluments shown for M Lewis are for the full year. He was appointed to the Board on 26th February 1997. Included within other benefits is £30,667 paid to M Lewis as part of an agreed relocation package.

[#] M G A McIntock's annual salary increased from £225,000 to £250,000 with effect from 1st February 1997, the date of his appointment as Chief Executive.

[^] D L Morgan's emoluments comprised an annual salary of £290,000 whilst Chief Executive and non-executive Director's fees of £65,000 annually with effect from 1st February 1997, the date of his appointment as Chairman of the Group.

During the year, the Group made interest-free loans in respect of rail season tickets to H J Haden, R S Hughes, M G A McIntock and D K Watson. The maximum amount outstanding during the year was £4,729 (1996 - £7,260). The balance at 30th September 1997 was £489 (1996 - £342).

Notes to the Accounts
30th September 1997

6 Report of the
Remuneration Committee
(continued)

| | Age at 30-9-97 | Years of pensionable service to 30-9-97 | Director's contributions in the year £'000 | Increase in accrued pension in 1997 (over and above inflation) £'000 pa | Accrued pension entitlement 1997 £'000 | 1996 £'000 |
|------------------------------------|-------------------|--|---|--|--|---------------|
| Current Executive Directors | | | | | | |
| V P Bazalgette | 46 | 1 | 6 | 4 | 4 | — |
| P A Emms | 48 | 5 | 5 | 4 | 19 | 15 |
| R S Hughes | 40 | 11 | 6 | 3 | 45 | 41 |
| M Lewis | 41 | 1 | 5 | 4 | 4 | — |
| M G A McLintock | 36 | 5 | 8 | 11 | 28 | 17 |
| D K Watson | 38 | 3 | 5 | 4 | 10 | 6 |
| Former Executive Directors | | | | | | |
| H J Haden | 56 | 25 | 2 | 1 | 83 | 81 |
| D L Morgan | 63 | 25 | 3 | 9 | 158 | 148 |

Notes: The accrued pension entitlement is the pension that would be paid at Normal Retirement Age (60) based on accrued service, as at 30th September.

The cost to the Group for the Directors' pensions amounted to £252,401 (1996 – £252,118).

The Group operates an arrangement to provide certain employees with the benefits to which they would have been entitled had the restrictions to the earnings limit imposed by the Finance Act 1989 not been introduced. Where this applies to a Director, the accrued entitlement stated above is inclusive of this extra amount.

Directors' Interests

The Directors' holdings and those of their families in the ordinary shares and share options of the Company according to the Register of Directors' holdings maintained by the Company are as follows:

| | 1997 | | | 1996 | | |
|------------------|-------------------------|---|-------------------------------|-------------------------|---|-------------------------------|
| | Fully paid shares | Savings- related share options | Executive share options | Fully paid shares | Savings- related share options | Executive share options |
| V P Bazalgette | 534 | 1,555 | 22,813 | — | — | — |
| H R Collum | 2,000 | — | — | 2,000 | — | — |
| A G Down | — | — | — | 1,800 | — | — |
| P A Emms | 2,759 | 3,122 | 67,983 | 2,212 | 3,122 | 54,676 |
| J S Fairbairn | 438,437 | — | — | 438,408 | — | — |
| R S Hughes | 28,860 | 1,511 | 52,892 | 29,434 | 2,333 | 38,444 |
| R D Kent | 2,600 | — | — | 2,600 | — | — |
| M Lewis | 546 | 622 | 19,961 | — | — | 19,961 |
| M G A McLintock | 4,260 | 3,122 | 64,987 | 3,212 | 3,122 | 47,877 |
| E C S Macpherson | 3,300 | — | — | 3,300 | — | — |
| D L Morgan | 6,247 | — | — | 29,840 | 2,660 | 107,194 |
| D K Watson | 1,644 | 1,578 | 38,375 | 1,098 | 1,578 | 26,969 |
| | 491,187 | 11,510 | 267,011 | 513,904 | 12,815 | 295,121 |

The holdings of the Directors include, where appropriate, ordinary shares acquired on behalf of each of them in accordance with the provisions of the M&G Group Profit Sharing Scheme. The holdings shown at 30th September 1996 of V P Bazalgette and M Lewis are as at the dates of their appointments.

All of the above interests are beneficially held.

In addition, A G Down and J S Fairbairn each have an interest in the shares of the Company as trustees of the Esmée Fairbairn Charitable Trust as shown on page 39. These interests are not beneficially held.

Notes to the Accounts

30th September 1997

6 Report of the Remuneration Committee (continued)

The number of shares subject to options held by the Directors and granted under the M&G Savings-Related and Executive Share Option Schemes are detailed opposite.

| | Number of share options | | | Exercise price (pence) | Market price at exercise (pence) | Date options exercisable | Date options expire |
|--------------------------|-------------------------|-------------------------|----------------------|------------------------|----------------------------------|--------------------------|---------------------|
| | At 1-10-96 | Granted During the year | Exercised At 30-9-97 | | | | |
| V P Bazalgette | | | | | | | |
| Savings-Related | – | 1,555 | 1,555 | 1,109.3 | | 25.03.02 | 24.09.02 |
| Executive | – | 22,813 | 22,813 | 1,315.0 | | 31.01.00 | 29.01.07 |
| P A Emms | | | | | | | |
| Savings-Related | 3,122 | | 3,122 | 580.5 | | 25.02.98 | 24.08.98 |
| Executive | 30,000 | | 30,000 | 778.0 | | 01.06.96 | 31.05.03 |
| | 1,400 | | 1,400 | 995.0 | | 20.12.96 | 19.12.03 |
| | 15,400 | | 15,400 | 940.0 | | 19.12.97 | 18.12.04 |
| | 7,876 | | 7,876 | 1,295.0 | | 19.01.99 | 18.01.06 |
| | | 13,307 | 13,307 | 1,315.0 | | 31.01.00 | 29.01.07 |
| R S Hughes | | | | | | | |
| Savings-Related | 1,444 | 1,444 | – | 519.0 | 1,275.0 | 24.03.97 | 23.09.97 |
| | 889 | | 889 | 1,163.7 | | 25.03.01 | 24.09.01 |
| | | 622 | 622 | 1,109.3 | | 25.03.02 | 24.09.02 |
| Executive | 1,350 | | 1,350 | 995.0 | | 17.12.96 | 16.12.03 |
| | 22,500 | | 22,500 | 940.0 | | 19.12.97 | 18.12.04 |
| | 14,594 | | 14,594 | 1,295.0 | | 19.01.99 | 18.01.06 |
| | | 14,448 | 14,448 | 1,315.0 | | 31.01.00 | 29.01.07 |
| M Lewis | | | | | | | |
| Savings-Related | – | 622 | 622 | 1,109.3 | | 25.03.02 | 24.09.02 |
| Executive | – | 19,961 | 19,961 | 1,315.0 | | 31.01.00 | 29.01.07 |
| M G A McLintock | | | | | | | |
| Savings-Related | 3,122 | | 3,122 | 580.5 | | 25.02.98 | 24.08.98 |
| Executive | 15,000 | | 15,000 | 778.0 | | 27.05.96 | 26.05.03 |
| | 1,000 | | 1,000 | 995.0 | | 21.12.96 | 20.12.03 |
| | 18,750 | | 18,750 | 940.0 | | 16.12.97 | 15.12.04 |
| | 13,127 | | 13,127 | 1,295.0 | | 19.01.99 | 18.01.06 |
| | | 17,110 | 17,110 | 1,315.0 | | 31.01.00 | 29.01.07 |
| D L Morgan | | | | | | | |
| Savings-Related | 1,444 | 1,444 | – | 519.0 | 1,325.0 | 24.03.97 | 23.09.97 |
| | 624 | 624 | – | 580.5 | 1,207.5 | 25.02.98 | 24.08.98 |
| | 592 | 592 | – | 1,163.7 | | 25.03.01 | 24.09.01 |
| Executive | 40,000 | 40,000 | – | 778.0 | 1,232.5 | 27.05.96 | 26.05.03 |
| | 1,750 | 1,750 | – | 995.0 | 1,232.5 | 20.12.96 | 19.12.03 |
| | 50,000 | 50,000 | – | 940.0 | 1,372.5 | 03.01.98 | 02.01.05 |
| | 15,444 | 15,444 | – | 1,295.0 | 1,372.5 | 19.01.99 | 18.01.06 |
| D K Watson | | | | | | | |
| Savings-Related | 393 | | 393 | 876.6 | | 21.03.00 | 20.09.00 |
| | 1,185 | | 1,185 | 1,163.7 | | 25.03.01 | 24.09.01 |
| Executive | 15,000 | | 15,000 | 940.0 | | 19.12.97 | 18.12.04 |
| | 11,969 | | 11,969 | 1,295.0 | | 19.01.99 | 18.01.06 |
| | | 11,406 | 11,406 | 1,315.0 | | 31.01.00 | 29.01.07 |
| Total | 287,975 | 101,844 | 111,298 | 278,521 | | | |
| By exercise price | | | | | | | |
| 519.0p | 2,888 | | 2,888 | – | | | |
| 581.0p | 6,868 | | 624 | 6,244 | | | |
| 778.0p | 85,000 | | 40,000 | 45,000 | | | |
| 876.6p | 393 | | | 393 | | | |
| 940.0p | 121,650 | | 50,000 | 71,650 | | | |
| 995.0p | 5,500 | | 1,750 | 3,750 | | | |
| 1,163.7p | 2,666 | | 592 | 2,074 | | | |
| 1,295.0p | 63,010 | | 15,444 | 47,566 | | | |
| 1,109.3p | | 2,799 | | 2,799 | | | |
| 1,315.0p | | 99,045 | | 99,045 | | | |
| Total | 287,975 | 101,844 | 111,298 | 278,521 | | | |

The market price of the shares at 30th September 1997 was 1,215p (1996 – 1,085p) and ranged from 1,042.5p to 1,457.5p during the year. No share options held by the current executive Directors of the Company lapsed during the year. Under the rules of the Executive Share Option Schemes the options held by former executive Directors H J Haden and D L Morgan were exercised within specified periods after their retirement. Certain of the options granted to H J Haden and D L Morgan under the Savings-Related Share Option Schemes lapsed in accordance with the scheme rules.

There have been no changes to the holdings or options of the Directors between 30th September 1997 and 17th November 1997. Further information relating to the Savings-Related and Executive Share Option Schemes is set out in notes 5 and 17.

Notes to the Accounts
30th September 1997

| | | 1997 £'000 | 1996 £'000 |
|--|--|---------------|---------------|
| 7 Interest receivable and investment income | Listed investments | 5,353 | 2,187 |
| | Unlisted investments (unit trust distributions) | 6,135 | 8,588 |
| | Deposits | 3,805 | 2,900 |
| | Rental income | 126 | 87 |
| | | 15,419 | 13,762 |
| <hr/> | | | |
| 8 Tax | Tax is based on the profits for the year and comprises: | | |
| | Corporation tax at 32% on taxable profit (1996: 33%) | 21,033 | 25,038 |
| | Transfer to deferred tax (note 16) | (1,635) | (6,665) |
| | | 19,398 | 18,373 |
| | Tax credit on UK franked investment income | 1,699 | 1,919 |
| | | 21,097 | 20,292 |
| | Overseas tax | 47 | 69 |
| | | 21,144 | 20,361 |
| <hr/> | | | |
| 9 Profit after tax attributable to shareholders of M&G Group P.L.C. | Profit after tax attributable to shareholders dealt with in the accounts of the holding Company | 30,000 | 27,000 |
| | The Company has taken advantage of the exemption under Section 230 of the Companies Act 1985 from presenting its own profit and loss account. | | |
| <hr/> | | | |
| 10 Dividends and earnings per ordinary share of 25p | Interim dividend 16p (1996 – 16p) | 11,968 | 11,964 |
| | Final dividend 24p (1996 – 20p) | 17,970 | 14,914 |
| | Total dividends 40p (1996 – 36p) | 29,938 | 26,878 |
| | The earnings per share have been calculated on the basis of the weighted average number of shares in issue during the year of 74,699,860 (1996 – 74,603,356) on profits after tax of £46,214,000 (1996 – £44,136,000). In 1996 the earnings per share, before exceptional items, of 66.2p have been calculated on the basis of profits after tax, before exceptional items, of £49,359,000. Diluted earnings per share are not materially different. | | |

Notes to the Accounts

30th September 1997

| | Freehold land and buildings £'000 | Computer equipment £'000 | Equipment and fittings £'000 | Motor vehicles £'000 | Total £'000 |
|--|---|--------------------------------|------------------------------------|----------------------------|----------------|
| 11 Tangible fixed assets | | | | | |
| Cost at 1st October 1996 | 20,196 | 18,087 | 12,903 | 3,083 | 54,269 |
| Additions | – | 1,962 | 1,360 | 944 | 4,266 |
| Disposals | – | (153) | (93) | (800) | (1,046) |
| Cost at 30th September 1997 | 20,196 | 19,896 | 14,170 | 3,227 | 57,489 |
| Depreciation at 1st October 1996 | 1,209 | 13,290 | 8,394 | 1,128 | 24,021 |
| Depreciation | 303 | 2,237 | 851 | 531 | 3,922 |
| Depreciation on disposals | – | (149) | (92) | (413) | (654) |
| Depreciation at 30th September 1997 | 1,512 | 15,378 | 9,153 | 1,246 | 27,289 |
| Balance sheet value at 30th September 1997 | 18,684 | 4,518 | 5,017 | 1,981 | 30,200 |
| Balance sheet value at 30th September 1996 | 18,987 | 4,797 | 4,509 | 1,955 | 30,248 |

Included within freehold land and buildings is land of £5,049,000 which has not been depreciated.

1997
£'000**12 Investments****Fixed asset investments****Group**

| | |
|--|----------|
| Valuation at 1st October 1996 | 260,782 |
| Additions | 35,563 |
| Disposals at cost | (24,775) |
| Change in value of Group investments | 15,561 |
| Change in value of investments held to match non-unit-linked liabilities | 3,611 |
| Valuation at 30th September 1997 | 290,742 |

1997
£'0001996
£'000**The investments consist of the following:**

| | | | |
|----------------|---|---------|---------|
| Listed: | (All listed on the London Stock Exchange) at middle-market value | | |
| | Government securities | 59,632 | 46,200 |
| | Investment trusts | 31,310 | 29,171 |
| | Other debt securities | 15,208 | 14,297 |
| Unlisted: | at Directors' valuation | | |
| | Authorised unit trusts | 177,970 | 163,320 |
| | Other unit trusts and assurance funds | 6,247 | 7,332 |
| | Leasehold property with more than 20 years to run, at professional valuation | 375 | 375 |
| | Interests in associated undertaking | – | 87 |
| | | 290,742 | 260,782 |
| | Profit realised on sale of investments during the year | 8,780 | 9,135 |
| | Historical cost of investments | 182,041 | 171,251 |
| Company | | | |
| | Group companies' shares at cost | 10 | 10 |
| | Unrealised surplus arising on restatement of underlying net assets of the subsidiary undertakings | 272,657 | 238,690 |
| | | 272,667 | 238,700 |

Current asset investments**Group**

| | | |
|------------------------|--------|--------|
| Listed debt securities | 36,629 | 18,950 |
|------------------------|--------|--------|

Notes to the Accounts
30th September 1997

| | | 1997 £'000 | 1996 £'000 |
|--|--|------------------|------------------|
| 13 Net assurance assets held to match unit-linked liabilities | Net assurance assets held to match unit-linked liabilities comprise: | | |
| | Property | – | 2,506 |
| | Equities | 1,291,617 | 1,167,966 |
| | Unit trusts | 1,597,411 | 1,393,297 |
| | Debt securities | 306,606 | 102,222 |
| | Deposits and loans | 193,113 | 122,053 |
| | Amounts receivable | 25,224 | 24,290 |
| | Creditors and accruals | (96,988) | (68,388) |
| | | 3,316,983 | 2,743,946 |
| 14 Debtors | Due after more than one year | | |
| | Deferred acquisition costs | 24,609 | 27,036 |
| | Due within one year | | |
| | Deferred acquisition costs | 13,619 | 14,411 |
| | Debtors for sales | 6,725 | 4,076 |
| | Debtors for assurance operations | 3,757 | 3,079 |
| | Unit trust trustees for units cancelled | 7,208 | 9,229 |
| | Securities realised awaiting settlement | 2,145 | 4,684 |
| | Accrued fees from institutional clients | 4,821 | 3,975 |
| | Other debtors | 6,855 | 4,954 |
| | Prepayments and accrued income | 5,186 | 4,081 |
| | | 50,316 | 48,489 |
| | Deferred acquisition costs | | |
| | Deferred acquisition costs brought forward | 41,447 | 32,144 |
| | Acquisition costs incurred | 14,841 | 23,621 |
| | Acquisition costs charged against profit for the year | (18,060) | (14,318) |
| | Deferred acquisition costs carried forward | 38,228 | 41,447 |

Notes to the Accounts
30th September 1997

| | | 1997 £'000 | 1996 £'000 |
|------------------------|---|----------------|----------------|
| 15 Creditors | Amounts falling due within one year | | |
| | Creditors for unit redemptions | 21,231 | 21,825 |
| | Assurance claims outstanding | 19,909 | 18,548 |
| | Creditors for units created | 2,286 | 21,921 |
| | Creditors for assurance operations | 227 | 1,293 |
| | Securities realised awaiting settlement | 556 | 2,101 |
| | Other creditors | 8,192 | 8,841 |
| | Accruals | 17,836 | 17,506 |
| | Taxes and social security | - | 352 |
| | Corporation tax | 17,016 | 13,726 |
| | Dividend | 17,970 | 14,914 |
| | | 105,223 | 121,027 |
| | Amounts falling due after more than one year | | |
| | Assurance non-unit-linked policyholder liabilities | 47,962 | 43,583 |
| | Accruals | 1,483 | 1,131 |
| | Corporation tax, payable 31st December 1998 | 24 | 35 |
| | | 49,469 | 44,749 |
| 16 Deferred tax | Balance brought forward | 22,635 | 17,725 |
| | Transfer to profit and loss account (note 8) | (1,635) | (6,665) |
| | Transfer from revaluation reserve (note 18) | 5,933 | 11,575 |
| | Balance carried forward | 26,933 | 22,635 |
| | The amounts of deferred tax provided in the accounts are: | | |
| | Unrealised surplus on revaluation of investments | 21,107 | 18,067 |
| | Depreciation in excess of capital allowances | (97) | (198) |
| | Deferred acquisition costs | 3,467 | 4,988 |
| | Postponed expense relief | (8,526) | (7,655) |
| | Assurance contingency reserve | 10,124 | 8,078 |
| | Other timing differences | 858 | (645) |
| | | 26,933 | 22,635 |

Notes to the Accounts
30th September 1997

| | | 1997 £'000 | 1996 £'000 |
|------------------|--|---------------|---------------|
| 17 Share capital | Authorised | | |
| | 96,000,000 ordinary shares of 25p each | 24,000 | 24,000 |
| | Allotted | | |
| | 74,867,741 (1996 – 74,571,733) ordinary shares of 25p each, fully paid | 18,717 | 18,643 |

During the year ended 30th September 1997, 296,008 ordinary shares of 25p each were issued fully paid with a total nominal value of £74,002 and for a total consideration of £2,127,658, following the exercise of options granted under the Company's Share Option Schemes.

In accordance with the provisions of the M&G 1992 Savings-Related Share Option Scheme, options in respect of 158,969 Ordinary Shares of the Company were granted during the year to 396 employees of the Group.

In accordance with the terms of the M&G Executive Share Option Scheme, options were granted during the year to six Directors and 65 employees in respect of a total of 360,632 Ordinary Shares of the Company.

At 30th September 1997 the following share options were held by six Directors and 465 employees of the Group, exercisable as follows:

Dates between which the options are exercisable:

| | Number of ordinary shares | Price per share |
|---|------------------------------|--------------------|
| Between 25th February 1998 and 24th August 1998 | 91,945 | 580.5p |
| Between 23rd March 1999 and 22nd September 1999 | 59,092 | 1,062.0p |
| Between 21st March 2000 and 20th September 2000 | 58,073 | 876.6p |
| Between 25th March 2001 and 24th September 2001 | 68,333 | 1,163.7p |
| Between 3rd December 1994 and 2nd December 2001 | 20,000 | 549.0p |
| Between 25th March 2002 and 24th September 2002 | 150,826 | 1,109.3p |
| Between 27th May 1996 and 31st May 2003 | 45,000 | 778.0p |
| Between 17th December 1996 and 22nd December 2003 | 24,885 | 995.0p |
| Between 16th December 1997 and 2nd January 2005 | 273,990 | 940.0p |
| Between 19th January 1999 and 25th January 2006 | 281,262 | 1,295.0p |
| Between 31st January 2000 and 29th January 2007 | 348,400 | 1,315.0p |
| Between 4th February 2000 and 2nd February 2007 | 7,385 | 1,354.0p |
| Total | 1,429,191 | |

If the above had been exercised at 30th September 1997 they would have represented 1.87% of the then enlarged issued share capital.

Notes to the Accounts

30th September 1997

| | | Share premium account £'000 | Revaluation reserve £'000 | Capital redemption reserve £'000 | Profit and loss account £'000 | Total £'000 |
|---------------------------------------|--|--------------------------------------|---------------------------------|---|--|----------------|
| 18 Movements in Group reserves | Balances at 1st October 1996 | 4,690 | 61,938 | 1,241 | 187,735 | 255,604 |
| | Movements during the year | | | | | |
| | Share premium on shares issued | 2,054 | - | - | - | 2,054 |
| | Changes in value of investments | - | 15,561 | - | 8,780 | 24,341 |
| | Tax on changes in value of investments | - | (5,933) | - | (655) | (6,588) |
| | Retained profit | - | - | - | 16,276 | 16,276 |
| | Balances at 30th September 1997 | 6,744 | 71,566 | 1,241 | 212,136 | 291,687 |

Included within profit and loss reserves are £76,933,000 (1996 – £51,555,000) held in the assurance companies' long-term funds. The Insurance Companies Act 1982 imposes restrictions on the distribution of these funds.

| | | Share premium account £'000 | Revaluation reserve £'000 | Capital redemption reserve £'000 | Profit and loss account £'000 | Total £'000 |
|---|--|--------------------------------------|---------------------------------|---|--|----------------|
| 19 Movements in Company reserves | Balances at 1st October 1996 | 4,690 | 224,989 | 1,241 | 24,684 | 255,604 |
| | Movements during the year | | | | | |
| | Share premium on shares issued | 2,054 | - | - | - | 2,054 |
| | Unrealised surplus arising from revaluation of investments | - | 33,967 | - | - | 33,967 |
| | Retained profit | - | - | - | 62 | 62 |
| | Balances at 30th September 1997 | 6,744 | 258,956 | 1,241 | 24,746 | 291,687 |

Restated
1997 1996
£'000 £'000

20 Cash flow **Reconciliation of operating profit to operating cash flows****(a) Operating activities**

| | | |
|---|----------|----------|
| Consolidated operating profit | 51,939 | 50,735 |
| Depreciation charges | 3,922 | 4,680 |
| Profit on sale of tangible fixed assets | (36) | (27) |
| Loss/(profit) on sale of liquid investments | 27 | (62) |
| Unrealised gain on liquid investments | (3,610) | (458) |
| Retained loss of associate | - | 26 |
| Deferred acquisition cost amortisation | 18,060 | 14,318 |
| Decrease/(increase) in stock | 14,207 | (250) |
| Increase in debtors | (16,295) | (33,135) |
| (Decrease)/increase in creditors | (17,419) | 29,238 |
| Net cash inflow from operating activities | 50,795 | 65,065 |

In accordance with FRS1 (revised), cash flows relating to long-term non-linked assurance funds have been included in the consolidated cash flow, resulting in a restatement of 1996 cash flows.

Notes to the Accounts
30th September 1997

| | | 1997 £'000 | Restated 1996 £'000 |
|---------------------------------|---|---------------|---------------------------|
| 20 Cash flow (continued) | (b) Analysis of changes in cash during the year: | | |
| | Balance brought forward | 55,282 | 53,024 |
| | (Decrease)/increase in cash | (3,413) | 2,258 |
| | Balance carried forward | 51,869 | 55,282 |
| | Analysis of changes in financing during the year: | | |
| | Balance brought forward (Share Capital and Share Premium Account) | 23,333 | 21,989 |
| | Cash inflow/(outflow) from financing | 2,128 | (1,252) |
| | Transfer from profit and loss account | – | 2,596 |
| | Balance carried forward (Share Capital and Share Premium Account) | 25,461 | 23,333 |
| | (c) Changes in net assurance assets held to match unit-linked liabilities: | | |
| | Movements during the year | | |
| | Increase in cash | 71,060 | 23,849 |
| | Net increase in unit-linked investments | 501,977 | 174,467 |
| | | 573,037 | 198,316 |
| | Balance brought forward | 2,743,946 | 2,545,630 |
| | Balance carried forward | 3,316,983 | 2,743,946 |

21 Pension commitments

The Group operates a funded pension scheme providing benefits based on final pay for its eligible employees. The assets of the scheme are held separately and managed independently from those of the Group. The Trust Deed forbids investment in the share capital of, or the making of loans to, M&G Group P.L.C. or any of its subsidiary undertakings. As a matter of policy, the trustees of the scheme do not allow the investment manager to stock-lend. The latest completed actuarial valuation of the Group's pension scheme was carried out as at 31st March 1997 by Aon Consulting, as Actuaries to the scheme, using the projected unit method.

The key assumptions (1994 comparatives shown in brackets) were as follows:

| | |
|---|---------------|
| Rate of return on investments | 9.00% (9.50%) |
| Rate of increase in salaries | 7.00% (8.50%) |
| Rate of increase of present and future pensions | 4.50% (5.50%) |
| Rate of dividend growth | 4.75% (4.75%) |

The valuation showed that the market value of the scheme's assets was £62,340,000 and that the actuarial value of those assets represented 132% of the benefits that had accrued to members, after allowing for expected future increases in earnings.

Following the Finance Act 1989, earnings used for calculating benefits under approved pension schemes are restricted to an earnings limit, currently set at £84,000 per annum. This applies to employees who joined approved pension schemes on or after 1st June 1989. The Group has introduced a temporary arrangement for certain employees which will provide them with the pension benefits they would have enjoyed had the earnings limit not been introduced. An amount of £329,000 has been provided for within the accounts to meet this potential liability.

Notes to the Accounts

30th September 1997

- 22 Subsidiary undertakings** The Company owns the whole of the issued capital of the following principal companies, which are incorporated in Great Britain and registered in England and Wales, unless otherwise indicated. The subsidiary undertakings operate in their country of incorporation and are involved in the management of unit and investment trusts, the issue of life and pension policies, and investment management and related activities. All subsidiary undertakings have been included in the consolidation.

The Company's holdings are indirect with the exception of its holding in M&G Limited.

| | |
|-----------------------------------|--|
| M&G Limited | M&G Life Assurance Company Limited |
| M&G Investment Management Limited | M&G Pensions and Annuity Company Limited |
| M&G Securities Limited | M&G (Guernsey) Limited – Guernsey |
| M&G Financial Services Limited | |

| | 1997 £'000 | 1996 £'000 |
|---|---------------|---------------|
| 23 Commitments | | |
| Capital commitments of the Group | | |
| Authorised but not contracted | – | 813 |
| Authorised and contracted | 473 | 92 |

Lease commitments

As at 30th September 1997 the Group had annual commitments under operating leases as set out below (1996 – £2,489,000)

| | Land and buildings £'000 | Other £'000 | Total £'000 |
|--------------------------------|--------------------------------|----------------|----------------|
| Operating leases which expire: | | | |
| Within one year | – | 10 | 10 |
| Between one and five years | 95 | 20 | 115 |
| In over five years | 1,730 | – | 1,730 |
| | 1,825 | 30 | 1,855 |

The parent Company had no capital or lease commitments as at 30th September 1997 and 30th September 1996.

- 24 Related party transactions** The Group received £88,503,000 during the year from the management of unit trusts and investment trusts as disclosed in note 2. Included within this amount is £1,263,000 which had been pre-paid to the Group as at 30th September 1997.
- The Trustees of the Esmée Fairbairn Charitable Trust, the Directors and certain of their close family members hold investments in unit trusts and investment trusts managed by the Group. The notifiable shareholdings are disclosed in the Report of the Remuneration Committee on page 26. The Board confirm, however, that the rights of those Directors or shareholders are not exercised in any way as to require disclosure under Financial Reporting Standard 8.
- Group investments and non-linked assurance fund investments, invested in unit trusts and investment trusts managed by the Group, were £192,501,000.

Report of the Directors

Principal Activity

The principal activity of the Group is investment management. This service is offered primarily in the United Kingdom, through the management of unit and investment trusts, PEPs, unit-linked life and pension policies, and the provision of investment management services to company pension funds, charities and other institutional clients. This Report should be read in conjunction with the Chief Executive's Review and Outlook on pages 6 to 16.

Financial Review

The Group profit before tax was £67,358,000. The tax charge for the year amounted to £21,144,000. The Group profit after tax attributable to shareholders amounted to £46,214,000. Out of these profits, provision has been made for dividends of £29,938,000, leaving unappropriated profits to be retained of £16,276,000.

The Directors recommend the payment of a final dividend of 24p per Ordinary Share which, with the interim dividend paid in July 1997, gives a total for the year of 40p. This is an increase of 11% on the total for the previous year of 36p per share. It is proposed that the final dividend will be paid on 15th January 1998 to shareholders on the register on 12th December 1997.

Share Capital

The total number of shares in issue at 17th November 1997 was 74,877,230 and the Share Premium Account now stands at £6,832,561.

At the Annual General Meeting, held on 29th January 1997, Members renewed the Company's authority under Section 166 of the Companies Act 1985 to make market purchases on the London Stock Exchange of up to 7,500,000 Ordinary Shares of 25p each of the Company, less the number of Ordinary Shares already purchased by the Company pursuant to previous authorities. The Company has not made any further purchases pursuant to this authority and, accordingly, the number of shares in respect of which the Company is now authorised to make market purchases remains at 2,540,000 Ordinary Shares of 25p each (representing approximately 3.4% of the present issued share capital of the Company).

The Directors believe that it is in the best interests of the Company for the authority to be renewed at the forthcoming Annual General Meeting. However, in the interest of administrative simplification it is intended to propose that the basis of the authority be altered so that market purchases of up to 7,500,000 Ordinary Shares may be made without taking account of Ordinary Shares purchased pursuant to previous authorities, thus establishing a fixed limit for the ensuing period of approximately 10% of the issued share capital of the Company instead of a limit which reduces over time.

Accordingly, it is intended to propose, as Special Business, at the forthcoming Annual General Meeting, a Special Resolution to renew the Directors' authority to make market purchases of shares of the Company of up to 7,500,000 Ordinary Shares of 25p each for a period which shall expire at the end of 18 months from the

date of the Meeting or (if earlier) at the next Annual General meeting if a renewal of this authority is proposed.

It is the policy of the Directors to seek to make selective market purchases of Ordinary Shares in circumstances where it will enhance earnings per share for the members of the Company. The Directors have no immediate intention of using this authority.

Substantial Shareholdings

At 17th November 1997, the Directors had been notified under Section 198 of the Companies Act 1985 that the following persons were interested in 3% or more of the Ordinary Shares of the Company:-

| | | | |
|---|---|--|------------------------|
| Sir Antony Acland | } | Trustees of the Esmée Fairbairn Charitable Trust | 25,000,000 (33.39%) |
| A G Down | | | |
| J S Fairbairn | | | |
| C J M Hardie | | | |
| Mrs. P A Hughes-Hallett | | | |
| M Lane Fox | | | |
| Mrs. V Linklater | | | |
| Lord Rees-Mogg | | | |
| A M L Tuckey | | | |
| Commercial Union Assurance Company Plc. | | | 3,800,000 (5.07%) |
| Royal & Sun Alliance Investment Management Limited | | | 2,301,983 (3.07%) |

Directors

The present Directors of the Company are shown on pages 4 and 5.

The interests of the Directors who held office at 30th September 1997 in the share capital of the Company are shown in note 6 on page 29.

V P Bazalgette, P A Emms, R S Hughes, M Lewis, M G A McLintock and D K Watson are employed under rolling one-year contracts of service.

D L Morgan was appointed Chairman at the close of the Annual General Meeting held on 29th January 1997 to succeed Sir David Money-Coutts who retired as a Director of the Company at that time.

M G A McLintock was appointed Chief Executive on 29th January 1997 to succeed D L Morgan.

H J Haden retired as a Director of the Company on 26th March 1997.

M Lewis was appointed an additional Director on 26th February 1997 and, being eligible, offers himself for re-election.

The other Directors who retire by rotation are A G Down, R S Hughes and M G A McLintock who, being eligible, offer themselves for re-election. R S Hughes and M G A McLintock have contracts of service as referred to above. A G Down does not have a contract of service.

There were no contracts of significance, in which any Director is or was materially interested, subsisting during or at the end of the financial year either with the Company or with any of its subsidiary undertakings.

Report of the Directors

Employment Policies

The Group's employment policies are designed to create an environment which encourages employees to be aware of, and involved in, the performance of the Group. The Group also seeks to encourage employees to express their ideas about the Group and its products and procedures.

Staff are kept informed of developments within the Group through various means including *M&G People*, which is published quarterly. All members of staff receive a copy of the Report and Accounts of M&G Group P.L.C. and the Interim Report, together with a summary of the highlights for the period in question.

A Staff Consultative Committee provides a forum where elected members of staff may meet with representatives from management on a regular basis to discuss various issues which affect employees and the Company. This Committee has been set up to meet the Company's statutory obligations to consult with employees on such matters as health and safety as well as seeking to promote communication throughout the Group on topical matters of concern or interest to employees or management. Additionally, it is intended that it will be the vehicle by which member-nominated trustees are appointed.

Applications for employment by disabled persons are always considered fully, bearing in mind the aptitudes and abilities of the applicant concerned. In the event of members of staff becoming disabled, every effort is made to ensure their employment continues. It is the policy of the Group that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of those who do not suffer from a disability.

The Group operates health and safety arrangements for the protection of its staff as required by legislation.

Environmental Policy

The Group recognises that the protection of the environment has become an increasing concern and that an active commitment to environmental issues is an essential part of business today. The Group ensures that, so far as it is consistent with its obligations to its shareholders, its own projects and processes are environmentally friendly, through, for example:

- conservation of energy and other natural resources used in our operations
- use of recyclable materials
- use of waste recycling schemes

Through corporate and personal efforts, contributions are made to charities and community projects, thereby enhancing the environment and community in which we operate.

Policy on Payment of Suppliers

It is the general policy of the Group to pay for the supply of goods and services in accordance with suppliers' terms and conditions, typically within 30 days of the date of an invoice. For certain suppliers special arrangements are established when agreeing the terms of each transaction.

The Group's number of days' billings from suppliers outstanding at 30th September 1997 is 21.

Charitable Contributions

During the year, the Group made payments totalling £91,843 for charitable purposes.

Auditors

KPMG Audit Plc have expressed their willingness to continue in office and a resolution to re-appoint KPMG Audit Plc as the Group's auditors will be proposed at the Annual General Meeting.

Approved by the Board of Directors
S H Henton, Secretary

3 Minster Court, Great Tower Street, London EC3R 7XH

26th November 1997

Report of the Auditors to the Members of M&G Group P.L.C.

We have audited the financial statements on pages 18 to 38.

Respective Responsibilities of Directors and Auditors

As described on page 42 under the heading 'legal, regulatory and other reporting requirements', 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 financial statements and to report our opinion to you.

Basis of Audit 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 Group'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.

Audit Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 30th September 1997 and of the profit of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

[Handwritten signature]
KPMG Audit Plc

Chartered Accountants, Registered Auditor
London, 26th November 1997

Corporate Governance

Primary responsibilities of the Directors

The primary responsibility of the Directors is to direct the management of the Group in such a way as to maximise the long-term return to shareholders. In order to do this they seek to ensure that proper regard is given to the interests of the Group's customers, its staff and the community.

Board of Directors

The Board of Directors, which currently consists of the non-executive Chairman, six executive and five non-executive Directors, meets regularly throughout the year, usually monthly. *It has a Schedule of Matters reserved for its consideration or approval which includes the Group's strategy, major items of capital expenditure and any material contracts.*

The individual Directors have different skills, experience and qualifications. Some have been or are working in other aspects of the financial services industry, others have been or are working in other sectors of the economy. In practice, when a matter comes before the Board it places extra reliance on the views of those who have the most relevant experience of, or skill in, that matter.

Directors may take independent legal, accounting or other professional advice at the expense of the Company in the furtherance of their duties. The Company Secretary's advice and services are also available to all Board members.

The Board encourages executive Directors and senior executives of the Group to become non-executive Directors of other companies or undertake equivalent roles in other bodies. The Group believes it will benefit from executives gaining wider experience and that the companies and other bodies will also benefit. Any fees earned by the Directors for carrying out these duties are paid to the Company.

Board Committees

The Audit and Compliance Committee comprises three non-executive Directors, and meets at least three times a year. Its terms of reference include the review of the adequacy and effectiveness of the Group's internal controls, accounting policies, financial reporting, and arrangements to ensure compliance with the requirements of the Financial Services Act. It also provides a forum through which the Group's external and internal auditors report to the Board.

The Remuneration Committee comprises solely the non-executive Directors under the chairmanship of R D Kent and determines the remuneration for executive Directors. The Committee employs the services of external advisers as it deems necessary.

The Nomination Committee comprises the Group Chairman, one executive and one non-executive Director and is responsible for proposing candidates for appointment to the Board, having regard to the balance and structure of the Board. The Committee employs the services of external advisers as it deems necessary.

Non-executive Directors

Non-executive Directors appointed since 1st January 1992 have been engaged for specific terms, usually of four years, which may be renewed for a further three years. The non-executive Directors each receive fees, but do not have contracts of service nor do they participate in the bonus and share option scheme arrangements and their service is not pensionable. As a general rule, it is envisaged that non-executive Directors will not serve beyond the Annual General Meeting following their 65th birthday.

The Board considers that the non-executive members are of sufficient calibre and number that their views can be expected to carry significant weight in the Board's decision making. The non-executive members of the Board have no financial or contractual interest in the Company other than by way of their fees and shareholdings, as disclosed in note 6 to the accounts. They do not participate in the Group's employee share ownership schemes and their service is not pensionable. The fees for non-executive Directors are determined by the Board as a whole.

Executive Directors

The executive Directors are members of the Executive Committee which is chaired by the Group Chief Executive. It normally meets monthly and acts as a general management committee, being authorised by the Board to carry out any activity with regard to the Group not expressly reserved for the Board.

Executive Directors are employed under rolling one-year contracts of employment. Their emoluments, including participation in the M&G Executive Share Option and the M&G Bonus Schemes, are determined by the Remuneration Committee, which consists solely of the non-executive Directors.

Legal, regulatory and other reporting requirements

In addition to the primary responsibilities and objectives, set out above, *the Board has a specific responsibility for reporting to shareholders and for safeguarding the assets of the Group.* The requirements of the Companies Act, the Stock Exchange and other legal, regulatory and accounting rules require that their report contains a number of statements and assertions in relation to the accounts. *The Directors are required to present for each accounting period financial statements prepared on a going concern basis, unless this is inappropriate, which comply with the provisions of the Companies Act 1985, in respect of the state of affairs of the Company and the Group as at the end of the accounting period and of the profit or loss for that period. In preparing the financial statements suitable accounting policies, framed by reference to reasonable and prudent judgements and estimates, are used and applied consistently. Applicable accounting standards are also followed, subject to any material departures being disclosed and explained in the notes to the accounts. The Directors are responsible for ensuring that arrangements are made for the maintenance of adequate accounting records, which disclose with*

reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements comply with the Companies Act 1985, and 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.

Going Concern

The Directors have examined all of the factors affecting whether the Group is a going concern and consider that the Group has adequate resources to continue in operational existence for the foreseeable future and have therefore continued to adopt the going concern basis in preparing the accounts.

Internal Control

The Board as a whole has collective responsibility for the governance of the Group, including the recommendations of the Cadbury Committee's Code of Best Practice which are noted below:

The Directors are responsible for the Group's system of internal financial control. On behalf of the Board, the Audit and Compliance Committee reviews the effectiveness of these systems. This is achieved primarily through a review of the internal audit programme and its findings, reviews of the half-year and annual financial statements and a review of the nature and scope of the external audit. Any significant findings or identified risks are closely reviewed and discussed to ensure that appropriate action is taken. Although no system of internal financial control can provide absolute assurance against material misstatement or loss, the Directors believe that the established framework of internal financial controls (outlined below) provides reasonable assurance that assets are safeguarded and that material errors and irregularities are either prevented or would be detected within a timely period.

- *Financial reporting – the financial results are reported monthly and compared to the budget for that period. Forecasts are prepared regularly throughout the year. The Group reports to shareholders on a half-yearly basis.*
- *Operating controls – all main business areas are required to self-certify their compliance with documented controls on a half-yearly basis. These certificates are reviewed by the Group's internal auditors. Independent and regular reviews of the Group's activities are carried out by the Group's internal auditors and, to the extent they consider necessary to support their audit report, the external auditors.*
- *Capital expenditure appraisal – the Group has guidelines for capital expenditure which include annual budgets, detailed appraisal and review procedures and appropriate levels of authorisation.*

- *The business of the Group, in common with other financial institutions, is also subject to the regulations and controls of a broad range of authorities. These include the Financial Services Authority (FSA), the Personal Investment Authority (PIA), the Investment Management Regulatory Organisation (IMRO) and the Department of Trade and Industry (DTI). The Group has well established compliance functions which are concerned with monitoring adherence to legal and regulatory requirements and internal procedures.*

- *Compliance philosophy – the Group has developed a compliance philosophy which encapsulates the Group's established values and standards and sets out its commitment to the highest levels of integrity and fair dealing. This philosophy reflects the manner in which the Group seeks to conduct its day-to-day activities and is designed to help staff understand and share in M&G's commitment to these standards.*

To keep under review the Group's compliance arrangements and the effectiveness of monitoring programmes and to consider proposed legislative and regulatory requirements, the Group has established a Regulation Committee. This Committee meets each month reporting to the Group's Executive Committee and also provides reports to the Audit and Compliance Committee.

The Board of Directors has overall responsibility for the Group's systems of internal financial control and for monitoring their effectiveness.

The Cadbury Code

The Company has complied with the recommendations of the Cadbury Committee's Code of Best Practice in relation to the management of the Group throughout the year.

Directors' Remuneration

The Greenbury report, published in July 1995, and the subsequent amendments to the Listing Rules of the London Stock Exchange have formalised the accountability, responsibility and disclosure relating to Directors' remuneration. The report to the Shareholders by the Remuneration Committee, together with note 5 on pages 25 and 26, incorporate the recommended disclosures. The Company complies fully with Section A of the best practice provisions annexed to the Listing Rules of the London Stock Exchange, which sets out recommendations regarding remuneration committees.

Report of the Auditors on Corporate Governance Matters to the Directors of M&G Group P.L.C.

Governance Matters

In addition to our audit of the financial statements, we have reviewed the Directors' statement on pages 42 and 43 on the Company's compliance with the paragraphs of the Cadbury Code of Best Practice specified for our review by the London Stock Exchange and their adoption of the going concern basis in preparing the financial statements. The objective of our review is to draw attention to non-compliance with Listing Rules 12.43(j) and 12.43(v).

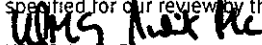
Basis of Opinion

We carried out our review in accordance with guidance issued by the Auditing Practices Board. This guidance does not require us to perform any additional work necessary to express a separate opinion on the effectiveness of either the Group's system of internal financial control or corporate governance procedures or on the ability of the Group to continue in operational existence.

Opinion

With respect to the Directors' statements on internal financial control and going concern on page 43, in our opinion the Directors have provided the disclosures required by the Listing Rules and such statements are not inconsistent with the information of which we are aware from our audit work on the financial statements.

Based on enquiry of certain Directors and Officers of the Company, and examination of relevant documents, in our opinion the Directors' statement on page 43 appropriately reflects the Company's compliance with the other paragraphs of the Code specified for our review by the Listing Rules.


KPMG Audit Plc
Chartered Accountants, Registered Auditor
London, 26th November 1997

Ten-Year Statistical Summary

| | 1988 £'000 | 1989 £'000 | 1990 £'000 | 1991 £'000 | 1992 £'000 | 1993 £'000 | 1994 £'000 | 1995 £'000 | 1996 £'000 | 1997 £'000 |
|--|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Turnover* | 188,001 | 281,023 | 282,412 | 244,807 | 281,205 | 323,734 | - | - | - | - |
| Revenue from Group consolidated activities* | | | | | | | 129,101 | 126,467 | 146,604 | 152,231 |
| Group Profits* | | | | | | | | | | |
| Profit before exceptional items and before tax (excluding realised and unrealised gains on investments) | 23,007 | 30,060 | 35,729 | 39,238 | 40,565 | 51,112 | 62,680 | 62,047 | 72,129 | 67,358 |
| Exceptional items | - | - | - | - | 1,157 | 230 | - | 18,835 | 7,632 | - |
| Tax | 7,487 | 9,848 | 11,645 | 11,897 | 11,854 | 14,880 | 19,584 | 12,774 | 20,361 | 21,144 |
| Profit after tax | 15,520 | 20,212 | 24,084 | 27,341 | 27,554 | 36,002 | 43,096 | 30,438 | 44,136 | 46,214 |
| Dividends | 6,545 | 9,345 | 12,831 | 14,462 | 15,127 | 18,780 | 22,345 | 23,858 | 26,878 | 29,938 |
| Retained profits before extraordinary items | 8,975 | 10,867 | 11,253 | 12,879 | 12,427 | 17,222 | 20,751 | 6,580 | 17,258 | 16,276 |
| Ordinary share capital & reserves* | 69,129 | 78,935 | 77,095 | 102,486 | 103,744 | 147,628 | 242,889 | 260,007 | 274,247 | 310,404 |
| Ordinary share statistics | | | | | | | | | | |
| Earnings before extraordinary and exceptional items (pence per share)* | 20.1 | 26.7 | 32.1 | 36.1 | 37.4 | 48.0 | 57.6 | 58.7 | 66.2 | 61.9 |
| Dividend (pence per share) | 8.50 | 12.50 | 17.00 | 19.00 | 20.00 | 25.00 | 30.00 | 32.00 | 36.0 | 40.0 |
| Dividend cover before exceptional items* | 2.4 | 2.2 | 1.9 | 1.9 | 1.9 | 1.9 | 1.9 | 1.8 | 1.8 | 1.5 |
| Net assets (pence per share)* | 89.8 | 105.6 | 102.2 | 134.7 | 137.3 | 196.5 | 326.6 | 348.7 | 367.8 | 414.6 |
| Return on average ordinary share capital & reserves* | | | | | | | | | | |
| Profit before exceptional items and before tax (excluding realised and unrealised gains on investments) as a percentage of the average ordinary share capital and reserves | 33.5 | 40.6 | 45.8 | 43.7 | 39.3 | 40.7 | 26.0 | 24.7 | 27.0 | 23.0 |
| Funds under management £m (excluding double counting) at 30th September | 4,938 | 6,915 | 5,947 | 7,899 | 7,473 | 10,558 | 11,796 | 13,789 | 15,554 | 18,104 |
| Number of accounts at 30th September | | | | | | | | | | |
| Unit trusts† | 488,056 | 557,411 | 614,543 | 629,300 | 618,524 | 637,564 | 748,933 | 815,954 | 849,401 | 831,166 |
| Investment trusts shareholders† | 6,296 | 6,639 | 6,665 | 6,845 | 58,188 | 59,873 | 58,116 | 57,877 | 86,017 | 88,817 |
| Life policies | 285,651 | 310,717 | 313,743 | 285,143 | 283,645 | 289,264 | 323,555 | 315,960 | 304,118 | 277,332 |
| Pensions policies | 38,283 | 49,221 | 52,799 | 57,575 | 60,046 | 61,042 | 63,716 | 64,426 | 62,544 | 61,124 |
| Windfall shares† | - | - | - | - | - | - | - | - | - | 25,816 |
| †PEP Accounts (included above) | 12,076 | 36,337 | 73,268 | 97,791 | 154,454 | 194,076 | 304,757 | 389,732 | 476,629 | 519,372 |
| Average number of employees during the year | 535 | 603 | 704 | 755 | 765 | 724 | 775 | 803 | 789 | 845 |
| FTSE All-share index | | | | | | | | | | |
| - At 30th September | 946.3 | 1,169.6 | 962.2 | 1,266.0 | 1,206.2 | 1,506.6 | 1,511.0 | 1,733.7 | 1,945.0 | 2,455.0 |
| - Average for the year | 925.8 | 1,063.3 | 1,120.8 | 1,140.1 | 1,205.7 | 1,384.5 | 1,586.3 | 1,587.4 | 1,842.1 | 2,136.0 |
| Annual percentage rate of inflation at 30th September | 5.9 | 7.6 | 10.9 | 4.1 | 3.6 | 1.8 | 2.2 | 3.9 | 2.1 | 3.6 |

* From 1994 onwards profit has been calculated by consolidating the results of the assurance subsidiaries using the 'modified statutory solvency' basis of accounting (data shown in blue).

*Turnover represents revenue derived from the purchase and sale of unit and investment trusts, management and other fees, and the premium income of the assurance business.

Analysis of Ordinary Shareholders

| as at 17th November 1997 | Number of Holdings | Number of Shares held | % of Capital |
|---|-----------------------|--------------------------|-----------------|
| Category of Shareholder | | | |
| Esmée Fairbairn Charitable Trust | 1 | 25,000,000 | 33.39 |
| Individuals | 6,658 | 8,782,387 | 11.73 |
| Nominee Companies | 1,151 | 34,912,802 | 46.63 |
| Limited Companies | 110 | 2,326,011 | 3.11 |
| Insurance Companies | 5 | 574,900 | 0.77 |
| Other corporate bodies | 74 | 2,193,279 | 2.93 |
| Pension funds | 5 | 782,021 | 1.04 |
| Employees' Profit Sharing Scheme | 1 | 305,830 | 0.40 |
| Totals | 8,005 | 74,877,230 | 100.00 |
| Number of shares held by Individuals | | | |
| 1-1,000 | 5,734 | 2,945,364 | 3.93 |
| 1,001-2,000 | 521 | 852,610 | 1.14 |
| 2,001-3,000 | 133 | 343,213 | 0.46 |
| 3,001-5,000 | 106 | 422,000 | 0.56 |
| 5,001-10,000 | 83 | 601,168 | 0.80 |
| 10,001-20,000 | 29 | 399,759 | 0.53 |
| 20,001-50,000 | 29 | 872,199 | 1.17 |
| 50,001-100,000 | 16 | 1,025,871 | 1.37 |
| 100,001-250,000 | 5 | 732,151 | 0.98 |
| 250,001-500,000 | 2 | 588,052 | 0.79 |
| Totals | 6,658 | 8,782,387 | 11.73 |

Capital Gains Tax Information

For the sale of shares by a shareholder the following values of M&G shares may be relevant:

The market value as at 31st March 1982 adjusted for subsequent capital changes was 37.5p.

The market value as at 31st March 1982 adjusted for subsequent capital changes and the movement in the Retail Prices Index from that date to 30th September 1997 is 75.2p.

Corporate Personal Equity Plans (PEPs)

In 1992 M&G introduced a General PEP and a Single Company PEP.

Details may be obtained from and queries directed to:

The Plan Manager,
Bradford & Bingley PEPs Limited,
P.O. Box 50, Main Street,
Bingley, West Yorkshire BD16 2LW

Bradford & Bingley
Telephone Helpline (01274) 555667

Executive Committee

M&G Group P.L.C.

Anthony Ashplant
Vivian Bazalgette
Peter Emms
Richard Hughes
Martin Lewis
Michael McLintock
David Watson

Non-Executive Directors of Subsidiary Undertakings

M&G (Guernsey) Limited

Ken Rowe
(Chairman) A Guernsey
resident and a Jurat of the
Royal Court in Guernsey.
A director of a number of
companies.

Peter Creed
A Guernsey resident and
Director responsible for
investment management
services provided by Kleinwort
Benson (Guernsey) Limited and
Kleinwort Benson (Jersey)
Limited.

David Hinshaw
A Guernsey resident and Chief
Executive of Kleinwort
Benson's Channel Islands
companies.

Len Moss
A Guernsey resident and a Jurat
of the Royal Court in Guernsey.
A director of a number of
companies.

M&G Life Assurance Company Limited

**M&G Pensions and
Annuity Company
Limited**

M&G Securities Limited

M&G Financial Services Limited

Stuart C James
Senior Partner at Rowe & Maw
and Head of the Pensions
Department. A council member
of the Society of Pension
Consultants and Fellow of the
Pensions Management
Institute. A director of a
number of companies.

Sir Robert McCrindle
A Member of Parliament,
1970–1992, Chairman of the
Parliamentary Committee on
Financial Services, 1989–1992.
Adviser to British Insurance
and Investment Brokers
Association, 1976–1992.
A director of a number of
companies.

Notice of Meeting

NOTICE IS HEREBY GIVEN that the Thirty-Ninth Annual General Meeting of the Members of the Company will be held at Painters Hall, Little Trinity Lane, London EC4 on Wednesday 14th January 1998 at 12 noon to transact the following business:-

Ordinary Resolutions

- Resolution 1** To receive and consider the report of the Directors and the accounts for the year ended 30th September 1997.
- Resolution 2** To declare a final dividend.
- Resolution 3** To re-elect A G Down as a Director.
- Resolution 4** To re-elect R S Hughes as a Director.
- Resolution 5** To re-elect M Lewis as a Director.
- Resolution 6** To re-elect M G A McIntock as a Director.
- Resolution 7** To re-appoint KPMG Audit Plc as the Company's Auditors and to authorise the Directors to fix their remuneration.

Other Business

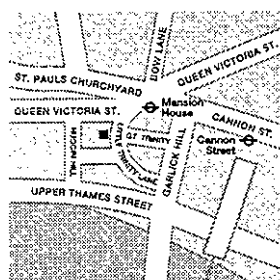
As Special Business to consider and, if thought fit, pass the following resolution, which will be proposed as a Special Resolution:-

Resolution 8 That in accordance with Article 10(c) of its Articles of Association and Section 166 of the Companies Act 1985, the Company be and is hereby granted general and unconditional authority to make market purchases (as defined in Section 163 of the Companies Act 1985) of any of its own Ordinary Shares on such terms and in such manner as the Board of Directors of the Company may from time to time determine PROVIDED THAT the general authority conferred by this Resolution shall:-

- (a) be limited to 7,500,000 Ordinary Shares of 25p each;
- (b) not permit the payment per Share of more than 5% above the average middle market quotation of the Ordinary Shares of the Company in the London Stock Exchange Daily Official List on the five dealing days immediately prior to the date of purchase or less than 25p (in each case exclusive of advance corporation tax payable (if any) and expenses);
- (c) expire 18 months after the date of the passing of this Resolution or (if earlier) at the next Annual General Meeting should a similar resolution be proposed (except in relation to the purchase of Shares the contract for which was concluded before the expiration of the said period and which might be executed wholly or partly after such date);
- (d) be in substitution for and replace the authority to purchase Ordinary Shares of the Company conferred on the Board of Directors at the Annual General Meeting of the Company held on 29th January 1997.

By order of the Board of Directors, S H Henton, Secretary

3 Minster Court, Great Tower Street, London EC3R 7XH, 16th December 1997



■ Painters Hall

1. Any member of the Company entitled to attend and vote at the above Meeting may appoint one or more persons as his proxy or proxies to attend and, on a poll, vote in his stead. A proxy need not be a Member of the Company.
2. The appointment of a proxy will not preclude a Member from attending the Meeting and voting thereat in person.
3. Copies of all Directors' contracts of service will be available for inspection at the registered office of the Company during normal business hours and, together with the Register of Directors' Interests, at the place of the Annual General Meeting for at least fifteen minutes prior to and during the Meeting.

Registered and Other Offices

London

Registered Office:

3 Minster Court

Great Tower Street

London EC3R 7XH

Telephone: 0171-626-4588

Telex: 887196

Facsimile: 0171-623- 8615

(Registered in England No. 633480)

Chelmsford

M&G House

Victoria Road

Chelmsford CM1 1FB

Telephone: 01245 390390

Telex: 99335

Facsimile: 01245 267789

Sales Support Centres are located in

Birmingham

Bristol

London

Manchester

Two subsidiary companies are located in Guernsey

Internet

http://www.iii.co.uk/m_g

Email: info@mandg.co.uk

Principal Advisers

Auditors

KPMG Audit Plc

PO Box 695

8 Salisbury Square

London EC4Y 8BB

Stockbrokers

Cazenove & Co.

12 Tokenhouse Yard

London EC2R 7AN

Merchant Bankers

ING Barings

60 London Wall

London EC2M 5TQ

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