

PaineWebber International (U.K.) Ltd

Registered No. 2418504

DIRECTORS

I D Myers (Chairman)
B Barefoot
D Francese
G A Larramendi
M O'Hanlon
S B Phillips
G Stanley
J A Wieland
M Woolf

SECRETARY

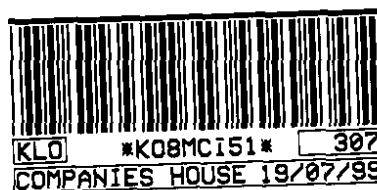
J G Rose

AUDITORS

Ernst & Young
Rolls House
7 Rolls Buildings
Fetter Lane
London EC4A 1NH

REGISTERED OFFICE

1 Finsbury Avenue
London EC2M 2NA



DIRECTORS' REPORT

The directors present their report and the financial statements for the year ended 31 December 1998.

REVIEW OF THE BUSINESS

The company's profit for the year after taxation amounted to \$31,262,000 (1997 - \$17,479,000). The company paid a dividend of \$2,500,000 (1997 - \$15,000,000) during the year. No further dividend is proposed.

The company is a member of The Securities and Futures Authority Limited. Its principal activity is engaging in financial services both on its own account and on behalf of its clients.

The company operates two branches in Switzerland.

YEAR 2000 COMPLIANCE

As is well known, many computer and digital storage systems express dates using only the last two digits of the year and will thus require modification or replacement to accommodate the Year 2000 and beyond in order to avoid malfunctions and resulting widespread commercial disruption. This is a complex and pervasive issue. The operation of our business depends not only on our own computer systems, but also to some degree on those of our suppliers and customers. This could expose us to further risk in the event that there is failure by other parties to remedy their own Year 2000 issues.

A company-wide programme, designed to address the impact of the Year 2000 on our business, has been commissioned by the Board and is under way. Resources have been allocated and the designated Board members responsible for the programme receive regular reports on progress.

A significant risk analysis has been performed to determine the impact of the issue on all our activities. From this, prioritised action plans have been developed which are designed to address the key risks in advance of critical dates and without disruption to the underlying business activities and processes. Priority is given to those systems which could cause a significant financial or legal impact on the company's business if they were to fail. The plan also includes a requirement for the testing of systems changes, involving the participation of users.

The risk analysis also considers the impact on our business of Year 2000 related failures by our significant suppliers (including computer bureaux) and customers. In appropriate cases we have initiated formal communication with these other parties.

Given the complexity of the problem, it is not possible for any organisation to guarantee that no Year 2000 problems will remain, because at least some level of failure may still occur. However, the Board believes that it will achieve an acceptable state of readiness and has also provided resources to deal promptly with significant subsequent failures or issues that might arise.

Much of the cost of implementing the action plans will be subsumed into the recurring activities of the departments involved. The total cost of modifications to our computer hardware and software is estimated at \$2.2m, of which \$0.9m is new equipment that will be capitalised and the remaining \$1.3m will be expensed as incurred. Of this \$2.2m total, expenditure of \$0.6m has been incurred during the year and the remaining \$1.6m is expected to be spread fairly evenly during 1999.

FIXED ASSETS

The changes in fixed assets during the year are summarised in the notes to the financial statements.

DIRECTORS' REPORT

DIRECTORS AND THEIR INTERESTS

The directors during the year and at the date of this report were as follows:

I D Myers (Chairman)
B Barefoot
D Francese
G A Larramendi
M O'Hanlon
S B Phillips
G Stanley
J A Wieland
M Woolf

None of the directors had a disclosable interest in the shares of the company, its holding company, or fellow subsidiaries.

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ACCOUNTS

Company law requires the directors to prepare accounts for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing those financial statements, the directors are required to:

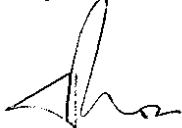
- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper 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. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

AUDITORS

A resolution to re-appoint Ernst & Young as auditors will be put to the members at the Annual General Meeting.

By order of the board



J G Rose

Secretary

31 MAR 1999

REPORT OF THE AUDITORS**to the members of PaineWebber International (U.K.) Ltd**

We have audited the financial statements on pages 5 to 14, which have been prepared under the historical cost convention and on the basis of the accounting policies set out in note 1.

Respective responsibilities of directors and auditors

As described on page 3 the company's directors are responsible for the preparation of the 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.

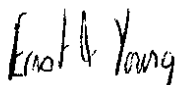
Basis of opinion

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

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

Opinion

In our opinion the financial statements give a true and fair view of the state of the company's affairs as at 31 December 1998 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.



Ernst & Young
Registered Auditor
London

31 MAR 1999

PaineWebber International (U.K.) Ltd

PROFIT AND LOSS ACCOUNT for the year ended 31 December 1998

	<i>Notes</i>	<i>1998 \$000</i>	<i>1997 \$000</i>
OPERATING INCOME	2	146,857	113,242
Administrative expenses		(100,241)	(86,704)
OPERATING PROFIT		<u>46,616</u>	<u>26,538</u>
Interest receivable	3	1,138	659
Interest payable	4	(1,894)	(1,901)
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION	5	<u>45,860</u>	<u>25,296</u>
Taxation on profit on ordinary activities	7	(14,598)	(7,817)
PROFIT ON ORDINARY ACTIVITIES AFTER TAXATION	15	<u>31,262</u>	<u>17,479</u>
Dividends		(2,500)	(15,000)
RETAINED PROFIT FOR THE YEAR		<u><u>28,762</u></u>	<u><u>2,479</u></u>

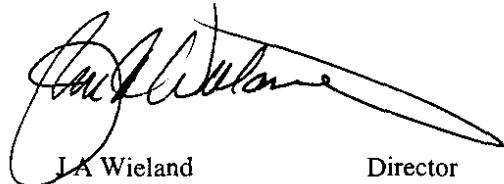
A statement of total recognised gains and losses has not been provided as there were no recognised gains or losses other than the profit for the year.

PaineWebber International (U.K.) Ltd

BALANCE SHEET

at 31 December 1998

	Notes	1998 \$000	1997 \$000
FIXED ASSETS			
Tangible assets	8	8,978	10,271
Investments	9	797	797
		<u>9,775</u>	<u>11,068</u>
CURRENT ASSETS			
Securities inventory		1,825,716	2,130,564
Debtors	10	6,649,499	7,359,607
Cash at bank and in hand		31,577	32,213
		<u>8,506,792</u>	<u>9,522,384</u>
CREDITORS: amounts falling due within one year	11	<u>(8,278,837)</u>	<u>(9,288,070)</u>
NET CURRENT ASSETS		<u>227,955</u>	<u>234,314</u>
TOTAL ASSETS LESS CURRENT LIABILITIES		<u>237,730</u>	<u>245,382</u>
CREDITORS: amounts falling due after more one year	12	-	(36,000)
PROVISION FOR LIABILITIES AND CHARGES			
Deferred taxation	13	(138)	(552)
		<u>237,592</u>	<u>208,830</u>
CAPITAL AND RESERVES			
Called up share capital	14	1,410	1,410
Share premium account	15	121,526	121,526
Profit and loss account	15	114,656	85,894
		<u>237,592</u>	<u>208,830</u>


 J.A. Wieland Director

31 MAR 1999

NOTES TO THE FINANCIAL STATEMENTS
at 31 December 1998

1. ACCOUNTING POLICIES

Accounting convention

The financial statements are prepared under the historical cost convention as modified by the inclusion of trading positions at market value. The financial statements are prepared in accordance with applicable accounting standards.

Preparation of financial statements in US dollars

It is considered that a fairer reflection of the company's activities is given by presenting the financial statements in US dollars since the majority of the company's transactions are denominated in this currency.

Securities inventory

Securities inventory consists of securities, warrants, options and futures and are valued at market prices ruling at the balance sheet date. Warrants issued, options written and short securities positions are included within creditors.

Income recognition

Income from securities transactions is accounted for on a trade date basis.

Underwriting commissions, corporate finance, management and syndication fees are credited to income on the completion of the related offerings.

Depreciation

Tangible assets are written off over their estimated useful lives on a straight line basis. Office equipment comprises computer equipment and fixtures and fittings. The estimated useful lives of these assets are as follows:

Computer equipment	-	3-7 years
Fixtures and fittings	-	5-10 years

Fixed asset investments

Fixed asset investments consist of market memberships and are stated at the lower of cost and market value.

Foreign currencies

Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date. Transactions in foreign currencies are recorded at the rate of exchange ruling at the transaction date. All differences are taken to the profit and loss account.

Stock borrowing and lending transactions

Stock borrowing and lending transactions are reflected in debtors and creditors, respectively, only to the extent that collateral given or received is in the form of cash. Details of stock borrowing and lending transactions against non cash collateral are shown in note 17.

Repurchase and resale agreements

In the course of financing its business and as part of its trading activities, the company enters into arrangements which involve the sale of securities with agreements to repurchase and the purchase of securities with resale agreements. Repurchase agreements are recorded as liabilities and the related securities, where owned by the company, are included in stock of marketable securities at market value. Resale agreements are recorded as debtors.

NOTES TO THE FINANCIAL STATEMENTS
at 31 December 1998

1. ACCOUNTING POLICIES (continued)

Deferred taxation

Deferred taxation is provided on the liability method on all timing differences to the extent that they are expected to reverse in the future without being replaced, calculated at the rate at which it is estimated that taxation will be payable.

Operating leases

Rentals paid under operating leases are charged on a straight line basis over the term of the lease.

Cash flow statement

A cash flow statement has not been prepared as the company's cash flows are consolidated into the consolidated cash flow statement prepared by PaineWebber UK Holdings.

2. OPERATING INCOME

Operating income has been disclosed instead of turnover as this reflects more accurately the results and nature of the company's activities, including trading interest income and expense recorded on a trade date basis. Operating income represents the amounts derived from the provision of services which fall within the company's continuing activities and is stated net of value added tax.

The directors consider that the company operates within a single class of business. The disclosure of income by geographical regions has been omitted as the directors consider that it would be seriously prejudicial to disclose this information.

Operating income includes trading interest income and expense as follows:

	1998 \$000	1997 \$000
Trading interest income:		
Group undertakings	33,591	45,944
Bank deposits and long positions	123,459	74,048
	<u>157,050</u>	<u>119,992</u>
Trading interest expense:		
Group undertakings	8,246	33,153
Loans, overdrafts and short positions	108,851	53,956
	<u>117,097</u>	<u>87,109</u>

Interests on loans, overdrafts and short positions exclude interest on subordinated debt (see note 4).

3. INTEREST RECEIVABLE

	1998 \$000	1997 \$000
Other	<u>1,138</u>	<u>659</u>

NOTES TO THE FINANCIAL STATEMENTS
at 31 December 1998

4. INTEREST PAYABLE AND SIMILAR CHARGES

	1998 \$000	1997 \$000
Group undertakings	1,894	1,901

5. PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION

(a) This is stated after charging:

	1998 \$000	1997 \$000
Directors' emoluments	2,995	2,414
Auditors' remuneration	273	251
Depreciation	2,760	2,858
Operating lease rentals - land and buildings	2,249	2,103
- other	649	641
Pension costs	1,714	1,542

Additional fees of \$327,340 were paid to the auditors during the year in respect of non audit services (1997 - \$151,331).

(b) Directors' remuneration:

Directors' remuneration consists of fees and other emoluments paid to the directors of the company in respect of their duties in the management of the company.

	1998 \$000	1997 \$000
Total emoluments	2,548	2,299
Contributions to defined contribution pension schemes	96	115
Compensation for loss of office (including a pension contribution of \$163,000)	351	-
	2,995	2,414

The emoluments and pension contributions of the highest paid director were £713,316 (1997 - £392,495) and £10,600 (1997 - £5,600), respectively.

NOTES TO THE FINANCIAL STATEMENTS
at 31 December 1998

6. EMPLOYEES

	1998 No.	1997 No.
Average monthly number of employees	246	238
	\$000	\$000
Wages and salaries	54,140	50,536
Social security costs	6,370	5,609
Other pension costs	1,714	1,542
	<u>62,224</u>	<u>57,687</u>

The company operates two defined contribution pension schemes, both of which require contributions to be made to separately administered funds. Contributions to these funds are charged to the profit and loss account as they become payable in accordance with the rules of the scheme.

7. TAXATION ON PROFIT ON ORDINARY ACTIVITIES

The taxation charge is made up as follows:

	1998 \$000	1997 \$000
Based on the profit for the year:		
UK Corporation tax at 31% (31.5% - 1997)	14,842	8,145
Prior Year Release	-	(750)
Total UK Tax	<u>14,842</u>	<u>7,395</u>
Swiss Tax	170	501
Deferred taxation	(414)	(79)
	<u>14,598</u>	<u>7,817</u>

NOTES TO THE FINANCIAL STATEMENTS

at 31 December 1998

8. TANGIBLE FIXED ASSETS

	<i>Office equipment \$000</i>
Cost:	
At 1 January 1998	18,661
Additions	1,474
Disposals	(306)
At 31 December 1998	<u>19,829</u>
Depreciation:	
At 1 January 1998	8,390
Provided during the year	2,760
Disposals	(299)
At 31 December 1998	<u>10,851</u>
Net book value:	
At 31 December 1998	<u>8,978</u>
At 1 January 1998	<u>10,271</u>

9. FIXED ASSET INVESTMENTS

	<i>1998 \$000</i>
Valuation:	
At 1 January and 31 December	<u>797</u>

There were no additions or disposals during the year.

10. DEBTORS

	<i>1998 \$000</i>	<i>1997 \$000</i>
Securities purchased under agreements to resell		
-third parties	5,111,362	6,190,713
-group undertakings	274,968	374,212
Trade debtors	487,902	449,917
Collateral on stock borrowed from group undertakings	695,204	199,754
Trade receivable from group undertakings	6,132	62,651
Collateral on stock borrowed from third parties	12,277	19,617
Prepayments and accrued income	53,196	55,902
Group undertakings	6,489	4,998
Other debtors	1,969	1,843
	<u>6,649,499</u>	<u>7,359,607</u>

PaineWebber International (U.K.) Ltd

NOTES TO THE FINANCIAL STATEMENTS

at 31 December 1998

11. CREDITORS: amounts falling due within one year

	1998 \$000	1997 \$000
Securities sold under agreements to repurchase		
-third parties	6,472,520	7,496,443
-group undertakings	3,550	14,952
Securities sold not yet purchased	565,219	889,832
Trade creditors	200,683	307,422
Collateral on stock lent to third parties	685,720	151,539
Bank loans and overdrafts	64,835	186,791
Group undertakings	155,098	138,605
Collateral on stock lent to group undertakings	16,217	17,554
Accruals and other creditors	62,127	76,722
UK corporation tax	13,998	5,045
Subordinated loan from Paine Webber Group Inc.	30,000	—
Subordinated loan from PaineWebber International Futures Ltd	6,000	—
Other taxes and social security costs	2,870	3,165
	<u>8,278,837</u>	<u>9,288,070</u>

The subordinated loans are due to be repaid on 31 December 1999. Early repayment can be made at the discretion of the company and subject to the approval of The Securities and Futures Authority Limited.

12. CREDITORS: amounts falling due after more one year

	1998 \$000	1997 \$000
Subordinated loan from Paine Webber Group Inc.	—	30,000
Subordinated loan from PaineWebber International Futures Ltd	—	6,000
	<u>—</u>	<u>36,000</u>

13. DEFERRED TAXATION

Full provision has been made for deferred taxation. The movement for the year was:

	1998 \$000
As of 31 December 1997	552
Short Term Timing Differences	(414)
As of 31 December 1998	<u>138</u>

NOTES TO THE FINANCIAL STATEMENTS
at 31 December 1998

14. CALLED-UP SHARE CAPITAL

	1998 000s	1997 000s
Authorised:		
Ordinary shares of \$1 each	1,500	1,500
	<u> </u>	<u> </u>
	\$000	\$000
Allotted, called up and fully paid:		
Ordinary shares of \$1 each	1,410	1,410
	<u> </u>	<u> </u>

15. RECONCILIATION OF SHAREHOLDERS' FUNDS AND MOVEMENTS ON RESERVES

	Share capital \$000	Share premium account \$000	Profit and loss account \$000	Total \$000
At 1 January 1997	1,410	121,526	83,415	206,351
Profit for the year			17,479	17,479
Dividend paid			(15,000)	(15,000)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
At 1 January 1998	1,410	121,526	85,894	208,830
Profit for the year			31,262	31,262
Dividend paid			(2,500)	(2,500)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
At 31 December 1998	1,410	121,526	114,656	237,592
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

16. RELATED PARTY TRANSACTIONS

The company has taken advantage of the exemption given in FRS8 to subsidiaries from disclosing related party transactions with other group companies.

17. CONTINGENT LIABILITIES

The company borrows and lends stock against non-cash collateral, as well as cash collateral, in the form of other stocks, bonds and standby letters of credit. These amounts are excluded from the balance sheet in accordance with general industry practice. The market value of non-cash collateral in use at 31 December was:

	1998 \$000	1997 \$000
Received in respect of stock lent	39,933	80,771
Given in respect of stock borrowed	55,225	235,704
	<u> </u>	<u> </u>

NOTES TO THE FINANCIAL STATEMENTS

at 31 December 1998

18. OBLIGATIONS UNDER LEASES

The annual commitments under non-cancellable operating leases are as follows:

	<i>Land and buildings</i>	<i>Other</i>	<i>Land and buildings</i>	<i>Other</i>
	<i>1998</i>	<i>1998</i>	<i>1997</i>	<i>1997</i>
	<i>\$000</i>	<i>\$000</i>	<i>\$000</i>	<i>\$000</i>
Operating leases which expire:				
Within one year	58	67	69	68
In the second to fifth years inclusive	680	550	733	575
Over five years	1,538	—	1,520	—
	<u>2,276</u>	<u>617</u>	<u>2,322</u>	<u>643</u>

19. ULTIMATE HOLDING COMPANY

PaineWebber UK Holdings, a company registered in England and Wales, is the parent undertaking of the smallest group for which group accounts are prepared. Copies of these group accounts can be obtained from 1 Finsbury Avenue, London, EC2M 2NA.

Paine Webber Group Inc., which is incorporated in the State of Delaware, USA, is the ultimate holding company and is the parent undertaking of the largest group for which group accounts are prepared. Copies of these group accounts can be obtained from 1285 Avenue of the Americas, New York City, USA.