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Close Brothers



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Annual Report 2002



Close Brothers

PROFILE

Close Brothers Group plc is an independent merchant banking group listed on the London Stock Exchange. Founded in the City of London over 120 years ago, Close Brothers is amongst the 200 largest companies by market capitalisation listed on the London Stock Exchange and employs over 1,800 people.

The group's activities comprise asset management, banking, corporate finance and market-making.

The group's major shareholders are large financial investors including investment groups, insurance companies and pension funds. The group's management and staff also have significant holdings directly, through share ownership schemes and through option schemes. Some management also have minority interests in certain subsidiaries. In addition, more than 2,800 private individuals hold shares directly in the group.

Close Brothers' strategy is to provide a diverse range of specialist financial services where we believe we can offer added value to our clients as a result of our particular expertise. We are dedicated to developing continuity in our relationships with clients through excellent service, objective advice and uncompromising professionalism.

We have concentrated on building up a balanced mix of activities in the financial sector and our aim is to deliver to our shareholders, over time, a consistent and increasing stream of profits and dividends.

HIGHLIGHTS

	2002	2001
Profit before taxation, exceptional costs and goodwill amortisation	£78.5m	£94.2m
Earnings per share before exceptional costs and goodwill amortisation	38.9p	47.4p
Profit before taxation	£68.4m	£89.5m
Earnings per share	32.3p	44.0p
Dividends per share	26.0p	26.0p
Shareholders' funds	£472m	£408m
Total assets	£3.1bn	£2.8bn

DIRECTORS AND ADVISERS

Directors of Close Brothers Group plc

Executive Directors

R.D. Kent, M.B.A., aged 55, Managing Director until the forthcoming Annual General Meeting after which he will become a non-executive director and consultant. He joined Close Brothers in 1974 having started his City career with Schroders. He was a partner in the management buy-out of Close Brothers in 1979 and was appointed to the board in August, 1984. He is also non-executive chairman of Grosvenor Limited and is a non-executive director of Bradford & Bingley Group plc (chairman designate) and Whitbread plc.

C.D. Keogh, M.B.A., Barrister, A.T.I.I., aged 49, will be appointed Chief Executive following the forthcoming Annual General Meeting. He joined Close Brothers in 1985 having previously been employed by Saudi International Bank and Arthur Andersen. Appointed a director in August, 1995.

P.L. Winkworth, F.C.A., A.T.I.I., aged 54, will be appointed joint Managing Director following the forthcoming Annual General Meeting with continued responsibility for finance. He was employed by KPMG and Barings, before joining Close Brothers in 1977. He was a partner in the management buy-out of Close Brothers in 1979 and was appointed to the board in August, 1984.

S.R. Hodges, Barrister, aged 48, will be appointed joint Managing Director following the forthcoming Annual General Meeting with continued responsibility for the banking division. He joined Close Brothers in 1985 having previously been employed by Hambros. Appointed a director in August, 1995.

D.G. Hardisty, aged 59, joined Close Brothers in 1987 to set up our asset finance business and was appointed a director in August, 1995. He was previously employed by British Credit Trust and North West Securities.

M.A. Hines, M.S.I., aged 53, joined Close Brothers in 1993 on the acquisition of Winterflood Securities and was appointed a director in March, 2002. He was previously employed by Bisgood Bishop. His alternate is the joint chief executive of our market-making division, **D.J. Macnamara**, aged 45, who also joined Close Brothers in 1993 on the acquisition of Winterflood Securities and who was also previously employed by Bisgood Bishop.

D.C. Pusinelli, A.C.A., aged 46, was appointed a director in September, 2002. Having previously qualified with Coopers & Lybrand he joined the corporate finance division of Close Brothers in 1986 and has been working within head office on the development activities of the company since 1998. He will continue to be responsible for corporate development.

Non-Executive Directors

Sir David Scholey, C.B.E., Chairman, aged 67, was previously chairman of the SG Warburg Group and is a senior adviser to UBS Warburg. His current directorships include Anglo American plc, Vodafone Group plc and The Chubb Corporation. Appointed to the board in March, 1999. Chairman of the Nomination Committee.

P.N. Buckley, C.A., aged 60, is the chairman of Caledonia Investments plc, which has an 18 per cent. shareholding in the company. His other directorships include Offshore Logistics, Inc. and Kerzner International Hotels Limited. Appointed to the board in November, 1995. His alternate is **M.G. Wyatt**, aged 64, a non-executive director of Caledonia Investments plc.

A.H. Farley, Solicitor, aged 56, was one of the founding partners of City solicitors, Watson, Farley and Williams, to whom he is now senior adviser. His other directorships include Opus Trust Limited and Opus Portfolio Limited. Appointed to the board in September, 1993. Chairman of the Audit Committees.

M.G.A. McLintock, aged 41, is chief executive of M&G and a director of Prudential plc. Prior to joining M&G he worked for Barings and Morgan Grenfell. Appointed to the board in May, 2001.

P.S. Wilmot-Sitwell, aged 67, was the senior partner of Rowe and Pitman and following the merger with SG Warburg, he became chairman of SG Warburg Securities and vice chairman of the SG Warburg Group until his retirement in 1994. He is chairman of Mercury World Mining Trust plc. Appointed to the board in November, 1995. Chairman of the Remuneration Committee.

Secretary

R.D. Sellers, A.C.A.

Auditors

Deloitte & Touche.

Ernst & Young LLP (Close Brothers Limited group).

Solicitors

Freshfields Bruckhaus Deringer.

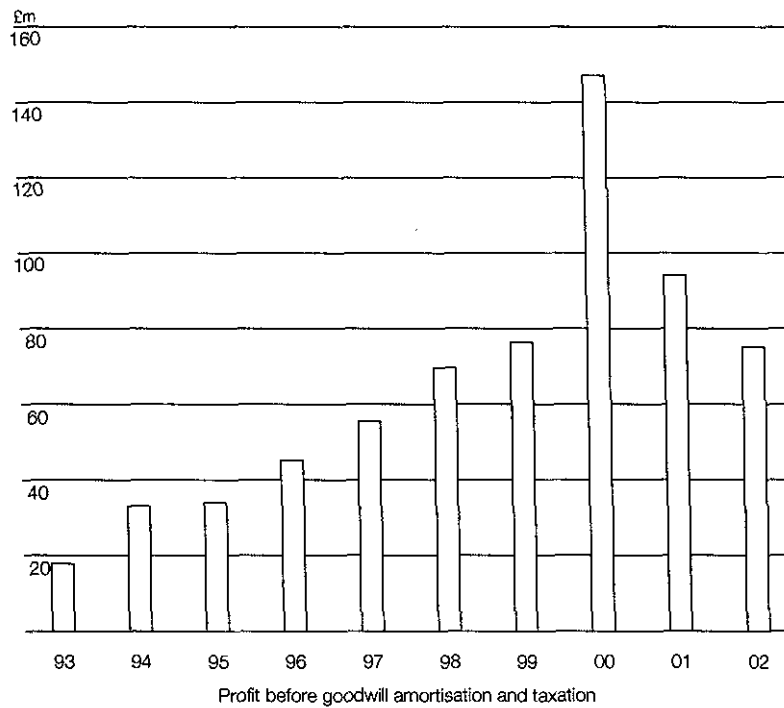
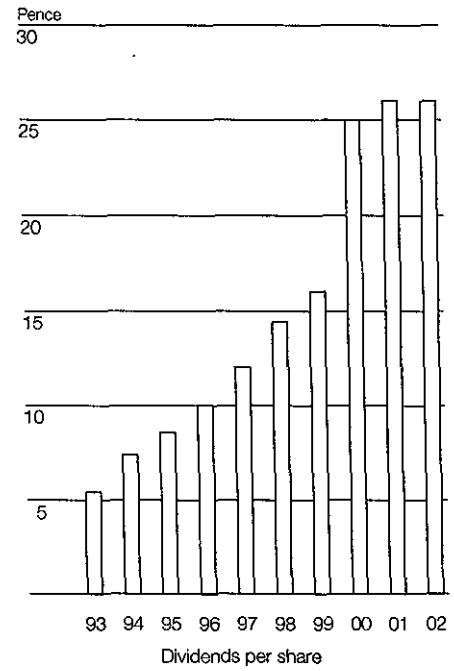
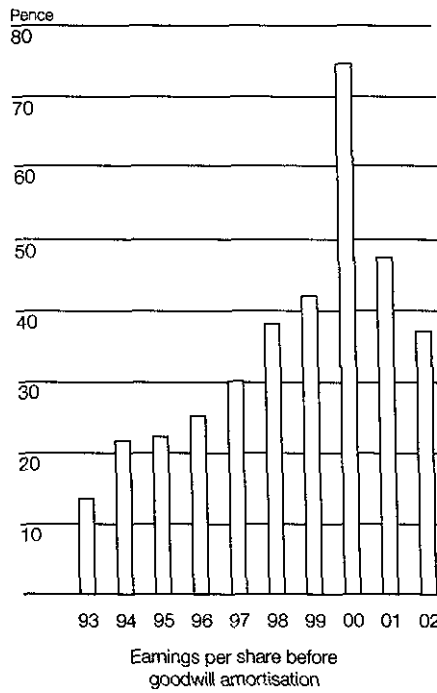
Stockbrokers

UBS Warburg.



Close Brothers

HISTORICAL TRENDS



CHAIRMAN'S STATEMENT

RESULTS

The operating profit on ordinary activities before taxation, exceptional costs and goodwill amortisation was £78.5 million, compared to £94.2 million last year, and earnings per share, on the same basis, were 38.9p compared to 47.4p.

After deducting a charge for exceptional costs of £3.4 million (2001 — £Nil) and goodwill amortisation of £6.7 million (2001 — £4.7 million), the operating profit on ordinary activities before taxation was £68.4 million (2001 — £89.5 million) and earnings per share, on the same basis, were 32.3p (2001 — 44.0p).

The board is recommending a final dividend of 17p per share which, together with the interim dividend, gives a total dividend for the year of 26p per share. This is the same as last year's total dividend and, based on the above earnings per share of 38.9p, is covered some 1.5 times.

OVERVIEW

The year ended 31st July, 2002 was another difficult one. The tragic events of 11th September, 2001 made for a turbulent start. Whilst stock markets appeared to recover swiftly, the rebound was short lived. Confidence both in business generally and, more particularly, in the City's financial markets continued to suffer, exacerbated in the second half of our financial year as deteriorating economic news and corporate scandals in the USA undermined stock markets.

It is a considerable achievement that in this climate the group has produced consistent profits (before tax and goodwill amortisation) for the last three of the previous four half years as illustrated below:

First half 2001	Second half 2001	First half 2002	Second half 2002
£57.9m	£36.3m	£37.4m	£37.7m

This steadiness has been achieved through our strategy of building a portfolio of diverse and distinct specialist activities. Thus, whilst the fall in equity markets affected to varying degrees our corporate finance, asset management and market-making businesses, this was counterbalanced by substantial growth in our banking division.

External market events had the most severe effect on our corporate finance division. Although the sharp downturn in M&A activity was offset to some extent by the success of our debt advisory and restructuring activities we nevertheless regretfully decided to reduce our headcount in the UK, in November, 2001 and July, 2002, which gave rise to exceptional costs of £3.4 million. These aside, the division managed to make a modest profit.

Our asset management and market-making divisions were, of course, not immune to these cold winds. Despite a commendable net inflow of £417 million of new funds, the decline in market values took its toll and over the year funds under management were broadly unchanged. Furthermore this year we did not benefit from performance fees in our technology funds, which suffered the severest downturn in valuations. As a result, profits in asset management deteriorated by approximately one third.

In market-making the green shoots that seemed to appear in late Autumn last year swiftly withered and the year ended on a subdued note. However, despite profits declining to £16.8 million this year from £27.4 million last year, Winterflood Securities Limited ("WINS") more than maintained its market share and increased its coverage substantially.

Our banking division produced substantial organic growth virtually across the board with pre-tax profits rising by 35 per cent. and the loan book increasing some 19 per cent. to over £1.4 billion. Bad debt levels continued to remain under good control.

As a result of all of the above factors and in the face of the volatility in financial markets, the mix of our operating profit has changed considerably over the past three years, as shown in the table below:

	2000	2001	2002
Asset Management	9%	23%	18%
Corporate Finance	6%	12%	2%
Banking	20%	39%	61%
Market-Making	65%	26%	19%
	<u>100%</u>	<u>100%</u>	<u>100%</u>

TRADING

Asset Management

The asset management division had a disappointing year principally because the success in gaining new funds to manage of £417 million net of withdrawals has been eroded by the falls in the market. As a result of this, our funds under management at the year end of some £3.1 billion have barely improved on the level last year. Our specialist technology funds, while performing well in relation to similar funds, have fallen sharply in absolute terms and we have not benefited from performance fees this year. The upshot was a lower profit, of £15.9 million, down from last year's £23.9 million, but ahead of that two years ago.

A substantial part of our asset management business relates to our offshore and unquoted operations, which are less vulnerable to the vagaries of the market than our listed funds. In the past year, some of our Channel Islands



Close Brothers

CHAIRMAN'S STATEMENT

businesses have been going through a period of reorganisation and have moved premises, which will be of long-term benefit.

We are confident that our strategy of focussing on specialist areas of asset management, such as private equity, private clients, quant-based products and technology and property funds, will prove to be rewarding over the medium term. The immediate outlook, however, continues to be unexciting.

Corporate Finance

Our corporate finance division had a very difficult year with the initial optimism reversed following 11th September, since when the market has been quiet and declining. This led to a detailed review of our UK cost structure and necessitated some, mainly voluntary, redundancies amongst our staff. By contrast, our French and German businesses, while experiencing testing market conditions, were able to recruit some new professional staff and since the year end we have also doubled our shareholding in Atlas Capital (Spain) to 20 per cent.

During the period we have been active on corporate restructuring work, which has enabled us to declare a modest profit (excluding exceptional costs) for the year of £2.1 million, albeit substantially lower than last year's £11.9 million. Although corporate finance activity generally is currently at a low ebb we believe that our strong focus on the mid market, our international reach and our reputation for independent advice will stand us in good stead when the market recovers.

Banking

Our banking division continued its good progress and profits grew substantially to £55.1 million from £40.9 million. This growth was virtually across the board with the loan book increasing to £1.4 billion from £1.2 billion. The climate for bad debts in our markets was benign and we reduced our charge to 1.5 per cent. (2001 — 1.7 per cent.) of our average loan book.

A particular high spot was our insurance premium financing activity which more than doubled its profits and which financed more than £1.3 billion of insurance premiums from 340,000 individual applications. Strong organic growth and the successful integration of the previous year's acquisition were boosted by the growth in our relatively new personal lines business. In addition the hardening of insurance premium rates increased the size of our average advance for commercial lines business and should continue to have a favourable impact during the next year.

Our property and asset finance businesses also made good progress. The UK property market has been strong and we continue to have a well-spread loan book both

geographically and by types of property. We have not relaxed our demanding security requirements. On our asset finance side we benefited from the continued development of our machine tool and healthcare businesses, from the revival in fortunes of the UK used car market and from the relative buoyancy of our chosen areas of the transport market. The printing machinery market, however, continued to be patchy due to overcapacity problems and softness in machine values.

Our armed forces business moved into modest profit and the challenge is now to develop it further. Our invoice finance and credit management businesses had another good year, as did our mortgage network activity, which processed more than 25,000 applications covering some £2.2 billion of mortgages.

During the year our treasury team was active and successful. We replenished and expanded our banking facilities in order to be ready for the further organic growth that we see ahead.

Provided that the UK economy does not slip into recession, the outlook for our banking division continues to be encouraging.

Market-Making

Despite a fall in the FT All-Share Index of some 23 per cent. over our financial year, WINS profits showed resilience. Whilst they fell by some 39 per cent., they showed a significant improvement from the low point in the second half of last year, as set out in the table below:

First half 2001	Second half 2001	First half 2002	Second half 2002
£25.9m	£1.5m	£9.6m	£7.2m

WINS traded profitably during every month in the period except September, producing a 33 per cent. pre-tax return on its capital, which in the circumstances was a commendable result.

The past year has seen continued development at WINS:

- the company moved to modern, open-plan offices, enabling more efficient working, and it up-graded the computer system;
- Bondscape, the joint venture with Barclays to provide a 'yellow strip' for UK gilt edged and other sterling fixed interest investments, has continued to develop and expand its connections;
- trading in NYSE and NASDAQ stocks commenced electronically on WINNER during the year; and
- trading in FTSE-100 SETS stocks commenced in December, 2001.

CHAIRMAN'S STATEMENT

In addition, we have taken on a specialist investment trust team which, from August, 2002, has been market-making as well as providing an integrated broking and advisory service in its sector.

During this period of relatively lower stock market volumes WINS has chosen to increase its market coverage substantially. Although the immediate outlook is unclear, when the market returns to more normal trading this broadening of our business base combined with our strength in electronic trading is expected to enhance our position.

DIRECTORS AND MANAGEMENT

As previously announced, Rod Kent will be stepping down as group managing director at the conclusion of our AGM on 31st October, 2002. We are delighted that he will continue as a non-executive director and consultant. Colin Keogh will become chief executive on 1st November, 2002 and Peter Winkworth and Stephen Hodges will be appointed managing directors at that time, continuing their respective duties as chief financial officer and head of banking. David Pusinelli, who is responsible for group development, joined the board on 26th September, 2002.

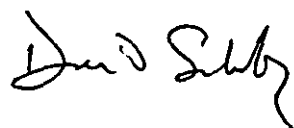
As we announced last year, Brian Winterflood retired from the board on 31st January, 2002, his 65th birthday. We are pleased that he is continuing as the non-executive chairman of WINS. Mike Hines, and David Macnamara as his alternate, the joint chief executives of WINS, were appointed to the board on 4th March, 2002. John Llewellyn-Lloyd, who was head of corporate finance, left the board on 31st December, 2001.

OUTLOOK

The financial year 2002 was a difficult one and, as we move into 2003, the short-term economic outlook remains neither clear nor particularly encouraging.

Whilst our banking division continues to grow, the current uncertainty of sentiment in markets means that growth in our other divisions would be hard won.

However, the harsher environment may well provide us with some good development opportunities and with our liquidity, which was recently augmented by a £55 million share placing, we will be well placed to take advantage of them. We remain confident in our strategy for the longer term; in the short term our stance remains one of continued caution.



Sir David Scholey
Chairman

TRIBUTE TO ROD KENT

In May 1974 Rod Kent, then aged 27, joined Close Brothers, a sub-subsiary of Consolidated Goldfields, and within a space of a few months became managing director. Although originally founded in 1878, Close Brothers was then a very small operation with a handful of employees, minimal business and just £1 million of capital.

A plan was conceived to develop a merchant bank aimed at serving up-and-coming smaller companies with growth potential. With the help of our late chairman Michael Morley, former banking director Peter Stone and current finance director Peter Winkworth, Rod steered the company through a management buy-out in 1979. For some 28 years Rod has led Close Brothers through a period of consistent expansion and growth into the significant merchant banking group that it is today, with 1,840 staff and £470 million of capital.

Rod's strategy, to build a range of distinct and diverse specialist activities, has enabled us to spread and balance our risk whilst developing strongly both organically and by acquisition. His philosophy of setting careful annual plans and budgets, delegating the running of each subsidiary to its management and strongly encouraging and supporting new ideas whilst constantly monitoring costs and margins, has enabled us to develop, retain and motivate a highly entrepreneurial team of operating directors and managers and has produced a compound annual growth rate of 20 per cent. over more than 20 years. His contribution to the group has been invaluable.

Having established a solid platform for the continued growth of the group, Rod retires from executive management with our deep gratitude and warm wishes. We hope that we will continue to enjoy the benefit of his judgement and advice, as a non-executive director and consultant, and that he will enjoy his wider range of interests and activities, for many years to come.



Close Brothers

REVIEW OF ACTIVITIES

FINANCIAL REVIEW

Overview

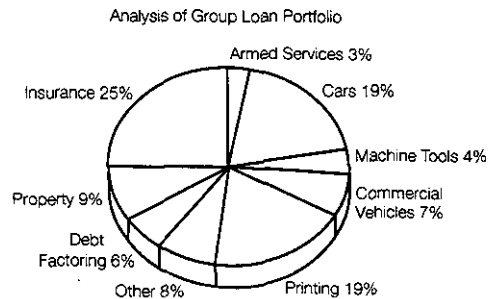
The mix of the group's operating income reflects the continued strong performance of the banking division, which generates the majority of the net interest income. Fee and dealing income were both slightly down as a proportion of the income mix.

	2000	2001	2002
	%	%	%
Net interest income	20	33	40
Net fee income	25	45	42
Net dealing income	53	20	17
Other income	2	2	1

We have continued to control costs, the largest element of which is staff costs. Our administrative expenses before exceptional costs fell by 1.6 per cent. whilst operating income fell by 5.6 per cent. Accordingly the expense/income ratio increased, by 2.5 percentage points, although this does not reflect the annualised benefit of cost reduction measures implemented during the year.

	2000	2001	2002
Operating income	£383m	£293m	£276m
Administrative expenses excluding exceptional costs	£210m	£174m	£171m
Administrative expenses as % of operating income	54.8%	59.4%	61.9%
Number of staff at year end	1,461	1,740	1,840

Staff numbers continued to increase mainly because of organic growth in our banking division, whose operating profits grew by 35 per cent. The increase was somewhat offset by reduced staff numbers in corporate finance.



Our loan book remains well spread, both by type of asset over which we take security and by number of loans. It represents some 300,000 separate advances, only nine of which exceed £3 million, the largest being £5.1 million.

Our customer deposits increased during the period by 7 per cent., whilst our customer loans and advances grew more rapidly by 19 per cent.

As in previous years our customer loans and advances remain able to be financed by capital and reserves and term facilities, which amounted to over £1.4 billion, of which £860 million was drawn at the year end. We continued our long established policy of broadly hedging interest rate exposure, whereby variable rate financing is swapped into fixed rate, particularly in regard to the asset finance book.

The group remains well capitalised and soundly financed. The consolidated risk asset ratio remains comfortably high at 26 per cent. (2001 — 22 per cent.).

Risk Management

Liquidity, credit, market and reputational risks are inherent in many of our businesses. Since each of our main operations is managed separately and there is little or no integration of systems, management or customers, risk management is carried out by the local management of each business. This is overseen on a regular basis by senior group management supported by an internal audit and compliance unit.

Each of our operations is responsible for its own liquidity within specified guidelines. Each is properly capitalised for its own business, normally comfortably above the regulatory minimum and, where necessary, has formal facilities from the group or external lenders. The liquidity of each operation is reviewed at its monthly board meeting and the overall position is reviewed by the group.

Credit risk is controlled by a number of local credit committees within centrally set limits of authority. For transactions above such limits, there is a group credit committee. In general terms, the group avoids the risk of multiple exposure to one counterparty. For example, we do not normally lend to a corporate finance advisory client, nor does one lending subsidiary seek to lend to clients of another lending subsidiary.

REVIEW OF ACTIVITIES

Market risk mainly relates to Winterflood Securities ("WINS"), our market-making subsidiary. We maintain real-time controls on the size and risk profile of the overall equity book and of individual books within this. There are also controls supplemented by cash limits on individual large and slow moving equities and gilts positions. The senior management of WINS is closely involved in this risk management process, which is also regularly monitored at group level. The group's exposures to market price risk resulting from the trading activities of WINS are shown in note 28.

Our asset management division has a range of controls to support the quality of the investment process, including asset allocation and investment committees, in which senior management of the group participate where appropriate. These are backed up by rigorous operational controls to safeguard clients' stock and money held for them.

Our corporate finance division involves reputational risk. This is controlled and monitored by either a new business committee or a risk committee, in which senior management of both corporate finance and the group participate. Underwriting risk is decided upon and monitored by a specific committee of the bank, which includes group directors who are not directly involved in corporate finance.

Our treasury operations do not actively trade in money market instruments, since these are normally bought and held to maturity. Nor do we trade speculatively in derivatives as a principal. Counterparties with whom we place deposits are approved and monitored by the treasury committee, which establishes specific limits.

We have minimal currency exposure, since almost all of our business is transacted in sterling. Non-sterling financing is funded by liabilities in the relevant currency or swapped into sterling to hedge currency exposure. Most of the group's activities are located in the British Isles. Since currency exposure resulting from our investment in overseas subsidiaries is currently relatively small, the extent to which the group's consolidated balance sheet is affected by movements in exchange rates is minimal.

As a financial institution, every transaction we undertake, either on behalf of our customers or for ourselves, involves financial instruments. We have described above our long standing policies to manage the risks inherent in these instruments.

The group's capital and reserves are necessarily subject to interest rate fluctuations and as a matter of policy these are not hedged as reflected in the interest rate repricing table shown in note 24.

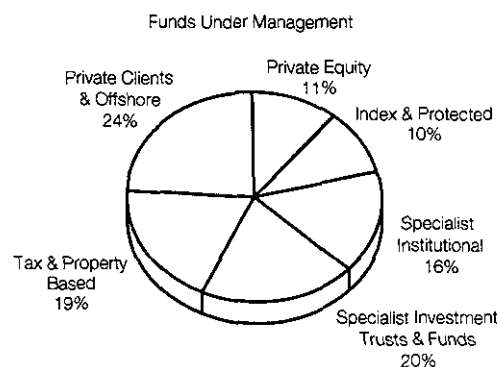
We have a central internal audit and compliance unit, as well as financial control and compliance functions at subsidiary level. Our central group control unit evaluates and examines the operational procedures of our separate businesses. The frequency of examination depends upon the perceived risk within each operation. Our central group control unit reports to the appropriate Audit Committee.

OPERATIONAL REVIEW

Asset Management

2002 has been a tough year for Close Investments, our asset management division. We have seen the market value of existing funds eroded, in some cases quite sharply, by falling equity markets. Against this uncertain background it has been difficult to raise new funds and, in the circumstances, we have done well to raise gross new funds of £788 million and net new funds of £417 million, just ahead of last year. Overall, our total funds under management at the end of the year of £3.1 billion remain unchanged from those at the beginning as the table below shows:

£bn	2001	2002
New funds raised	0.7	0.8
Withdrawals	(0.4)	(0.4)
Net funds raised	0.3	0.4
Market effect	(0.4)	(0.5)
Acquisition	0.6	0.1
Total at start of year	2.6	3.1
Total at end of year	3.1	3.1



The diverse and specialist nature of our business has to some extent enabled us to combat the inclement market conditions and there have been some bright spots — the successful creation of our latest private equity fund, the launch of two specialist investment trusts and the raising of over £150 million in specialist property investment products.



Close Brothers

REVIEW OF ACTIVITIES

Our specialist investment trust business has seen some marked falls in asset values in our technology, pharmaceutical and life sciences trusts. Although long term relative performance continues to be good, absolute returns have meant that we have not earned the performance fees that we enjoyed last year. Progress in raising new money for our open ended funds has been disappointing despite good relative performance.

Our specialist index and protected funds business had a solid year, including successfully raising over £75 million in two specialist closed end funds. Our protected funds, including our unique flagship 100 per cent. capital protected unit trust, the Close Escalator 100 Fund, have performed extremely well and generated good inflows as well as new distribution outlets. Our other funds have performed as expected.

OLIM, our specialist institutional business, had a successful year with good absolute and relative performance, boosted by a performance fee. It also won a number of mandates particularly from charities. The property side of this business had a strong year winning an important new specialist mandate from a large pension fund.

Our private equity business has enjoyed another successful year, particularly pleasing against the backdrop of the turmoil in quoted markets. It has closed its sixth fund above target, the investment of which is progressing well. It has also been a good year for successful exits. The focus on the UK mid market is proving a winning formula for this business.

Our specialist tax and property based investment business has held up well with good growth, particularly on the property side where we have developed a strong position in retail investment products.

Our private client businesses made progress and consistently attracted new funds to manage.

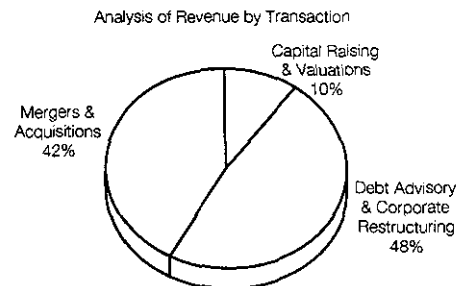
Our offshore businesses have, collectively, had a busy and challenging year contributing some 40 per cent. of divisional profits. In its first full year our Cayman Islands business did well and started a banking operation. Isle of Man had a steady year and our small Geneva business continues to make progress. Our Channel Islands businesses had a more difficult year with banking margins on cash management under some pressure as interest rates have fallen. During the year almost all our offshore businesses have moved into new premises and our Channel Islands and Isle of Man businesses have been investing heavily in new computer systems, all of which will be of long term benefit.

We are confident in our strategy of specialisation and diversification in Close Investments for the medium term, although we remain cautious in the short term.

Corporate Finance

This has been a turbulent and difficult year for the mergers and acquisitions market and our corporate finance business has suffered along with everybody else. Profits were substantially down from last year, particularly in the second half.

However, whilst the M&A side of our business and particularly the technology sector has been hard hit, our debt advisory and corporate restructuring groups have been busy. The former assisted in the raising and refinancing of over £3.3 billion of debt and the latter has worked on 22 restructurings during the year.



In order to align our cost base with current revenue levels we undertook a detailed review of our costs during the year. This led to some 40 (mainly voluntary) redundancies in the UK and, with other savings, a reduction in our overhead costs of some £6 million per annum. Following the departure of the previous chief executive, John Llewellyn-Lloyd, the division is now led by Richard Grainger.

Our French and German businesses have also found their market conditions testing. In contrast to the UK, however, our German business in particular has taken the opportunity to recruit much needed professional staff in the highly competitive Frankfurt market. We have also doubled our shareholding in Atlas Capital (Spain) to 20 per cent. since the year end and its name has been changed to Atlas Capital Close Brothers.

Towards the end of the year Houlihan Lokey, our US associate, decided to open a UK office concentrating on corporate restructuring. As a result we mutually agreed to a formal termination of our relationship although we continue to work together on a number of joint mandates.

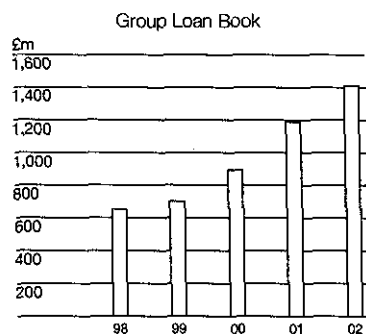
REVIEW OF ACTIVITIES

Against the background of the current lack of corporate finance activity we firmly believe that our strong mid market focus, our independent advice untainted by possible conflicts and our international network, together with our position in the debt advisory and corporate restructuring markets, will stand us in good stead when business picks up.

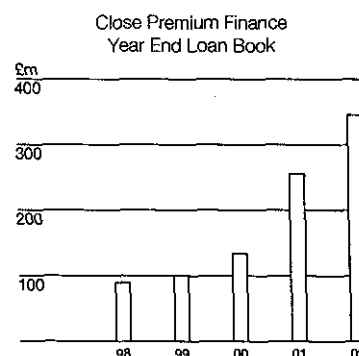
Banking

Our banking division is comprised of a number of specialist lending businesses together with our central treasury and funding operation. It produced another strong performance virtually across the board, with operating profits up by 35 per cent. to £55.1 million whilst the loan book, including securitised receivables, grew by 19 per cent. to £1.4 billion.

Margins and fee income continued to rise and net provisions made during the year fell as a percentage of the average loan book to 1.5 per cent. from 1.7 per cent. last year. The pre-tax return on income and opening net assets were 40 per cent. and 29 per cent. respectively. A pleasing aspect of the year was that the asset growth was largely organic with no acquisitions taking place, other than a small loan book which was acquired by our factoring business in January, 2002.



Close Premium Finance, which changed its name from Prompt in December, 2001, had another year of significant growth, with its contribution up by 115 per cent. During the year we financed 340,000 loans (2001 — 240,000) with a value of £1.3 billion (2001 — £1 billion). The increasing number of borrowers together with rising insurance premiums bodes well for the immediate future of this business. As well as a new name, we expanded into additional premises in Tolworth and continued our development in the personal lines market with the launch of a number of new products and initiatives. We continued to improve our technology, with more than 60 per cent. of proposals now being received electronically, and our systems are being further developed to assist with underwriting and data management.



Close Property Finance had a steady year. This long established business, which specialises in residential and commercial pre-let development finance, has a short term loan book which is well spread within the UK avoiding concentrations or large exposures, for example by way of property, customer or area. Whilst there is concern that some parts of the UK residential market may be overheating, our underwriting parameters remain conservative but still commercially attractive to our target market.

Close Asset Finance, comprising our UK commercial asset finance businesses, produced record profits during the year on the back of receivables which grew by 16 per cent. to £532 million from £457 million and which represented 38 per cent. of the group loan book. The diversification of assets financed continued, with non-print business now accounting for 50 per cent. of this loan book (2001 — 47 per cent.). This activity now covers the commercial vehicles and coaches, healthcare, engineering, machine tools, contractors' plant and light aircraft sectors. We faced recessionary conditions in the print and machine tools markets, but tight underwriting and our knowledge of second-hand markets held us in good stead. Our healthcare operations showed excellent growth and delivered a profit in only their second year with the group. Braemar Finance — aimed at dentists, veterinarians and opticians — made solid progress, and we financed a growing quantity of equipment for use by NHS trusts and private hospitals.

Close Consumer Finance had a good year in which we strengthened senior management and rationalised our branch network. Operating income grew significantly, as the consumer market for new and used vehicles continued to improve. Our strategy of concentrating on better quality business resulted in improved arrears and losses on repossessions were reduced. Our intention with this business is to improve our return on assets rather than to increase significantly our loan volumes. We have made good progress in this regard and believe that



Close Brothers

REVIEW OF ACTIVITIES

there are further efficiencies to be achieved. We will also be looking at extending our involvement in the motor cycle and light commercial vehicle markets.

Close Finance (CI) provides both commercial and consumer finance in Jersey and Guernsey and the results for its first full year under our ownership surpassed expectations. It has a strong market position and provides some geographic diversification for our growing loan book.

Close Brothers Military Services, which changed its name from Warrior in May, 2002, had a much improved year. We reaped the benefits of our re-organisation of the loan book as improved credit management processes enabled us to make this part of the business profitable for the first time since our acquisition. Our car sales and car finance businesses for the Armed Forces delivered improved performance.

Close Invoice Finance had an improved year despite a difficult environment for many of its clients. Market conditions for small and medium sized businesses have been challenging and there was a high level of insolvencies during the year. Nevertheless, with a first full year's contribution from Metropolitan Factors and the acquisition of a small loan book, our performance was satisfactory.

Close Credit Management produced another record year with its Close Assistance product, aimed at the motor finance market, making a significant contribution. We also launched a new activity, Credit Control Online, which provides credit management services on the internet and for which the initial level of trading has been as expected.

Mortgage Intelligence, our residential mortgage arranging business, had an exciting year and established itself as a leading participant in its market. Its network arranged some 25,000 mortgages with a value of £2.2 billion and it benefited from the strong market for mortgages both owner occupied and buy-to-let.

Our Treasury operation manages our customer deposit base as well as providing funding for our commercial loan book. Deposits grew by 7 per cent. to £1.2 billion and our team of business development managers was increased during the year. We diversified our sources of funding during the year with our first floating rate note issue, launched successfully in December 2001, and with an increase in our securitisation of insurance premium finance receivables to £175 million. We continue to be well capitalised with substantial undrawn committed funding available to finance the future growth of the loan book.

Market-Making

The twelve months to the end of July, 2002 were generally volatile for stock markets, and continued the long bear phase. Our year started in subdued fashion even prior to the shock of 11th September, 2001. The UK market then showed a small pick-up in late Autumn, but this was not sustained and markets broadly marked time until this Summer. With the accounting scandals in the USA and lack of significant economic progress on both sides of the Atlantic, markets fell sharply in June and have been depressed ever since.

In these circumstances, the private client has tended to be cautious and activity has been lower than in the heady days either side of the Millennium. Such conditions represented a challenging environment for our market-making division but the challenge was met head on with results being satisfactory in the circumstances. Although profits fell to £16.8 million, the working capital of the business also fell with the net equity (bull/bear) position down to £8.4 million from £23.8 million last year and from £42.3 million two years ago. Whilst lower than last year, the overall return on shareholders' funds (33 per cent.) and the net margin on operating income (36 per cent.) were satisfactory.

Notwithstanding the difficult conditions, WINS once again continued to broaden the scope of its activities. This development has included the further expansion of Bondscape with more clients connecting to the service and more stocks being covered. It has also encompassed the broadening of our international coverage, with the commencement of electronic trading in NYSE and NASDAQ stocks (Autumn 2001), and we have joined the LSE International Retail Service as a committed principal. With our new office space we were able to offer trading in FTSE-100 SETS stocks in December, 2001.

Since the year end we have launched a comprehensive service in the specialist investment trust sector, covering market-making, sales, research and corporate broking.

We now have the largest coverage of any retail service provider on the London Stock Exchange. All of this development has also meant that more than 80 per cent. of our equity trades are now handled by WINNER, our electronic automatic trading system.

The immediate outlook remains unclear and our new year has started quietly. However, the expansion and development of our business in recent years means that we will be well placed to move forward when more normal trading returns to our market-place.

REVIEW OF ACTIVITIES

OUTLOOK

The diversity of the group has provided some resilience in a difficult year. The growth of our banking division has somewhat offset the downturn in our other businesses which was caused by market factors.

The picture looking forward is somewhat similar. Stock markets remain subdued and this affects our asset management, corporate finance and market-making businesses, the immediate outlook for which therefore remains unclear. However, our banking division continues to grow and, provided the incidence of bad debt can be contained, the outlook for it remains encouraging.



R.D. Kent
Managing Director



C.D. Keogh
Chief Executive
designate



Close Brothers

REPORT OF THE DIRECTORS

The directors present their report and the audited financial statements for the year ended 31st July, 2002.

Principal Activities

Close Brothers Group plc is the parent company of a group of companies engaged in merchant banking operations. The principal subsidiary companies as at 31st July, 2002 and their principal activities are listed in note 29 to these financial statements. A detailed review of current and future developments is presented in the Review of Activities.

Results and Dividends

The consolidated results for the year are shown on page 23. The directors recommend a final dividend for 2002 of 17.0p (2001 — 17.0p) on each ordinary share which, together with the interim dividend of 9.0p (2001 — 9.0p), makes a total distribution for the year of 26.0p (2001 — 26.0p) per share.

Statement of Responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the group as at the end of the financial year and of the profit or loss of the group 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;
- state whether all applicable accounting standards have been followed; and
- 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 of the group and which enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for the system of internal control and for safeguarding the assets of the company and of the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Share Capital

Details of changes in the company's ordinary share capital during the year are given in note 20 to these financial statements.

Substantial Interests

At 3rd September, 2002 the following had notified the company that they were interested in 3 per cent. or more of the issued share capital of the company:

	Ordinary shares	%
Caledonia Investments plc	25,400,000	17.68
Prudential plc	11,585,931	8.06
Lloyds TSB Group plc	5,490,025	3.82
The Standard Life Assurance Company	4,658,831	3.24

Directors and Interests

(a) The present members of the board, all of whom served throughout the year except Mr. M.A. Hines and his alternate Mr. D.J. Macnamara, and Mr. D.C. Pusinelli who were appointed respectively on 4th March, 2002 and 26th September, 2002, are set out on page 3.

Mr. E.J. Llewellyn-Lloyd and Mr. B.M. Winterflood left the board respectively on 31st December, 2001 and 31st January, 2002.

(b) The directors' interests in the share capital of the company are shown below:

	Ordinary shares	
	31st July, 2002*	1st August, 2001
P.N. Buckley**	—	—
A.H. Farley	9,800	9,800
D.G. Hardisty	14,157	10,555
M.A. Hines	18,599	17,559
S.R. Hodges	374,586	332,188
R.D. Kent	223,192	419,590
C.D. Keogh	309,512	303,107
D.J. Macnamara (alternate)	25,772	24,732
M.G.A. McLintock***	4,440	—
D.C. Pusinelli	219,468	220,507
Sir David Scholey	10,000	10,000
P.S. Wilmot-Sitwell	10,000	10,000
P.L. Winkworth	628,187	627,147
M.G. Wyatt** (alternate)	—	—

*or at date of appointment if later.

**Mr. P.N. Buckley, and his alternate Mr. M.G. Wyatt, are respectively the chairman and a non-executive director of Caledonia Investments plc, which has an interest in 25,400,000 ordinary shares of the company at 31st July, 2002 (1st August, 2001 — 25,400,000).

***Mr. M.G.A. McLintock is a director of Prudential plc which has an interest in 11,585,931 ordinary shares of the company at 31st July, 2002 (1st August, 2001 — 11,735,000).

Details of the options to subscribe for shares held by the directors under the company's sharesave and executive share option schemes are given in note 3 to these financial statements. The beneficial interests of the directors in the share capital of the company have remained unchanged since 31st July, 2002.

(c) Mr. M.A. Hines is a director and minority shareholder in Winterflood Securities Limited. At 31st July, 2002 he and his spouse were beneficially interested in 1,250 ordinary shares of that company (date of appointment — 1,250).

(d) In accordance with the provisions of the Articles of Association, Mr. A.H. Farley, Mr. R.D. Kent, Mr. C.D. Keogh and Sir David Scholey, who were appointed in September 1993,

REPORT OF THE DIRECTORS

August 1984, August 1995 and March 1999 respectively, retire by rotation and, being eligible, offer themselves for re-election. Mr. A.H. Farley and Sir David Scholey are non-executive directors who do not have a service contract. Mr. C.D. Keogh has a service contract which can be terminated on not more than twelve months' notice. Mr. R.D. Kent also has a service contract which can be terminated on not more than twelve months' notice. Following the Annual General Meeting it is intended that he will become a non-executive director and consultant whereupon he will no longer have a service contract, in line with all non-executive directors of the company. As a consultant he will have a consultancy agreement which can be terminated on not more than six months' notice.

Mr. M.A. Hines and Mr. D.C. Pusinelli, having been elected since the last Annual General Meeting, retire in accordance with the Articles of Association and being eligible offer themselves for re-election. Mr. M.A. Hines and Mr. D.C. Pusinelli are executive directors each of whom has a contract which can be terminated on not more than respectively twenty four and twelve months' notice.

(e) The company has established an employee benefit trust in which all employees of the group, including executive directors, are potential beneficiaries. The trust currently owns 1,245,797 shares in the company, 271,926 of which are conditionally earmarked for deferred bonuses. This trust acquired these shares at an average cost of 384p per share compared to a market value of 452.5p per share at 31st July, 2002. Dividends have been waived on these shares.

Corporate Social Responsibility

(a) The Environment

The group's environmental policy has recently been published on its website. The chief executive designate is responsible for implementing this policy, supported by a management system with clear roles and responsibilities. The group has collected data on its significant environmental impacts in order to set targets which will be regularly monitored. The group has started to implement processes to manage environmental risks so as to lower its greenhouse gas emissions and reduce, reuse and recycle, wherever possible, waste materials. Dialogue with, and support from, Business in the Environment, to whom the group subscribes, is expected to assist the group in improving its environmental performance, which is a key aim of the policy.

(b) Community Support and Charitable Contributions

In August 2002 the company made a charitable investment of £250,000 in BOOST, which is a Government backed project which has as one

of its objectives, generating employment in the most deprived areas of East London.

Contributions made during the year for charitable purposes amounted to £127,000 (2001 — £101,000).

(c) Health and Safety

The maintenance of healthy and safe working conditions is a group objective. Group companies have established procedures appropriate to their particular activities to monitor, maintain and improve their health and safety standards. Often health and safety committees are established, with staff representatives, to provide training and improve the working environment.

(d) Staff

Group companies are encouraged to develop their own consultative policies. These include regular meetings held between local management and employees to allow a free flow of information and ideas and to discuss decisions likely to affect their interests. Employees participate directly in the success of the business through the group's profit sharing scheme and savings related share option scheme.

It is the group's policy to give appropriate consideration to applications for employment from disabled persons, having regard to their particular aptitudes. For the purposes of training, career development and promotion, disabled staff, including any who become disabled in the course of their employment, are treated on equal terms with other employees.

(e) Suppliers' Payments Policy

All banking, market-making and investment transactions are settled in accordance with applicable terms and conditions of business agreed with the counterparty. Average creditor days for all other approved expenses is 23 (2001 — 28).

Special business at the Annual General Meeting

(a) Authority to purchase own shares

At the last Annual General Meeting the company was given authority to make market purchases of up to approximately 15 per cent. of its issued share capital. This authority, which will expire at the conclusion of the Annual General Meeting, has not been used by the directors.

Nevertheless your board considers it would be appropriate to renew the authority. Share purchases would only be made where the directors believed that they were in the best interests of the company and they would enhance earnings per share, taking into account other available investment opportunities and the overall financial position of the group. Accordingly, a special resolution will be proposed at the Annual General Meeting to authorise the company to purchase not more



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REPORT OF THE DIRECTORS

than 21,551,000 of its 25p ordinary shares, being approximately 15 per cent. of the issued share capital of the company.

The maximum price which may be paid will not be more than 5 per cent. above the average of the middle market quotations for the ordinary shares as derived from the London Stock Exchange Daily Official List for the five business days before the purchase is made. The minimum price will be the par value. The directors would only begin to purchase shares after considering the criteria referred to above.

The authority will expire on whichever date is the earlier of the date eighteen months from the date the special resolution is passed and the date of the 2003 Annual General Meeting. Details of shares purchased pursuant to the authority will be notified to the London Stock Exchange and to the Registrar of Companies and will be disclosed in the 2003 Annual Report.

(b) Directors' authority to allot shares

A resolution will be proposed at the Annual General Meeting to grant the directors authority to allot unissued shares of the company up to a nominal amount of £11,973,000 which represents approximately one third of the issued share capital. Other than in respect of options in issue, the directors do not have any present intention to allot unissued shares pursuant to this authority. The authority, if granted, will last for a period of five years from the date of passing of the resolution.

(c) Waiver of pre-emption rights

It is proposed to renew, until the next Annual General Meeting, the directors' flexibility to issue shares for cash other than strictly pro rata to existing shareholders. This authority will be limited to a nominal amount of £897,000 which represents approximately 2½ per cent. of the issued share capital. The directors intend to comply with the guidelines of the investment committees of the Association of British Insurers and the National Association of Pension Funds to the effect that no more than 7½ per cent. of the issued share capital should be allotted for cash on a non pre-emptive basis in any rolling three year period.

(d) Save As You Earn

The Close Brothers Group plc Sharesave Scheme (the "Sharesave Scheme") was approved by shareholders in 1993, and attracts favourable tax treatment as an Inland Revenue approved scheme. Under the Sharesave Scheme, the directors may grant eligible employees an option to acquire ordinary shares in the company at a price determined at the date of grant, which may be at a discount of up to 20 per cent. from the share price at the time. The exercise price of the option is financed by monthly contributions to a

designated saving account for a three or five year period. The directors believe that the company has benefited from giving employees at all levels the opportunity to acquire shares under the Sharesave Scheme. Since the Sharesave Scheme is due to expire in 2003, it is proposed to seek the approval of shareholders for a replacement scheme which will also be capable of approval by the Inland Revenue.

(e) Share Incentive Plan ("SIP")

The company has for many years operated an Inland Revenue approved profit sharing scheme under which employees have been able to share in the success of the business through the award of shares on tax-favoured terms. The directors believe that the company has benefited from giving all employees the opportunity to receive share awards under the scheme. As a result of recent legislation, the company will not be able to make allocations under the profit sharing scheme after this year.

In order to operate a comparable alternative scheme, it is proposed to seek the approval of shareholders for the SIP. The SIP contains a number of elements which the company may operate in a particular year. The SIP allows the company to award free shares to participants which, when held in trust for five years, attract similar tax advantages to those which applied to shares acquired under profit sharing scheme allocations. In addition, the SIP allows the company to make an offer of "partnership shares", under which employees may purchase up to £1,500 worth of shares per year using pre-tax salary. When partnership shares are offered under the SIP, the company may also award "matching shares". If awarded, matching shares are provided in a ratio of up to a maximum of two matching shares for each partnership share purchased. The SIP allows the company to award free and matching shares on the basis that matching shares will be subject to forfeiture if a participant leaves employment with the group within a period of up to three years from the date of the relevant award.

Auditors

Deloitte & Touche have expressed their willingness to continue in office as auditors and a resolution to re-appoint them will be proposed at the Annual General Meeting.

By order of the board
R.D. Sellers
Secretary
26th September, 2002

CORPORATE GOVERNANCE

The board has reviewed its Corporate Governance practices and, together with relevant information contained in the Report of the Board on Directors' Remuneration on pages 19 to 21 and the Report of the Directors on pages 14 to 16, this statement explains how Close Brothers Group plc has applied the principles of good governance contained in Section 1 of the Combined Code for the year ended 31st July, 2002.

Board Responsibilities

The board currently comprises seven executive directors and five non-executive directors. The senior independent director is Mr. P.S. Wilmot-Sitwell. Mr. P.N. Buckley is a director of Caledonia Investments plc, which owns 18 per cent. of the issued share capital of the company, Mr. M.G.A. McLintock is a director of Prudential plc, which owns 8 per cent. of the issued share capital of the company, Mr. A.H. Farley has been a non-executive director of the company for just over nine years and Sir David Scholey is a senior adviser to UBS Warburg, which is financial adviser and stockbroker to the company. All the non-executive directors are regarded by the board as independent.

The board is supplied in a timely manner with information in a form and of a quality appropriate to enable it to discharge its duties and meets regularly throughout the year (normally monthly) to deal with important aspects of the group's affairs, including setting and monitoring strategy, reviewing performance, ensuring adequate financial resources and reporting to shareholders. The chairman is responsible for the running of the board and the managing director is responsible for the running of the company's business which ensures a clear division of responsibility at the head of the company. All directors have direct access to the advice and services of the company secretary and outside professional advisers as necessary.

The board has appointed the following committees with the following memberships and terms of reference:

Bank Audit Committee (Mr. A.H. Farley (chairman), Mr. P.N. Buckley and Mr. P.S. Wilmot-Sitwell (non-executive directors)).

In respect of Close Brothers Limited and its subsidiaries, ("the Bank Activities"), to review the scope and findings of the internal and external auditors, to commission any additional investigation work, to review the adequacy of controls and procedures including reputational, financial, operational and compliance controls and risk management and to consider the form and content of published announcements and statutory accounts.

Non-Bank Audit Committee (Mr. A.H. Farley (chairman), Mr. P.N. Buckley and Mr. M.G.A. McLintock (non-executive directors)).

In respect of all activities of the group other than the Bank Activities, to review the scope and findings of the internal and external auditors, to commission any additional investigation work, to review the adequacy of controls and procedures including reputational, financial, operational and compliance controls and risk management and to consider the form and content of published announcements and statutory accounts.

Remuneration Committee (Mr. P.S. Wilmot-Sitwell (chairman), Mr. P.N. Buckley and Sir David Scholey (non-executive directors)).

To recommend for determination by the non-executive directors, the remuneration of the executive directors and the senior executives of the group.

Nomination Committee (Sir David Scholey (chairman), Mr. P.N. Buckley and Mr. P.S. Wilmot-Sitwell (non-executive directors) and Mr. R.D. Kent (an executive director)).

To consider the appointment or retirement of directors, to review proposed nominations and make recommendations thereon to the board.

Internal Control

The board has overall responsibility for the group's system of internal control and for reviewing its effectiveness. The system of internal control is designed to ensure that the reputational, financial, operational and compliance risks taken by the holding company and its operating subsidiaries in the conduct of their business are identified and evaluated so that appropriate controls are put in place to manage those risks. Such systems are designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, but not absolute, assurance against material misstatement or loss.



Close Brothers

CORPORATE GOVERNANCE

The system of internal control is supported by a well established organisational structure within the group, with clear levels of responsibility and delegation of authority and a strong control culture embedded in the day to day management of each operating company. Each operating company in the group regularly undertakes a review of, and reports to its board on, these controls and procedures, having due regard to its key risks. Where necessary, steps are taken to improve internal control and risk management further following these reviews. The Financial Review Statement on pages 8 and 9 details these key risks and explains how such risks are controlled.

Group control, which is the central internal audit and compliance unit, regularly reviews the effectiveness of controls and procedures established in each company to manage key risks. The head of group control reports through the audit committees to the board, to which he has unrestricted access through the chairman.

The company has complied with the Turnbull Committee's guidance for directors. Identifying, evaluating and managing the group's significant risks is an ongoing process which is regularly reviewed by the board, and which has been in place for the year ended 31st July, 2002 and up to the date of the approval of these financial statements.

Auditors' Independence

The group has employed two firms of auditors for many years. Ernst & Young are the auditors of Close Brothers Limited, our principal banking subsidiary, and its subsidiaries. Deloitte & Touche are the auditors of the holding company and the remainder of the group.

In addition to their statutory audit responsibilities, the group typically uses the auditors for other work that they are well placed to undertake in that role. This includes formalities relating to borrowings, shareholder and other circulars; regulatory, pension scheme and other ancillary audit work; work in respect of acquisitions and disposals; and tax compliance.

Several firms are considered for other work, including the auditors in some instances. In such cases due consideration is given to the impact of the assignment on the independence of the auditors and to their qualifications to carry out the role, including competitive tenders for larger assignments.

Having given consideration to the extra work undertaken by the auditors, and after careful discussion with the responsible partners in the two firms and the executive directors, the audit committees are satisfied as to the independence of the statutory auditors.

Relations with Shareholders

The group has a programme of communication with shareholders through the regular interim and annual reports and the Annual General Meeting. Shareholders are given the opportunity to participate by asking questions at the Annual General Meeting, or by submitting written questions in advance. The group's website at www.closebrothers.co.uk contains information on the group and the products and services it offers. Communication with the group's largest institutional shareholders is undertaken by a regular programme of visits and presentations.

Going Concern

The financial statements are prepared on a going concern basis as the directors are satisfied that, at the time of approving the financial statements, the group has the resources to continue in business for the foreseeable future.

Compliance with the Combined Code

The company has complied with Section 1 of the Combined Code throughout the year ended 31st July, 2002.

REPORT OF THE BOARD ON DIRECTORS' REMUNERATION

Constitution of the Remuneration Committee

The Remuneration Committee, which was established by the board in 1993, recommends for determination by the non-executive directors, the remuneration and other terms and conditions of employment of the executive directors and the senior executives of the group.

The chairman of the Committee is Mr. P.S. Wilmot-Sitwell. Other members are Mr. P.N. Buckley and Sir David Scholey, both non-executive directors. The group managing director, Mr. R.D. Kent, and chief executive designate, Mr. C.D. Keogh, attend meetings on invitation.

Policy on senior executive remuneration

General principles

The Committee aims to ensure that the senior executive remuneration arrangements are fair and competitive within the financial sector and that they will enable the group to retain, motivate and attract key personnel.

Advice is taken from external consultants on comparative data and other relevant aspects of compensation of senior group executives.

In determining directors' remuneration consideration has been given to matters specific to the company such as the sector it operates within, and its performance measured against its peers in that sector. Other considerations are the experience and performance of individual directors, their areas of responsibility and salary levels throughout the group.

Main components

Basic salary

Basic salaries are reviewed annually, having regard to individual responsibilities and performance and also to comparative information.

Annual discretionary performance related awards

Annual performance related awards are at the discretion of the Committee. In some instances they are based upon a profit sharing pool in an individual operating company but for most executive directors they are determined in the light of the individual's performance and contribution to the profitability of their operating company or function, as appropriate, and of the profitability of the group, both overall and in relation to its competitors.

Benefits

The group provides senior management with healthcare, prolonged disability and life assurance cover. It also provides a company car or payment in lieu.

Long-term incentives

The group has for several years operated a number of long-term incentive arrangements. These include the 1995 Executive Share Option Scheme, which replaced the 1985 Executive Share Option Scheme, under which grants of performance-related options are made over a number of years; Inland Revenue approved Savings Related Share Option and Profit Sharing Schemes; and local minority interests in operating subsidiaries.

Details of directors' share options are shown in note 3.

Pensions

Messrs. M.A. Hines and his alternate Mr. D.J. Macnamara, R.D. Kent and P.L. Winkworth participated in defined contribution schemes. Messrs. D.G. Hardisty, S.R. Hodges and C.D. Keogh participated in a defined benefits scheme, under which the normal pensionable age is 65, the pension at normal pensionable age is two-thirds of final pensionable salary subject to completion of 30 years' service and there is a widow's pension on death. The table on page 21 summarises accrued pensions for directors who participated in the defined benefits scheme.

Directors' service contracts

Executive directors' service contracts are terminable on no more than twelve months' notice except for Mr. M.A. Hines, whose contract is terminable upon twenty-four months' notice. Non-executive directors do not have service contracts but are engaged under a letter of appointment for terms not exceeding three years and renewable by mutual agreement.



Close Brothers

REPORT OF THE BOARD ON DIRECTORS' REMUNERATION

Non-executive directors

Fees of all non-executive directors are set by the board in accordance with the Articles of Association (without the participation of the non-executive directors themselves).

External appointments

All fees earned by executive directors in respect of non-executive directorships are taken into account in determining their remuneration.

Directors' remuneration

The following table shows a breakdown of the remuneration of individual directors for the year ended 31st July, 2002:

	Salaries and fees £'000	Benefits £'000	Performance related awards in respect of the current year		Compensation for loss of office £'000	Total £'000	Company pension contributions £'000
			Current £'000	Deferred £'000			
Executive:							
D.G. Hardisty	277	15	225	—	—	517	69
M.A. Hines	75	8	150	—	—	233	31
S.R. Hodges	277	14	500	—	—	791	69
R.D. Kent	387	17	375	—	—	779	91
C.D. Keogh	277	17	450	—	—	744	69
E.J. Llewellyn-Lloyd	100	6	—	—	389	495	10
D.J. Macnamara (alt.)	75	9	150	—	—	234	20
P.L. Winkworth	350	16	375	—	—	741	82
B.M. Winterflood	80	10	225	—	—	315	22
Non-executive:							
P.N. Buckley	35	—	—	—	—	35	—
A.H. Farley	35	—	—	—	—	35	—
M.G.A. McLintock	35	—	—	—	—	35	—
Sir David Scholey	125	—	—	—	—	125	—
P.S. Wilmot-Sitwell	35	—	—	—	—	35	—
	<u>2,163</u>	<u>112</u>	<u>2,450</u>	<u>—</u>	<u>389</u>	<u>5,114</u>	<u>463</u>

The following table shows a breakdown of the remuneration of individual directors for the year ended 31st July, 2001:

	Salaries and fees £'000	Benefits £'000	Performance related awards in respect of the current year		Compensation for loss of office £'000	Total £'000	Company pension contributions £'000
			Current £'000	Deferred £'000			
Executive:							
D.G. Hardisty	265	14	225	—	—	504	66
S.R. Hodges	265	13	398	103	—	779	66
R.D. Kent	370	12	555	245	—	1,182	87
C.D. Keogh	265	19	398	103	—	785	66
E.J. Llewellyn-Lloyd	230	12	345	155	—	742	23
P.L. Winkworth	335	15	503	198	—	1,051	78
B.M. Winterflood	265	21	440	—	—	726	72
Non-executive:							
P.N. Buckley	27	—	—	—	—	27	—
Lord Cobbold	7	—	—	—	—	7	—
A.H. Farley	27	—	—	—	—	27	—
M.G.A. McLintock	5	—	—	—	—	5	—
Sir David Scholey	125	—	—	—	—	125	—
P.S. Wilmot-Sitwell	27	—	—	—	—	27	—
	<u>2,213</u>	<u>106</u>	<u>2,864</u>	<u>804</u>	<u>—</u>	<u>5,987</u>	<u>458</u>

Mr. M.G. Wyatt, alternate non-executive director for Mr. P.N. Buckley, did not receive any remuneration from the group.

Performance related awards in respect of the current year include allocations under an Inland Revenue approved profit sharing scheme and amounts awarded by the Remuneration Committee on a discretionary basis.

REPORT OF THE BOARD ON DIRECTORS' REMUNERATION

Messrs. D.G. Hardisty, S.R. Hodges, C.D. Keogh and P.L. Winkworth have the right to call for respectively 21,459, 35,463, 21,887 and 40,000 shares in the company from the employee benefit trust, at nil cost, at any time, at their option, between varying dates from 1st August, 2000 to 1st August, 2008. These represent performance related awards in respect of earlier years deferred bonuses, which have previously been disclosed in the accounts of those years and for which provisions have been made.

Directors' pension entitlements

The following table summarises pension benefits for all directors who participated in a defined benefit scheme. The accrued pension is that which would be paid annually on retirement based on service to the end of the year. The increase in accrued pension during the year excludes any increase for inflation. The transfer value has been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GNII less directors' contributions. Participants of the defined benefit scheme have the option of paying Additional Voluntary Contributions; neither such contributions nor the resulting benefits are included in the table below:

	Accrued annual pension at 31st July, 2002 £'000	Increase in accrued annual pension in the year £'000	Transfer value of increase in accrued annual pension £'000
D.G. Hardisty	82	10	56
S.R. Hodges	91	10	24
C.D. Keogh	91	10	25

The transfer values disclosed above do not represent a sum paid or payable to the individual director. Instead they represent potential liabilities of the pension scheme.



Close Brothers

REPORT OF THE AUDITORS

Independent Auditors' Report to the Members of Close Brothers Group plc

We have audited the financial statements of Close Brothers Group plc for the year ended 31st July, 2002 which comprise the profit and loss account, the balance sheets, the cash flow statement, the statement of total recognised gains and losses and the related notes 1 to 37. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of directors and auditors

As described in the Statement of Responsibilities, the company's directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibility is to audit the financial statements in accordance with relevant United Kingdom legal and regulatory requirements, auditing standards, and The Listing Rules of the Financial Services Authority ("The Listing Rules").

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or The Listing Rules regarding directors' remuneration and transactions with the company and other members of the group is not disclosed.

We review whether the corporate governance statement reflects the company's compliance with the seven provisions of the Combined Code specified for our review by The Listing Rules and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the group's corporate governance procedures or its risk and control procedures.

We read the Report of the Directors and other information contained in the Annual Report for the above year and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom 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 circumstances of the company and of the group, consistently applied and adequately disclosed.

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

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company and of the group as at 31st July, 2002 and of the profit of the group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche Deloitte & Touche

Deloitte & Touche
Chartered Accountants
and Registered Auditors
London

26th September, 2002

CONSOLIDATED PROFIT AND LOSS ACCOUNT

	Note	For the year ended 31st July, 2002			Year ended
		Ordinary activities before exceptional costs and goodwill amortisation	Exceptional costs and goodwill amortisation	Total ordinary activities	31st July, 2001
		£'000	£'000	£'000	£'000
Interest receivable		198,890	—	198,890	208,982
Interest payable		(88,449)	—	(88,449)	(112,598)
Net interest income		110,441	—	110,441	96,384
Dividend income		64	—	64	153
Fees and commissions receivable		140,795	—	140,795	153,753
Fees and commissions payable		(24,740)	—	(24,740)	(21,542)
Net dealing income — market-making		48,365	—	48,365	58,331
Other operating income		1,429	—	1,429	5,600
Other income		165,913	—	165,913	196,295
Operating income		276,354	—	276,354	292,679
Administrative expenses	2	170,937	3,446	174,383	173,732
Depreciation	12	7,614	—	7,614	6,861
Provisions for bad and doubtful debts	9	19,256	—	19,256	17,919
Amortisation of goodwill	29	—	6,681	6,681	4,671
Total operating expenses		197,807	10,127	207,934	203,183
Operating profit on ordinary activities before taxation	5	78,547	(10,127)	68,420	89,496
Taxation on profit on ordinary activities	6	22,855	(1,016)	21,839	28,639
Profit on ordinary activities after taxation		55,692	(9,111)	46,581	60,857
Minority interests — equity		2,252	—	2,252	1,754
Profit attributable to shareholders		53,440	(9,111)	44,329	59,103
Dividends:					
Interim dividend 9.0p per share (2001 — 9.0p)				12,195	12,121
Proposed final dividend 17.0p per share (2001 — 17.0p)				24,214	22,927
Total dividends 26.0p per share (2001 — 26.0p)				36,409	35,048
Retained profit for the year	21			7,920	24,055
Earnings per share before exceptional costs and amortisation of goodwill				38.9p	47.4p
Earnings per share on profit attributable to shareholders	34			32.3p	44.0p
Diluted earnings per share	34			32.0p	43.6p

All income and profits are in respect of continuing operations.



Close Brothers

CONSOLIDATED BALANCE SHEET

At 31st July, 2002

	Note	2002 £'000	2001 £'000
Assets			
Cash and balances at central banks		671	586
Loans and advances to banks	7	443,175	593,894
Loans and advances to customers		1,410,998	1,189,405
Non-recourse borrowings	8	(175,000)	(33,000)
	8	1,235,998	1,156,405
Debt securities — long positions	10	64,352	35,764
Debt securities — other	10	712,380	481,936
Settlement accounts		246,456	147,750
Equity shares — long positions	11	15,971	33,413
Equity shares — investments	11	28,484	27,529
Intangible fixed assets — goodwill	29	113,065	114,080
Tangible fixed assets	12	24,667	20,468
Share of gross assets of joint ventures		14,331	3,103
Share of gross liabilities of joint ventures		(13,905)	(2,675)
		426	428
Other assets	17	134,684	119,060
Deferred taxation	18	10,345	11,507
Prepayments and accrued income		22,956	23,863
Total assets		3,053,630	2,766,683
Liabilities			
Deposits by banks	13	83,159	55,643
Customer accounts	14	1,222,541	1,144,155
Bank loans and overdrafts	15	505,655	607,629
Debt securities — loan notes issued	16	100,000	18,140
Debt securities — short positions		52,231	38,182
Settlement accounts		202,343	114,174
Equity shares — short positions		7,589	9,594
Other liabilities	17	228,068	197,372
Accruals and deferred income		77,105	71,910
Subordinated loan capital	19	96,937	96,937
Minority interests — equity		6,079	5,056
		2,581,707	2,358,792
Shareholders' funds			
Called up share capital	20	35,920	34,055
Share premium account	21	248,456	193,253
Profit and loss account	21	187,547	180,583
Total equity shareholders' funds		471,923	407,891
Total liabilities and shareholders' funds		3,053,630	2,766,683
Memorandum items			
Contingent liabilities — guarantees	22	2,412	3,555
Commitments — other	23	166,512	138,903

Approved by the Board of Directors on 26th September, 2002

Sir David Scholey	} Directors
R.D. Kent	
P.L. Winkworth	

COMPANY BALANCE SHEET

At 31st July, 2002

	Note	2002 £'000	2001 £'000
Fixed assets			
Tangible fixed assets	12	4,055	4,499
Investments in subsidiaries	29	323,997	319,059
Equity shares	11	4,969	5,386
		<u>333,021</u>	<u>328,944</u>
Current assets			
Debtors	30	100,631	70,527
Other assets		191	246
		<u>100,822</u>	<u>70,773</u>
Creditors: Amounts falling due within one year	31	59,766	71,841
Net current assets/(liabilities)		<u>41,056</u>	<u>(1,068)</u>
Total assets less current liabilities		<u>374,077</u>	<u>327,876</u>
Creditors: Amounts falling due after more than one year	32	27,072	27,072
Net assets		<u>347,005</u>	<u>300,804</u>
Capital and reserves			
Share capital	20	35,920	34,055
Share premium account	21	248,456	193,253
Profit and loss account	21	62,629	73,496
Total equity shareholders' funds		<u>347,005</u>	<u>300,804</u>

Approved by the Board of Directors on 26th September, 2002

Sir David Scholey

R.D. Kent

P.L. Winkworth

} Directors

David Scholey
R.D. Kent
P.L. Winkworth



Close Brothers

CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

For the year ended 31st July, 2002	2002	2001
	£'000	£'000
Profit attributable to shareholders	44,329	59,103
Exchange adjustment	(978)	13
Total recognised gains and losses related to the year	43,351	59,116
Prior period deferred taxation adjustment due to adopting FRS 19		3,517
Total gains and losses recognised since the last annual report		62,633

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31st July, 2002	Note	2002	2001
		£'000	£'000
Net cash (outflow)/inflow from operating activities	35(a)	(29,611)	243,901
Returns on investments and servicing of finance:			
Interest paid on subordinated loan capital		(7,825)	(5,838)
Dividends paid to minorities		(178)	(1,703)
		<u>(8,003)</u>	<u>(7,541)</u>
Taxation:			
Taxation paid		(25,586)	(47,608)
Capital expenditure and financial investment:			
Purchase of tangible fixed assets		(14,396)	(8,243)
Sale of tangible fixed assets		2,416	2,073
Purchase of equity shares held for investment		(5,173)	(14,885)
Sale of equity shares held for investment		2,647	5,655
		<u>(14,506)</u>	<u>(15,400)</u>
Acquisitions and disposals:			
Minority interests acquired for cash		(1,194)	(22,537)
Purchase of subsidiaries	35(b)	(6,685)	(64,424)
		<u>(7,879)</u>	<u>(86,961)</u>
Equity dividends paid		(35,122)	(34,818)
Net cash (outflow)/inflow before financing		(120,707)	51,573
Financing:			
Issue of ordinary share capital including premium	35(c)	57,068	2,455
Issue of subordinated loan capital	35(c)	—	45,000
(Decrease)/increase in cash	35(d)	(63,639)	99,028

In the directors' view, cash is an integral part of the operating activities of the group, since it is a bank's stock in trade. Nevertheless, as required by Financial Reporting Standard No. 1 (Revised), cash is not treated as cash flow from operating activities but is required to be shown separately in accordance with the format above.

THE NOTES

1. Accounting policies

(a) Format of financial statements

The group financial statements are prepared in accordance with the special provisions of Part VII of the Companies Act 1985 relating to banking groups and those of the company in accordance with section 226 of, and Schedule 4 to, the Companies Act 1985. The financial statements are prepared in accordance with applicable accounting standards.

(b) Accounting convention

The financial statements have been prepared under the historical cost convention, modified by the revaluation of equity shares and debt securities.

(c) Fees and commissions receivable

Fee and commission income is taken to the profit and loss account when invoiced except for fees from certain monitoring and administration services and investment management fees which accrue to the profit and loss account on a day to day basis irrespective of when they are invoiced.

(d) Net dealing income

Net dealing income includes the net profit arising from both buying and selling securities and from positions held in securities.

(e) Loans and advances to customers

Loans and advances are stated net of provisions against doubtful debts which are made on the basis of regular review by management. The provision raised is an estimate of the amount needed to reduce the carrying value of the asset to its expected net realisable value and takes into account management's assessment of a combination of factors including each portfolio structure, characteristics of individual cases, past and expected credit losses and business and economic conditions.

(f) Finance leases, operating leases and instalment finance

Finance leases are recognised as loans at the minimum lease payments receivable less finance charges.

Finance charges on both hire purchase obligations and leases are taken to income in proportion to the net funds invested after deducting, where applicable, a fixed percentage in respect of set-up costs.

Rental costs under operating leases are charged to the profit and loss account in equal annual amounts over the period of the leases.

(g) Equity shares and debt securities

The long and short positions in equity shares and debt securities held for trading purposes represent the aggregate of trading positions in individual securities arising respectively from a net bought and net sold position. They are valued at the dealers' bid and offer prices respectively at the close of business on the balance sheet date.

Debt securities held for liquidity and investment purposes are included in the balance sheet at cost, net of provision for any material decline in market value. Equity shares held for investment purposes are included in the balance sheet at middle market values if listed and at directors' valuation if unlisted.

Equity shares held by the employee share benefit trust are shown at cost, and realised surpluses and losses are taken to the profit and loss account.

(h) Investments in subsidiaries

Investments in subsidiaries are stated at cost less provision for impairment in value.

(i) Depreciation

The provision for depreciation on tangible fixed assets is calculated to write off their cost over their estimated useful lives by equal annual instalments as follows:

Freehold and long leasehold property	2.5%
Office machinery and furniture	10%—33%
Motor vehicles	25%
Short leasehold property	over the length of the lease

No depreciation is provided in respect of freehold land, which is stated at cost.

(j) Foreign currencies

Foreign currency deposits and advances are translated into sterling at the rates of exchange ruling at the balance sheet date. Translation differences are taken to the profit and loss account.

(k) Deferred taxation

Deferred taxation is provided in full on material timing differences, at the rates of taxation expected to apply when these differences crystallise, arising from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the financial statements. This policy reflects the group's adoption of Financial Reporting Standard No. 19 on Deferred Taxation.

(l) Goodwill

Before 1st August, 1998, goodwill arising on the acquisition of business assets, representing the excess of the purchase consideration over the fair value ascribed to the net tangible assets, was written off to reserves in the year of acquisition. From 1st August, 1998, as required by Financial Reporting Standard No. 10, such goodwill arising has been capitalised in intangible assets and is amortised in equal annual instalments over its estimated useful life of up to 20 years.

(m) Pensions

The cost of providing pensions is charged to the profit and loss account so as to spread the cost for those employees in defined benefit schemes over the expected service lives of those employees. Contributions within defined contribution schemes are charged to the profit and loss account as they become payable in accordance with the rules of the schemes.



Close Brothers

THE NOTES

2. Administrative expenses	2002	2001
	£'000	£'000
Staff costs:		
Wages and salaries	94,943	94,222
Social security costs	10,360	11,323
Other pension costs	6,827	4,787
	<u>112,130</u>	<u>110,332</u>
Other administrative expenses	62,253	63,400
	<u>174,383</u>	<u>173,732</u>

Administrative expenses include exceptional costs of £3,446,000 (2001 — £Nil) relating to reorganisation and redundancy. The average number of persons employed by the group during the year was 1,801 (2001 — 1,648).

3. Information regarding directors	2002	2001
	£'000	£'000
Directors' emoluments:		
Salaries	2,058	2,132
Fees	105	81
Other benefits	112	106
Performance related awards in respect of the current year		
— Current	2,450	2,864
— Deferred	—	804
Compensation for loss of office	389	—
	<u>5,114</u>	<u>5,987</u>
Gains upon exercise of options	191	595
Company pension contributions	463	458
	<u>5,768</u>	<u>7,040</u>

The remuneration of individual directors is shown on page 20.

Directors' share options:

Executive directors hold options under the 1995 Executive Share Option Scheme ("1995 Scheme"), approved by shareholders in November 1995, and an Inland Revenue approved Saving Related Share Option Scheme ("SAYE Scheme").

Non-executive directors do not hold options over ordinary shares of the company.

Unexercised options over ordinary shares held by directors under the 1995 Scheme and SAYE Scheme were as follows:

	Granted		Exercised during the year	Options in issue 31st July, 2002		Options in issue Exercise dates		Options exercised	
	1st August, 2001	during the year		Exercise price*	Earliest	Latest	Exercise price	Market price	
D.G. Hardisty			30,455 2,562					330.00p 378.00p	885.00p 810.00p
	228,767	27,168	33,017	222,918	583.23p	6th Nov, 99	25th Sep, 11		
M.A. Hines	82,260	25,000	—	107,260	866.31p	3rd Nov, 02	25th Sep, 11	—	—
S.R. Hodges	309,971	70,000	—	379,971	611.43p	30th Oct, 00	25th Sep, 11	—	—
R.D. Kent	354,222	77,168	2,562	428,828	648.29p	7th Oct, 01	25th Sep, 11	378.00p	810.00p
C.D. Keogh	322,153	70,000	—	392,153	598.84p	6th Nov, 99	25th Sep, 11	—	—
D.J. Macnamara (alternate)	82,260	25,918	—	108,178	858.65p	3rd Nov, 02	25th Sep, 11	—	—
D.C. Pusinelli	187,816	31,511	—	219,327	629.29p	6th Nov, 99	25th Sep, 11	—	—
P.L. Winkworth	391,641	75,000	—	466,641	621.30p	30th Oct, 00	25th Sep, 11	—	—
*weighted average									

The interests of directors in options have remained unchanged since 31st July, 2002.

Option grants from the 1995 Scheme are phased and no options are granted at a discount. Under the terms of the 1995 Scheme, options may be exercised between three and ten years after the date of grant, only if performance targets are met. In relation to half of these options granted, the target requires that the growth in earnings per share over any three year period is at least RPI plus 4 per cent. per annum. In relation to the remainder of these options granted, the target requires that the growth in earnings per share over any five year period is such as to place the company in the top quartile of FTSE-100 companies by comparative measurement.

Under the terms of the SAYE Scheme, options are granted for a fixed contract period of three or five years, usually at a discount of 20 per cent. to the mid-market price.

The mid-market price of the company's shares on 31st July, 2002 was 452.5p and the range during the year was 423p to 900p.

THE NOTES

4. Segmental analysis

	Operating income		Profit before goodwill, exceptional items and taxation		Net assets	
	2002	2001	2002	2001	2002	2001
	£'000	£'000	£'000	£'000	£'000	£'000
Asset Management	66,010	70,315	15,914	23,949	120,285	116,017
Corporate Finance	26,160	48,315	2,101	11,937	11,045	13,189
Banking	137,131	116,306	55,067	40,895	208,835	191,529
Market-Making	46,552	57,210	16,812	27,379	50,942	50,482
Group	501	533	(11,347)	(9,993)	80,816	36,674
Total	276,354	292,679	78,547	94,167	471,923	407,891

Substantially all of the group's activities are located within the British Isles.

5. Operating profit on ordinary activities before taxation	2002	2001
	£'000	£'000
Profit on ordinary activities before taxation is stated after charging:		
Audit fees:		
To Deloitte & Touche	447	395
To Ernst & Young LLP	363	382
	<u>810</u>	<u>777</u>
Other fees paid to the auditors in respect of:		
Corporation tax compliance	292	199
Corporation tax & VAT advice	123	125
Regulatory and pension audit work	69	166
Due diligence reviews	20	60
Other advisory work	86	181
	<u>590</u>	<u>731</u>
Operating lease rentals payable	<u>6,203</u>	<u>5,162</u>

Aggregate rentals received in respect of finance leases and hire purchase contracts amounted to £380,951,000 (2001 — £301,326,000).

6. Taxation on profit on ordinary activities	2002	2001
	£'000	£'000
The current year tax charge comprises:		
UK corporation taxation	19,445	27,897
Overseas taxation	2,049	2,072
Deferred taxation (note 18)	1,162	(1,041)
Prior year over-provision	(817)	(289)
	<u>21,839</u>	<u>28,639</u>
Reconciliation to the current year tax charge:		
Operating profit on ordinary activities before taxation	<u>68,420</u>	<u>89,496</u>
Tax on above operating profit at 30% (2001 — 30%)	20,526	26,849
Goodwill amortisation disallowed	2,004	1,401
Disallowable expenses and other permanent differences	126	678
Prior year over-provision	(817)	(289)
	<u>21,839</u>	<u>28,639</u>



Close Brothers

THE NOTES

7. Loans and advances to banks	2002	2001
	£'000	£'000
Repayable:		
On demand	158,018	221,742
Within three months	273,043	349,438
Between three months and one year	12,114	22,714
	<u>443,175</u>	<u>593,894</u>

8. Loans and advances to customers	2002	2001
	£'000	£'000
Loans and advances (net of provisions and non-recourse borrowings) comprise:		
Hire purchase agreement receivables	595,682	530,088
Finance lease receivables	231,139	178,235
Other loans and advances	409,177	448,082
	<u>1,235,998</u>	<u>1,156,405</u>

The aggregate cost of assets acquired for the purpose of letting under finance leases and hire purchase agreements was £1,247,842,000 (2001 — £1,043,568,000).

	2002	2001
	£'000	£'000
Loans and advances are repayable:		
On demand or at short notice	57,412	67,388
Within three months	313,562	295,059
Between three months and one year	320,116	328,988
Between one and two years	254,024	214,224
Between two and five years	305,572	268,883
After more than five years	19,675	18,585
Provisions	(34,363)	(36,722)
	<u>1,235,998</u>	<u>1,156,405</u>

Receivables securitised by non-recourse borrowings

Close Brothers Limited ("CBL") has securitised £182,000,000 of its insurance premium finance receivables with Cruise Limited ("Cruise") in return for non-refundable finance of £175,000,000. If the receipts from the finance receivables exceed interest and principal loan liabilities due to Cruise, the surplus is due to CBL. Should there be a shortfall, CBL and the group are not obliged to, and do not intend to, support any losses and the providers of the funding have agreed to this. CBL has the option to replace these securitised loans as they are repaid. The balance sheet of Cruise comprises principally insurance premium finance receivables of £182,000,000 and borrowings of £175,000,000. The profit and loss account, other recognised gains and losses and cashflows of Cruise are negligible.

9. Provisions for bad and doubtful debts	2002	2001
	£'000	£'000
At 1st August, 2001	36,722	23,992
Acquisition of subsidiaries	—	7,926
Charge for the year	19,256	17,919
Amounts written off	(21,615)	(13,115)
At 31st July, 2002	<u>34,363</u>	<u>36,722</u>

THE NOTES

10. Debt securities	2002	2001
	£'000	£'000
Debt securities held for trading purposes:		
Long positions	<u>64,352</u>	<u>35,764</u>

Long positions are accounted for on the basis outlined in note 1(g) and comprise debt securities held by Winterflood Gilts Limited. £3,972,000 (2001 — £2,314,000) were due to mature within one year and £60,380,000 (2001 — £33,450,000) were due to mature in one year and over. That company's short positions, which are shown in the consolidated balance sheet, were £52,231,000 (2001 — £38,182,000).

	2002	2001
	£'000	£'000
Other:		
Certificates of deposit (held for liquidity purposes at cost)	702,397	471,956
Floating rate notes (held for investment purposes at cost)	<u>9,983</u>	<u>9,980</u>
	<u>712,380</u>	<u>481,936</u>

At both 31st July, 2002 and 31st July, 2001 the certificates of deposit were unlisted and issued by banks and building societies, and were due to mature within one year. The floating rate notes, of which £3,999,000 (2001 — £1,997,000) mature in less than one year, were listed and issued by UK banks and building societies and are intended to be held until maturity.



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11. Equity shares

	Trading		Investment	
	2002	2001	2002	2001
	£'000	£'000	£'000	£'000
Group				
Listed	15,971	33,413	6,942	8,217
Unlisted	—	—	21,542	19,312
	<u>15,971</u>	<u>33,413</u>	<u>28,484</u>	<u>27,529</u>
Company				
Listed	—	—	4,787	5,204
Unlisted	—	—	182	182
	<u>—</u>	<u>—</u>	<u>4,969</u>	<u>5,386</u>

Equity shares are accounted for on the basis outlined in note 1(g).

All trading shares are held by Winterflood Securities Limited and form that company's long positions. Its short positions, which are shown in the consolidated balance sheet, were £7,589,000 (2001 — £9,594,000).

The listed equity shares held by the company relate to the company's ordinary shares held by the employee share benefit trust.

The historical cost of equity shares held for investment purposes is as follows:

	Group		Company	
	2002	2001	2002	2001
	£'000	£'000	£'000	£'000
Listed	8,528	9,523	4,787	5,204
Unlisted	23,072	20,533	182	182
	<u>31,600</u>	<u>30,056</u>	<u>4,969</u>	<u>5,386</u>

The movement on equity shares held for investment purposes is as follows:

	Group	Company
	£'000	£'000
At 1st August, 2001	27,529	5,386
Additions	5,173	—
Disposals	(3,582)	(417)
Unrealised deficit on revaluation	(636)	—
At 31st July, 2002	<u>28,484</u>	<u>4,969</u>

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12. Tangible fixed assets

	Land and buildings	Office machinery and furniture	Motor vehicles	Total
Group	£'000	£'000	£'000	£'000
Cost or valuation				
At 1st August, 2001	7,820	26,696	5,679	40,195
Additions	1,108	11,835	1,453	14,396
Disposals	(653)	(1,069)	(3,457)	(5,179)
At 31st July, 2002	8,275	37,462	3,675	49,412
Depreciation				
At 1st August, 2001	1,001	16,627	2,099	19,727
Charge for the year	474	6,112	1,028	7,614
Disposals	(5)	(897)	(1,694)	(2,596)
At 31st July, 2002	1,470	21,842	1,433	24,745
Net book value at 31st July, 2002	6,805	15,620	2,242	24,667
Net book value at 31st July, 2001	6,819	10,069	3,580	20,468
Company				
Cost or valuation				
At 1st August, 2001	3,732	1,601	224	5,557
Additions	3	42	53	98
Disposals	—	(4)	(49)	(53)
At 31st July, 2002	3,735	1,639	228	5,602
Depreciation				
At 1st August, 2001	372	562	124	1,058
Charge for the year	237	241	49	527
Disposals	—	(4)	(34)	(38)
At 31st July, 2002	609	799	139	1,547
Net book value at 31st July, 2002	3,126	840	89	4,055
Net book value at 31st July, 2001	3,360	1,039	100	4,499

The net book value of land and buildings comprises:

	Group		Company	
	2002	2001	2002	2001
	£'000	£'000	£'000	£'000
Freehold	2,013	2,727	—	—
Long leasehold	1,082	249	—	—
Short leasehold	3,710	3,843	3,126	3,360
	6,805	6,819	3,126	3,360

13. Deposits by banks

	2002	2001
	£'000	£'000
Repayable:		
On demand or at short notice	1,940	4,911
Within three months	76,219	33,732
Between three months and one year	5,000	17,000
	83,159	55,643



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14. Customer accounts	2002	2001
	£'000	£'000
Repayable:		
On demand or at short notice	336,932	238,539
Within three months	825,997	829,895
Between three months and one year	59,062	68,765
Between one and two years	526	2,000
Between two and five years	24	4,956
	<u>1,222,541</u>	<u>1,144,155</u>
<hr/>		
15. Bank loans and overdrafts	2002	2001
	£'000	£'000
Repayable:		
On demand or at short notice	16,887	3,025
Within three months	30,000	54,342
Between three months and one year	45,050	32,500
Between one and two years	136,718	175,797
Between two and five years	228,000	292,965
Over five years	49,000	49,000
	<u>505,655</u>	<u>607,629</u>
<hr/>		
16. Debt securities – loan notes issued	2002	2001
	£'000	£'000
Repayable:		
Between three months and one year	—	18,140
Between one and two years	—	—
Between two and five years	100,000	—
	<u>100,000</u>	<u>18,140</u>
<hr/>		
<p>£100,000,000 of floating rate notes were issued during the year. They are repayable on 28th December, 2004. £18,140,000 of loan notes, which were U.S. dollar denominated, were repaid on 10th June, 2002.</p>		
<hr/>		
17. Other assets and liabilities	2002	2001
	£'000	£'000
Other assets		
Loans to money brokers against stock advanced	90,385	60,096
Other assets	44,299	58,964
	<u>134,684</u>	<u>119,060</u>
Other liabilities		
Loans from money brokers against stock advanced	84,299	28,646
Current corporation taxation	9,905	14,965
Proposed dividend	24,214	22,927
Other liabilities	109,650	130,834
	<u>228,068</u>	<u>197,372</u>

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18. Deferred taxation

	Group		Company	
	2002	2001	2002	2001
	£'000	£'000	£'000	£'000
Group				
Capital allowances	5,804	6,184	(575)	(248)
Short term and other timing differences	4,541	5,323	1,025	795
Total deferred taxation asset	10,345	11,507	450	547
Movement in the year:			Group	Company
			£'000	£'000
Asset at 1st August, 2001			11,507	547
Charge for the year			(1,162)	(97)
Asset at 31st July, 2002			10,345	450

19. Subordinated loan capital

Final maturity date	Prepayment date at issuer's option	Initial interest rate (%)	Notes	2002	2001
				£'000	£'000
2010	2005	10.07	(a)	21,937	21,937
2020	2015	7.39	(b)	30,000	30,000
2026	2021	7.42	(c)	15,000	15,000
2026	2021	7.62	(c)	30,000	30,000
				96,937	96,937

(a) The 2010 subordinated loan capital is initially denominated in sterling and converts to U.S. dollars in 2005. If Close Brothers Limited ("CBL") opts not to prepay in 2005, the interest rate is reset to a margin over the 5 year U.S. Treasury rate, payable in U.S. dollars.

(b) The 2020 subordinated loan capital is denominated in sterling. If CBL opts not to prepay in 2015, the interest rate is reset to a margin over the yield on 5 year U.K. Treasury securities.

(c) The 2026 subordinated loan capital is denominated in sterling. If CBL opts not to prepay in 2021, the interest rate is reset to a margin over the yield on 5 year U.K. Treasury securities.

There are no circumstances in which early repayment can be demanded of any issue other than upon the passing of a winding-up order in respect of the issuer, CBL, in which case the loan capital is subordinated to the claims of all unsubordinated creditors, including depositors. The subordinated loan capital is guaranteed by the company.



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20. Share capital	2002		2001	
	No.'000	£'000	No.'000	£'000
Authorised				
Ordinary shares of 25p each	<u>200,000</u>	<u>50,000</u>	<u>200,000</u>	<u>50,000</u>
Allotted, issued and fully paid				
At 1st August, 2001	136,220	34,055	135,039	33,760
Issued during the year	6,800	1,700	520	130
Exercise of options	<u>658</u>	<u>165</u>	<u>661</u>	<u>165</u>
At 31st July, 2002	<u>143,678</u>	<u>35,920</u>	<u>136,220</u>	<u>34,055</u>

On 22nd April, 2002, 6,800,000 ordinary shares, with an aggregate nominal value of £1,700,000, were allotted and issued for 805p per share by way of a placing for cash, fully paid. The total consideration before expenses was £54,740,000. The issue was made under an authority granted by the company's shareholders at the last Annual General Meeting.

The following options to subscribe for ordinary shares have been granted under the sharesave and executive share option schemes to 613 employees:

Year of grant	Exercise period	Exercise price per share	2002 Number	2001 Number
1993	29th October, 1998 to 28th October, 2003	219.90p	64,262	64,262
1994	4th November, 1999 to 3rd November, 2004	231.68p	32,598	44,822
1995	3rd November, 1998 to 2nd November, 2005	316.00p	4,000	12,500
1995	3rd November, 2000 to 2nd November, 2005	316.00p	50,000	80,800
1996	6th November, 1999 to 5th November, 2006	330.00p	138,180	187,270
1996	6th November, 2001 to 5th November, 2006	330.00p	373,885	541,250
1996	1st December, 2001 to 31st May, 2002	252.00p	—	117,809
1997	30th October, 2000 to 29th October, 2007	482.50p	309,509	371,259
1997	30th October, 2002 to 29th October, 2007	482.50p	564,750	582,750
1997	1st December, 2002 to 31st May, 2003	386.00p	65,580	74,781
1998	7th October, 2001 to 6th October, 2008	417.50p	630,217	773,875
1998	7th October, 2003 to 6th October, 2008	417.50p	689,125	751,826
1998	9th November, 2001 to 8th November, 2008	552.50p	6,000	6,000
1998	9th November, 2003 to 8th November, 2008	552.50p	6,000	6,000
1998	1st December, 2001 to 31st May, 2002	378.00p	—	50,455
1998	1st December, 2003 to 31st May, 2004	378.00p	75,546	81,794
1999	3rd November, 2002 to 2nd November, 2009	779.50p	715,750	728,250
1999	3rd November, 2004 to 2nd November, 2009	779.50p	674,500	728,250
1999	1st December, 2002 to 31st May, 2003	590.00p	89,371	119,301
1999	1st December, 2004 to 31st May, 2005	590.00p	70,464	138,473
2000	23rd October, 2003 to 22nd October, 2010	1125.00p	529,973	580,405
2000	23rd October, 2005 to 22nd October, 2010	1125.00p	529,973	580,405
2000	1st December, 2003 to 31st May, 2004	958.00p	2,481	69,132
2000	1st December, 2005 to 31st May, 2006	958.00p	3,555	91,088
2001	16th April, 2004 to 15th April, 2011	865.50p	8,665	27,850
2001	16th April, 2006 to 15th April, 2011	865.50p	8,665	27,850
2001	26th September, 2004 to 25th September, 2011	560.00p	675,534	—
2001	26th September, 2006 to 25th September, 2011	560.00p	675,534	—
2001	1st December, 2004 to 31st May, 2005	438.00p	419,697	—
2001	1st December, 2006 to 31st May, 2007	438.00p	397,925	—
			<u>7,811,739</u>	<u>6,838,457</u>

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21. Reserves

	Share premium account	Profit and loss account
Group	£'000	£'000
At 1st August, 2001	193,253	180,583
Retained profit for the year	—	7,920
Exchange adjustment	—	(978)
Shares issued net of expenses	55,203	—
Goodwill reduction in respect of deferred consideration	—	22
	<u>248,456</u>	<u>187,547</u>
At 31st July, 2002	<u>248,456</u>	<u>187,547</u>

The cumulative goodwill written off directly to reserves since the formation of the group is £81,923,000 (2001 — £81,945,000). This goodwill is accounted for on the basis outlined in note 1(i) and would be charged or credited to the profit and loss account should the businesses to which the goodwill relates be sold.

	Share premium account	Profit and loss account
Company	£'000	£'000
At 1st August, 2001	193,253	73,496
Retained loss for the year	—	(10,867)
Shares issued net of expenses	55,203	—
	<u>248,456</u>	<u>62,629</u>
At 31st July, 2002	<u>248,456</u>	<u>62,629</u>

Reconciliation of movements in shareholders' funds:	2002	2001
Group	£'000	£'000
Profit for the year	44,329	59,103
Dividends	(36,409)	(35,048)
	<u>7,920</u>	<u>24,055</u>
Retained profit for the year	7,920	24,055
Exchange adjustment	(978)	13
Shares issued net of expenses — capital	1,865	295
— premium	55,203	8,010
Goodwill	22	4,159
	<u>64,032</u>	<u>36,532</u>
Net addition to shareholders' funds	64,032	36,532
Opening shareholders' funds	407,891	371,359
	<u>471,923</u>	<u>407,891</u>
Closing shareholders' funds	<u>471,923</u>	<u>407,891</u>



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22. Contingent liabilities

Memorandum items

There are group contingent liabilities in respect of guarantees arising in the normal course of business amounting to £2,412,000 (2001 — £3,555,000).

Other contingent liabilities

The company has given guarantees in respect of amounts drawn under subsidiaries' bank facilities amounting to £489,350,000 (2001 — £574,221,000). In addition, the company has given guarantees in respect of long term loan notes issued by subsidiaries amounting to £97,937,000 (2001 — £122,540,000).

A subsidiary recently received notice of a potential claim against it in respect of advisory work. Any such claim will be vigorously resisted and, on the basis of their current assessment, the directors believe that the claim, if made, will not have a material effect on the group's financial position.

23. Commitments	2002	2001
	£'000	£'000
Memorandum items		
Undrawn facilities, credit lines and other commitments to lend:		
Within one year	163,545	137,750
After more than one year	2,967	1,153
	<u>166,512</u>	<u>138,903</u>

Other commitments

The group is committed to purchase minority interests in certain subsidiaries at agreed fair valuation at varying dates in the period to 31st July, 2011.

Subsidiaries had contracted capital commitments relating to capital expenditure of £235,000 (2001 — £91,000).

Subsidiaries had contracted capital commitments in connection with private equity funds managed by the group of £17,228,000 (2001 — £8,044,000).

Annual commitments under non-cancellable operating leases at 31st July, 2002 were as follows:

	Premises £'000	Other £'000
Expiring:		
Within one year	65	23
Within two to five years	665	396
After more than five years	7,367	—
	<u>8,097</u>	<u>419</u>

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24. Interest rate exposure

The group's interest rate exposure is summarised below in the form of an interest rate repricing table. The table reflects the repricing profile of the group's non trading assets, liabilities and net interest rate swap contracts as at the year end. The trading activities of Winterflood Securities Limited and Winterflood Gilts Limited are different in nature and so are the only net assets excluded here and instead analysed in note 28. The table shows the sensitivity of the group's non trading net assets to interest rate movements. The cumulative gap of interest bearing net assets of £373,162,000 (2001 — £326,638,000) broadly equates to the group's non trading share capital and reserves, which as a matter of policy are not hedged. The table therefore demonstrates the group's policy of broadly hedging interest rate exposure.

At 31st July, 2002

	Within three months £'000	Between three and six months £'000	Between six months and one year £'000	Between one and five years £'000	After more than five years £'000	Non- interest bearing £'000	Total £'000
Non trading assets							
Cash and balances at central banks	—	—	—	—	—	671	671
Loans and advances to banks	431,060	9,163	2,952	—	—	—	443,175
Loans and advances to customers	406,994	124,761	149,560	536,030	18,653	—	1,235,998
Debt securities and equity shares	678,546	24,334	9,500	—	—	28,910	741,290
Settlement accounts	—	—	—	—	—	246,456	246,456
Other assets	92,116	—	—	4,067	—	209,534	305,717
	<u>1,608,716</u>	<u>158,258</u>	<u>162,012</u>	<u>540,097</u>	<u>18,653</u>	<u>485,571</u>	<u>2,973,307</u>
Non trading liabilities							
Deposits by banks	78,159	5,000	—	—	—	—	83,159
Customer accounts	1,177,144	29,141	15,706	550	—	—	1,222,541
Bank loans and overdrafts	390,569	115,000	86	—	—	—	505,655
Debt securities — loan notes issued	100,000	—	—	—	—	—	100,000
Settlement accounts	—	—	—	—	—	202,343	202,343
Other liabilities	103,367	300	1,743	872	—	198,891	305,173
Subordinated loan capital	—	—	—	21,937	75,000	—	96,937
Minority interests and shareholders' funds	—	—	—	—	—	478,002	478,002
	<u>1,849,239</u>	<u>149,441</u>	<u>17,535</u>	<u>23,359</u>	<u>75,000</u>	<u>879,236</u>	<u>2,993,810</u>
Non trading net (liabilities)/assets	<u>(240,523)</u>	<u>8,817</u>	<u>144,477</u>	<u>516,738</u>	<u>(56,347)</u>	<u>(393,665)</u>	<u>(20,503)</u>
Net interest rate swaps							
Floating rate	236,401	185,000	—	—	—	—	421,401
Fixed rate	(50,500)	(35,000)	(123,080)	(212,821)	—	—	(421,401)
	<u>185,901</u>	<u>150,000</u>	<u>(123,080)</u>	<u>(212,821)</u>	<u>—</u>	<u>—</u>	<u>—</u>
Interest rate sensitivity gap	<u>(54,622)</u>	<u>158,817</u>	<u>21,397</u>	<u>303,917</u>	<u>(56,347)</u>	<u>—</u>	<u>—</u>
Cumulative gap	<u>(54,622)</u>	<u>104,195</u>	<u>125,592</u>	<u>429,509</u>	<u>373,162</u>	<u>—</u>	<u>—</u>



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24. Interest rate exposure *continued*

At 31st July, 2001

	Within three months £'000	Between three and six months £'000	Between six months and one year £'000	Between one and five years £'000	After more than five years £'000	Non- interest bearing £'000	Total £'000
Non trading assets							
Cash and balances at central banks	—	—	—	—	—	586	586
Loans and advances to banks	575,745	17,149	1,000	—	—	—	593,894
Loans and advances to customers	404,343	114,019	163,197	457,274	17,572	—	1,156,405
Debt securities and equity shares	428,089	38,000	16,000	—	—	27,804	509,893
Settlement accounts	—	—	—	—	—	147,750	147,750
Other non trading assets	65,610	—	—	4,067	—	219,301	288,978
	<u>1,473,787</u>	<u>169,168</u>	<u>180,197</u>	<u>461,341</u>	<u>17,572</u>	<u>395,441</u>	<u>2,697,506</u>
Non trading liabilities							
Deposits by banks	38,643	17,000	—	—	—	—	55,643
Customer accounts	1,075,491	37,607	24,101	6,956	—	—	1,144,155
Bank loans and overdrafts	456,935	141,276	9,418	—	—	—	607,629
Debt securities — loan notes issued	—	—	18,140	—	—	—	18,140
Settlement accounts	—	—	—	—	—	114,174	114,174
Other non trading liabilities	44,581	5,835	1,304	1,203	—	216,359	269,282
Subordinated loan capital	—	—	—	—	96,937	—	96,937
Minority interests and shareholders' funds	—	—	—	—	—	412,947	412,947
	<u>1,615,650</u>	<u>201,718</u>	<u>52,963</u>	<u>8,159</u>	<u>96,937</u>	<u>743,480</u>	<u>2,718,907</u>
Non trading net (liabilities)/assets	<u>(141,863)</u>	<u>(32,550)</u>	<u>127,234</u>	<u>453,182</u>	<u>(79,365)</u>	<u>(348,039)</u>	<u>(21,401)</u>
Net interest rate swaps							
Floating rate	266,140	131,860	1,052	—	—	—	399,052
Fixed rate	(80,882)	(32,500)	(65,161)	(240,509)	—	—	(399,052)
	<u>205,258</u>	<u>99,360</u>	<u>(64,109)</u>	<u>(240,509)</u>	<u>—</u>	<u>—</u>	<u>—</u>
Interest rate sensitivity gap	<u>63,395</u>	<u>66,810</u>	<u>63,125</u>	<u>212,673</u>	<u>(79,365)</u>	<u>—</u>	<u>—</u>
Cumulative gap	<u>63,395</u>	<u>130,205</u>	<u>193,330</u>	<u>406,003</u>	<u>326,638</u>	<u>—</u>	<u>—</u>

These tables do not reflect the benefit of interest rate caps taken out by the group to protect against the risk of a rise in interest rates. At 31st July, 2002 the group had no interest rate caps (2001 — one with a contract amount of £20,000,000).

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25. Interest rate and exchange rate contracts	2002	2001
	£'000	£'000
Interest rate contracts:		
Contract amount	441,139	452,802
Credit risk weighted amount	258	331
Exchange rate contracts:		
Contract amount	—	20,166
Credit risk weighted amount	—	161

Interest rate and exchange rate contracts are entered into only for hedging purposes. The credit risk weighted amounts have been prepared in accordance with guidelines laid down by the Financial Services Authority and are intended to give an indication of credit risk.

26. Assets and liabilities in foreign currencies

The aggregate amounts of assets and liabilities denominated in foreign currencies, mainly U.S. dollars, were as follows:

	2002	2001
	£'000	£'000
Assets	<u>320,056</u>	<u>309,357</u>
Liabilities	<u>306,592</u>	<u>306,445</u>

The group's exposure to foreign exchange risk is considered by the directors to be minimal.



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27. Fair values of financial instruments and unrecognised gains and losses on hedges

The fair values of the group's trading financial assets and liabilities are dealt with in note 28. The tables below highlight the unrecognised gains and losses, attributable to the group's derivative financial instruments and non trading financial assets and liabilities, for which liquid and active markets exist. Certificates of deposit and derivative financial instruments are normally held to maturity and are purchased for liquidity and hedging purposes respectively. The fair values of the financial instruments have been obtained from independent, open market sources or using discounted cash flow techniques based on prevailing market rates.

	2002		2001	
	Book value £'000	Fair value £'000	Book value £'000	Fair value £'000
Primary financial assets:				
Debt securities	712,380	712,461	481,936	482,166
Listed investments — equity shares	6,942	7,870	8,217	13,237
	<u>719,322</u>	<u>720,331</u>	<u>490,153</u>	<u>495,403</u>
Primary financial liabilities:				
Floating rate notes	100,000	99,868	—	—

The directors deem that the fair value of the group's other non trading financial assets and liabilities materially equate to their book value.

In order to minimise the impact of interest rate and currency rate changes to the group's financial assets and liabilities, derivative financial instruments are purchased to hedge exposures. The tables below summarise the unrecognised gains and losses on these derivative financial instruments:

	2002		2001		Total net losses £'000
	Book value £'000	Fair value £'000	Book value £'000	Fair value £'000	
Derivative financial instruments held to manage the interest rate and currency exposure:					
Interest rate swaps	—	(5,101)	—	(2,393)	
Currency swaps	—	—	—	589	
	<u>—</u>	<u>(5,101)</u>	<u>—</u>	<u>(1,804)</u>	
Unrecognised gains and losses on hedges:		Gains £'000	Losses £'000		
At 1st August, 2001		1,258	3,062		(1,804)
Gains and losses on hedges arising in previous years that were recognised in the current year		1,083	1,256		(173)
Gains and losses on hedges arising in previous years that were not recognised in the current year		175	1,806		(1,631)
Gains and losses on hedges arising in the current year that have not yet been recognised		34	3,504		(3,470)
At 31st July, 2002		<u>209</u>	<u>5,310</u>		<u>(5,101)</u>
Of which:					
Gains and losses on hedges expected to be recognised next year		206	4,797		(4,591)
Gains and losses on hedges expected to be recognised later than next year		3	513		(510)

THE NOTES

28. Trading book exposure

The group's trading activities relate to Winterflood Securities Limited and its subsidiary Winterflood Gilts Limited.

The following table shows the group's trading book exposure to market price risk for the year ended 31st July, 2002:

		Highest exposure £'000	Lowest exposure £'000	Average exposure £'000	Exposure at 31st July £'000
Equities	— Long	34,598	15,971	25,343	15,971
	— Short	20,613	7,223	12,136	7,589
				<u>13,207</u>	<u>8,382</u>
Debt securities	— Long	70,897	34,276	51,797	64,352
	— Short	61,936	32,221	48,014	52,231
				<u>3,783</u>	<u>12,121</u>

The following table shows the group's trading book exposure to market price risk for the year ended 31st July, 2001:

		Highest exposure £'000	Lowest exposure £'000	Average exposure £'000	Exposure at 31st July £'000
Equities	— Long	67,007	33,122	48,951	33,413
	— Short	18,201	9,013	13,120	9,594
				<u>35,831</u>	<u>23,819</u>
Debt securities	— Long	49,377	23,969	33,445	35,764
	— Short	45,864	22,506	31,459	38,182
				<u>1,986</u>	<u>(2,418)</u>

The average exposure has been calculated on a daily basis. The highest and lowest exposures occurred on different dates and therefore a net position of these exposures does not reflect a spread of the trading book. The basis on which the trading book is valued each day is given in the accounting policies in note 1(g).

Based upon the trading book exposure at 31st July, 2002 given above, a 10 per cent. hypothetical fall in market prices would result in a £838,000 (2001 — £2,382,000) decrease in the group's income and net assets on the equity trading book and a £1,212,000 decrease (2001 — £242,000 increase) on the debt securities trading book. However, the group's trading activity is a jobbing business where positions are managed throughout the day on a continuous basis. Accordingly the result shown above is purely hypothetical.

Summarised below are the gains for the year on financial assets and liabilities held for trading:

	2002	2001
	£'000	£'000
Net dealing income — equities	43,247	50,332
— debt securities	5,118	7,999
	<u>48,365</u>	<u>58,331</u>



Close Brothers

THE NOTES

29. Investments in subsidiaries

The group's principal subsidiaries at 31st July, 2002 were:

Name of company	Principal activity	Percentage of equity held by group	Country of registration and operation
Air and General Finance Limited	Aircraft financing	100	England
Braemar Finance Limited	Commercial asset financing	87	England
Close Asset Finance Limited	Commercial asset financing	100	England
Close Asset Management Guernsey Limited	Offshore investment management	100	Guernsey
Close Asset Management Holdings Limited	Asset management holding company	100	England
Close Asset Management Jersey Limited	Offshore investment management	100	Jersey
Close Bank (Cayman) Limited	Offshore banking	100	Cayman
Close Bank Guernsey Limited	Offshore banking	100	Guernsey
Close Bank (Isle of Man) Limited	Offshore banking	100	Isle of Man
Close Brothers (Cayman) Limited	Trust and company administration	85	Cayman
Close Brothers Corporate Finance Limited	Corporate finance	100	England
Close Brothers Finance plc	Finance company	100	England
Close Brothers Growth Capital Limited	Integrated debt and equity investment	87	England
Close Brothers Investment Limited	Tax based personal investment products	98 ¹	England
Close Brothers Limited	Commercial lending and treasury	100	England
Close Brothers Military Services Limited	Financial services for the Armed Forces	80	England
Close Brothers Private Equity Limited	Private equity fund management	99	England
Close Consumer Finance Limited	Car financing	100	England
Close Credit Management Limited	Credit management and debt collection	99	England
Close Finance (CI) Limited	Commercial and consumer asset financing	91	Jersey
Close Finsbury Asset Management Limited	Investment trust and funds management	100	England
Close Fund Management Limited	Special investment and unit trust management	90	England
Close Fund Services Limited	Offshore fund administration	100	Guernsey
Close Investment Limited	AIM fund management	97	England
Close Investment Management (Isle of Man) Limited	Offshore investment management	100	Isle of Man
Close Invoice Finance Limited	Debt factoring and invoice discounting	95	England
Close Portfolio Management Limited	Investment company	100	England
Close Private Asset Management Limited	Private client fund management	100	England
Close Trust Company Jersey Limited	Trust and company administration	100	Jersey
Close Trustees Guernsey Limited	Trust and company administration	100	Guernsey
Close Trustees (Isle of Man) Limited	Trust and company administration	100	Isle of Man
Close Trustees (Switzerland) S.A.	Trust and company administration	70	Switzerland
Close Wealth Management Limited	Private client discretionary fund management	90 ²	England
Dôme Close Brothers S.A.	Corporate finance	50	France
Freyberg Close Brothers GmbH	Corporate finance	50	Germany
Metropolitan Factors Limited	Debt factoring	95	England
Mortgage Intelligence Limited	Mortgage broking	95	England
OLIM Limited	Institutional fund management	80	England
Rebourne Technology Investment Management Limited	Technology and biotechnology fund management	52	England
Surrey Asset Finance Limited	Commercial asset financing	88	England
Winterflood Gilts Limited	Gilts market-making	100	England
Winterflood Securities Limited	Equities market-making	100	England

1 In respect of Close Brothers Investment Limited, the group holds 7 per cent. and has a 99 per cent. holding in Close Brothers Private Equity Limited which itself holds a further 92 per cent.

2 In respect of Close Wealth Management Limited, the group holds 40 per cent. and has an 83 per cent. holding in Wealth Management Limited which itself holds the remaining 60 per cent.

The movement in the company's investments in subsidiaries was as follows:

	£'000
At 1st August, 2001	319,059
Net investments in subsidiaries during the year	4,938
At 31st July, 2002	323,997

THE NOTES

29. Investments in subsidiaries *continued*

Each acquisition made in the year has been consolidated using acquisition accounting. The book value of the acquisitions and the movement on goodwill are shown below:

Net liabilities of subsidiaries acquired during the year	£'000 <u>(86)</u>
Consideration for purchase of shares:	
Cash	1,150
Deferred consideration	<u>1,853</u>
Total consideration	<u>3,003</u>
Goodwill arising on acquisitions	3,089
Goodwill arising on acquisitions of minority interests	<u>2,577</u>
Goodwill capitalised during the year	5,666
Goodwill as at 1st August, 2001	114,080
Less:— amortisation during the year	<u>(6,681)</u>
Goodwill as at 31st July, 2002	<u>113,065</u>

Investments in joint ventures

The group has investments in a number of joint ventures totalling £5,000 (2001 — £5,000). They have been accounted for using the gross equity method. The group's share of operating loss of these joint ventures is £8,000 (2001 — profit of £3,079,000). The group did not receive any dividends (2001 — £2,400,000) from these joint ventures and has amounts owed by them totalling £4,669,000 (2001 — £4,454,000).

30. Debtors	2002	2001
	£'000	£'000
Company		
Amounts falling due within one year:		
Amounts owed by subsidiaries	97,466	68,623
Prepayments and accrued income	214	224
Corporation taxation receivable	2,501	1,133
Deferred taxation asset (note 18)	<u>450</u>	<u>547</u>
	<u>100,631</u>	<u>70,527</u>
31. Creditors: Amounts falling due within one year	2002	2001
	£'000	£'000
Company		
Bank loans and overdrafts	—	19,000
Amounts owed to subsidiaries	13,188	10,512
Accruals and deferred income	11,697	12,904
Proposed dividend	24,214	22,927
Other creditors	<u>10,667</u>	<u>6,498</u>
	<u>59,766</u>	<u>71,841</u>



Close Brothers

THE NOTES

32. Creditors: Amounts falling due after more than one year	2002	2001
	£'000	£'000
Company		
Loan from subsidiary	<u>27,072</u>	<u>27,072</u>

The loan is interest free and carries no fixed repayment date.

33. Profit of parent company

As permitted by Section 230 of the Companies Act 1985, the profit and loss account of the parent company is not presented as part of these financial statements. The parent company's profit for the financial year, before dividends payable, amounted to £25,542,000 (2001 — £61,867,000).

34. Earnings per share

The calculation of earnings per share on profit attributable to shareholders is based on profit after taxation and minority interests of £44,329,000 (2001 — £59,103,000) and on 137,244,000 (2001 — 134,422,000) ordinary shares, being the weighted average number of shares in issue during the year excluding those held by the employee share benefit trust.

The diluted earnings per share is based on the same profit after taxation and minority interests disclosed above, and on 138,445,000 (2001 — 135,405,000) ordinary shares, being the weighted average number of shares in issue also disclosed above, plus the weighted dilutive potential on ordinary shares of exercisable employee share options in issue during the year.

THE NOTES

35. Consolidated cash flow statement	2002	2001
	£'000	£'000
(a) Reconciliation of operating profit on ordinary activities before taxation to net cash (outflow)/inflow from operating activities		
Operating profit on ordinary activities before taxation	68,420	89,496
(Increase)/decrease in:		
Interest receivable and prepaid expenses	907	(5,510)
Net settlement accounts	(10,537)	18,023
Net equity shares held for trading	15,437	18,441
Net debt securities held for trading	(14,539)	48
Increase in interest payable and accrued expenses	4,911	1,468
Depreciation and amortisation	14,295	11,532
Net cash inflow from trading activities	<u>78,894</u>	<u>133,498</u>
(Increase)/decrease in:		
Debt securities held for liquidity	(230,444)	4,552
Loans and advances to customers	(221,593)	(130,104)
Loans and advances to banks not repayable on demand	86,995	136,607
Other assets less other liabilities	28,749	(24,810)
Increase/(decrease) in:		
Deposits by banks	27,516	(11,739)
Customer accounts	78,386	77,767
Bank loans and overdrafts	(101,974)	43,271
Non-recourse borrowings	142,000	33,000
Debt securities — loan notes issued	81,860	(18,141)
Net cash (outflow)/inflow from operating activities	<u>(29,611)</u>	<u>243,901</u>
(b) Analysis of net cash outflow in respect of the purchase of subsidiaries		
Cash consideration in respect of current year purchases	(1,150)	(73,217)
Loan stock redemptions and deferred consideration paid in respect of prior year purchases	(6,865)	—
Net movement in cash balances	<u>1,330</u>	<u>8,793</u>
	<u>(6,685)</u>	<u>(64,424)</u>
(c) Analysis of changes in financing		
Share capital (including premium) and subordinated loan capital:		
Opening balance	324,245	270,940
Shares issued for cash	57,068	2,455
Shares issued other than for cash	—	5,850
Subordinated loan capital issued	—	45,000
Closing balance	<u>381,313</u>	<u>324,245</u>
(d) Analysis of cash balances	Movement in the year	
	£'000	
Cash and balances at central banks	85	586
Loans and advances to banks repayable on demand	<u>(63,724)</u>	<u>221,742</u>
	<u>(63,639)</u>	<u>222,328</u>



Close Brothers

THE NOTES

36. Pensions

The group operates defined contribution pension schemes and a defined benefit pension scheme for eligible employees. Assets of all schemes are held separately from those of the group. The group pension charge for the schemes in total was £6,827,000 (2001 — £4,787,000).

In accordance with Statement of Standard Accounting Practice No. 24 on Accounting for Pension Costs, contributions to the defined benefit pension scheme are determined by an independent qualified actuary based on triennial valuations using the aggregate cost method. The most recent such valuation was at 31st July, 2000, when the market value of the assets of this scheme was £12,539,000 representing 85 per cent. of the benefits accrued to the 118 members, allowing for future earnings increases. The agreed company contribution rate was 25 per cent. per annum of pensionable salaries. Future contributions to be made by the participating companies under actuarial advice should meet all pension obligations. A 1 per cent. per annum differential between investment returns and salary increases is assumed.

In addition, in accordance with the transitional requirements of Financial Reporting Standard No. 17 ("FRS 17") on Retirement Benefits, this full actuarial valuation has been reviewed and updated as at 31st July, 2002 based upon the following annual financial assumptions: inflation — 2.50 per cent. (2001 — 2.60 per cent.); increase in salaries — 4.00 per cent. (2001 — 4.60 per cent.); increase in pension in payments — 3.00 per cent. (2001 — 3.00 per cent.); discount rate for scheme liabilities — 5.85 per cent. (2001 — 6.15 per cent.) and; expected return on equities — 7.00 per cent. (2001 — 7.00 per cent.), bonds — 5.85 per cent. (2001 — 6.00 per cent.) and gilts and cash — 5.00 per cent. (2001 — 5.00 per cent.). This valuation method is prescribed by FRS 17 and the accompanying assumptions do not necessarily reflect those used by the independent qualified actuary in the triennial valuation at 31st July, 2000 which determines the company contribution rate for future years, also as detailed above. Nonetheless, FRS 17 requires the directors to disclose the assets and liabilities of the scheme using these FRS 17 assumptions.

The group's total accumulated profit and loss account reserve, which was £187,547,000 (2001 — £180,583,000), would have been £180,269,000 (2001 — £175,481,000) if the FRS 17 net deficit disclosed below had been accounted for as a liability of the group:

	2002 £'000	2001 £'000
Equities	7,513	8,869
Bonds	2,008	1,412
Gilts and cash	872	1,145
Total market value of scheme assets	10,393	11,426
Present value of scheme liabilities	(20,790)	(18,715)
Deficit	(10,397)	(7,289)
Related deferred taxation asset	3,119	2,187
Net deficit	(7,278)	(5,102)

THE NOTES

36. Pensions *continued*

If the FRS 17 net deficit had been accounted for as a liability of the group this year, the charge to the group profit and loss account, the effect on the statement of total recognised gains and losses and the movement on the pension scheme deficit would have been:

	(Charge)/credit to the group profit and loss account £'000	Statement of total recognised gains and losses £'000	Pension scheme net liabilities £'000
Deficit at 1st August, 2001			(7,289)
Contributions			1,566
Expected return on scheme assets	763		
Interest discount on scheme liabilities	(1,216)		
Other finance costs	(453)		
Current service cost	(936)		
Actual return less expected return on scheme assets (representing 32% of the market value of scheme assets)		(3,365)	
Experience gains and losses arising on scheme liabilities (representing 1% of the present value of scheme liabilities)		(224)	
Changes in assumptions underlying the present value of the scheme liabilities		304	
Total actuarial loss (representing 16% of the present value of scheme liabilities)		(3,285)	(3,285)
	<u>(1,389)</u>		<u>(1,389)</u>
Deficit at 31st July, 2002			<u>(10,397)</u>

The theoretical FRS 17 charge to the profit and loss account of £1,389,000 shown above compares to the actual charge for this year of £1,566,000.

37. Related party transactions

Transactions with directors

Certain directors of the company maintained deposit accounts with Close Brothers Limited, a deposit taker authorised by the Financial Services Authority, during the course of the year on normal commercial terms.

Mr. D.G. Hardisty held £3,500,000 of unsecured loan notes, at 31st July, 2002 and 31st July, 2001, issued by Close Brothers Limited on normal commercial terms.

Transactions with joint ventures

Close Asset Management Holdings Limited ("CAMHL") has an investment in a joint venture, Roselead Limited, a company engaged in property development. In May 2001 CAMHL purchased all of the 2028 10 per cent. debenture loan stock which was issued by Roselead Limited with a nominal value of £4,067,000. Interest is payable 6 monthly and the loan is secured on the assets of the company. At 31st July, 2002 the loan balance outstanding was £4,067,000.

Close Brothers Investment Limited has an investment in a joint venture, Astergold Limited. Close Portfolio Management Limited undertook a commitment to fund certain transactions entered into by Astergold Limited. As at 31st July, 2002 the loan balance outstanding was £602,000.



Close Brothers

ADDITIONAL INFORMATION

Five Year Financial Summary

		1998	1999	2000	2001	2002
Operating income	£m	166.3	185.6	383.1	292.7	276.4
Profit before taxation, exceptional costs and goodwill amortisation	£m	69.6	76.3	155.1	94.2	78.5
Earnings per share before exceptional costs and goodwill amortisation	p	38.2	42.1	78.8	47.4	38.9
Profit before taxation	£m	69.6	76.3	144.8	89.5	68.4
Profit attributable to shareholders	£m	46.2	50.9	96.6	59.1	44.3
Earnings per share	p	38.2	42.1	72.9	44.0	32.3
Dividends per share	p	14.4	16.0	25.0	26.0	26.0
Shareholders' funds	£m	206	266	371	408	472
Total assets	£m	1,645	1,702	2,648	2,767	3,054
Number of employees		807	923	1,461	1,740	1,840

Share Price



ADDITIONAL INFORMATION

Shareholder Analysis

Number of shares held	Number of shareholders		Total shares held	
	2002	2001	2002	2001
Up to 500	1,844	1,814	503,337	500,486
501 — 1,000	1,196	1,274	944,681	1,011,640
1,001 — 2,000	749	755	1,102,997	1,109,879
2,001 — 5,000	607	610	1,952,509	2,004,447
5,001 — 10,000	237	249	1,727,950	1,833,146
10,001 — 50,000	360	376	8,397,776	8,601,885
Over 50,000	269	205	129,048,894	121,158,298
	<u>5,262</u>	<u>5,283</u>	<u>143,678,144</u>	<u>136,219,781</u>
Category of shareholders				
Investment groups	182	190	62,430,885	61,531,639
Insurance companies	23	30	44,017,359	37,113,774
Private shareholders	2,843	2,535	22,981,024	20,578,685
Pension funds	10	10	8,882,044	10,619,911
Others	2,204	2,518	5,366,832	6,375,772
	<u>5,262</u>	<u>5,283</u>	<u>143,678,144</u>	<u>136,219,781</u>

Calendar

Annual General Meeting	31st October, 2002
Payment of final dividend	5th November, 2002
Announcement of interim results	Early March, 2003
Payment of interim dividend	Mid April, 2003
Announcement of final results	September, 2003

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Close Brothers

GROUP OPERATIONS

Group

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Surrey Asset Finance Limited

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Mortgage Intelligence Limited

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Close Brothers

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Specialist Investment Trusts and Funds

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Investment Trust and Funds Management
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Close Investment Limited

AIM Fund Management
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Rebourne Technology Investment Management Limited

Technology and Biotechnology Fund Management
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Specialist Institutional Fund Management

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Index and Protected Unit Trusts

Close Fund Management Limited

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Offshore Financial Services

Guernsey:

Close International Private Banking

Private Banking, Safe Custody, Asset Management and Trust & Company Services

Close Bank Guernsey Limited

Close Asset Management Guernsey Limited

Close Trustees Guernsey Limited

Close International Custody Services Limited

PO Box 116,
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St. Peter Port, Guernsey
Channel Islands GY1 3EZ
Telephone: 01481 726014
Fax: 01481 711594
E-mail: enquiry@closeipb.com
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Close Fund Services Limited

Third Party Fund Administration
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Channel Islands GY1 3EP
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Isle of Man:

Close Private Bank

Offshore Banking, Investment Management and Trust & Company Administration

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Fax: 01624 622039
E-mail: info@close.co.im
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GROUP OPERATIONS

Jersey:

Close International Private Banking

*Private Banking, Asset Management
and Trust & Company Services*

Close Asset Management Jersey Limited

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Close Bank Guernsey Limited – Jersey Branch

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Switzerland:

Close Trustees (Switzerland) S.A.

Trust and Company Administration
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1207 Geneva
Switzerland
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Website: www.closetrusteesgeneva.com

Cayman:

Close Brothers (Cayman) Limited

*Trust and Company Administration, Mutual Fund
Administration and Investment Management*
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Close Bank (Cayman) Limited

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Tax and Property-Based Investment Management

Close Brothers Investment Limited

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Close Enterprise Management

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Close Property Investment

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Close Property Management

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Close Venture Management

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Private Equity Funds

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Close Brothers Growth Capital Limited

Integrated Debt and Equity Investment
Fax: 020 7426 4084
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