MIDLAND BANK PLC
ANNUAL REPORT
& ACCOUNTS 1988

MIDLAND GROUP

CONTENTS

FINANCIAL SUMMARY

	1988 £m	1987 £m
RESULTS FOR THE YEAR		
Profit before exceptional item and taxation	693	511
Profit/(loss) before taxation	693	(505)
Profit/(loss) attributable	412	(393)
Retentions/(deficit)	286	(483)
AT YEAR-END		
Total assets	55,729	48,450
Shareholders' funds	3,039	2,586
Total capital resources	5,038	4,488
PER ORDINARY SHARE		
Earnings/(loss)	75.1p	(125.3)p
Dividend	23.0p	20.1p
Net asset value	553p	473p
RATIOS		
Return on average equity – before taxation	24.3%	(23.3)%
Return on average shareholders' funds – profit attributable	15.0%	(18.9)%
Total equity/total assets	5.7%	5.5%
Dividend cover	3.3 times	–

The annual report on Form 20-F, which will be available when filed with the Securities and Exchange Commission in the US, contains additional statistical information and analyses of the Group's financial position and results of operations for 1988. Copies will be supplied on application to the secretary.

Midland Bank plc

FINANCIAL CALENDAR 1989

Dividend payments	May and October
Interest payments	
7½% Subordinated Unsecured Loan Stock 1983/93	30 June and 31 December
10¼% Subordinated Unsecured Loan Stock 1993/98	30 June and 31 December
14% Subordinated Unsecured Loan Stock 2002/07	31 May and 30 November
Half-yearly results announced	August
Annual general meeting	27 April

CHAIRMAN'S STATEMENT

I am glad to report that the 1988 pre-tax profit for the Group stands at £693m, its highest ever level and 36% above the comparable figure (ie before tax and exceptional item) for 1987. This result reflects a substantially improved contribution from almost all our businesses. The excellent results from Midland Montagu are particularly gratifying in the light of the difficult conditions that have prevailed in many capital markets.

These overall results have been achieved after the creation of a further £112m of provisions against loans to developing countries (compared with £111m last year). We believe that in current circumstances these provisions are adequate although there are, of course, many uncertainties.

I am pleased to report that our capital position continues to strengthen. In relation to the internationally agreed 'convergence' capital standards, Midland Group's ratio of 11.8% compares well with the internationally agreed minimum of 8%. A revaluation of the Group's UK properties resulted in an addition of £203m to the existing revaluation surplus, bringing the total surplus for the Group to £457m. Subject to approval at the annual general meeting, a two-for-five scrip issue is proposed which will capitalise about £220m of that surplus. Under the new international capital standards this will have the effect of further improving the composition of our capital base.

During the year progress was made towards achieving a number of the Group's objectives. The cost/income ratio improved from 73.0% to 70.8% and by a greater amount if we eliminate the distorting impact of The Thomas Cook Group. The return on shareholders' funds, after tax, reached 15%, a considerable improvement on the levels achieved in recent years. In spite of the large increases in the share capital in 1987 following the rights issue and the subscription by The Hongkong and Shanghai Banking Corporation, earnings per share at 75.1p were only marginally lower than in 1986.

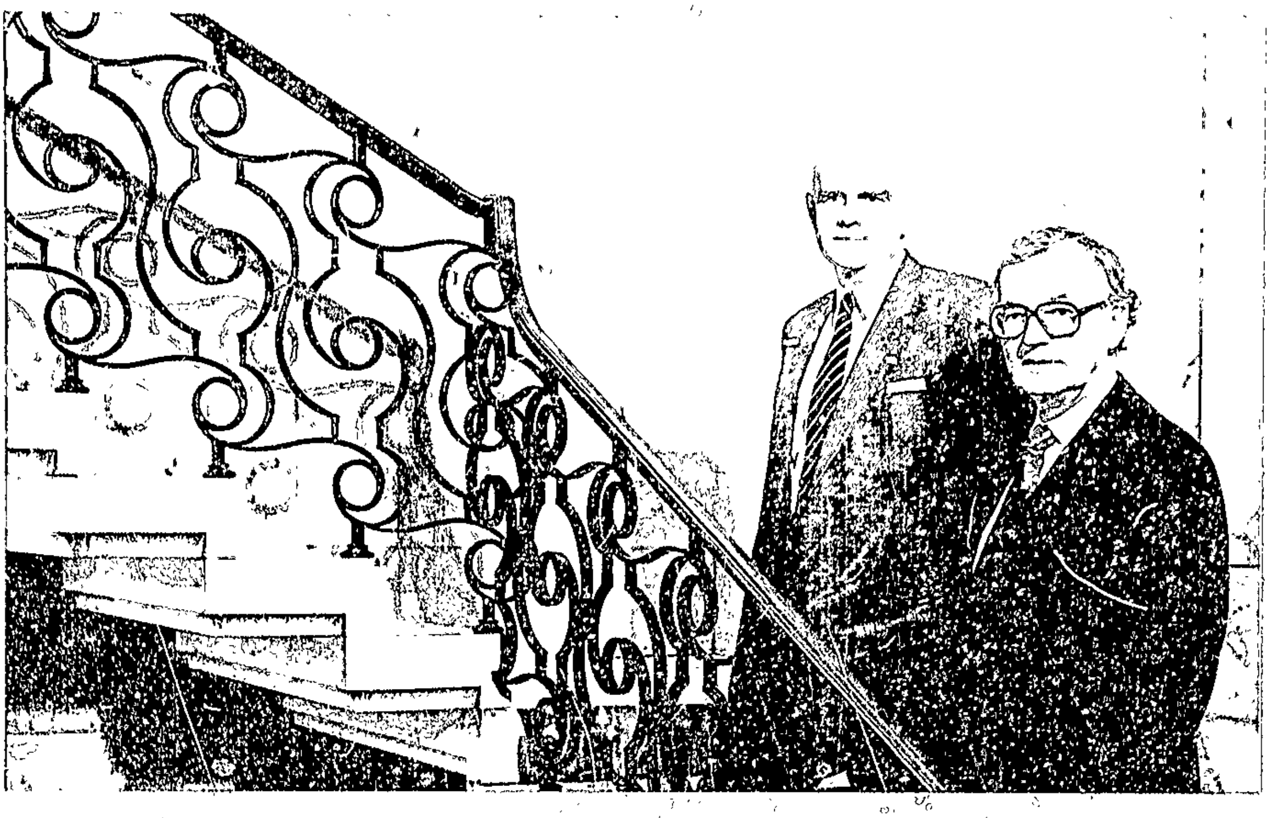
As a result of these overall improvements, the board of directors has been pleased to declare a second interim dividend of 13.5p, taking the total dividend for the year to 23.0p per share, an increase of 14.4% over last year's payment when the latter is adjusted for the rights issue.

The greatly improved profitability of the Group is reflected in the retained earnings of £286m which, at 11% of opening shareholders' funds, provide the platform for continued internally-generated growth.

A detailed explanation of the Group's results can be found in the Financial Review on pages 26 to 34.

The environment in which we operate

Over the past year we have operated in an increasingly challenging environment. In our traditional domestic markets, the forces of



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competition grew even fiercer. Perhaps the most dramatic example has been the move, led by the building societies but followed by ourselves and the other clearing banks, to the payment of interest on current accounts. But it was manifest in most product lines – such as house mortgages – and most customer groupings – from the multinational company to the corner shop – as a large range of financial institutions battled for market share. Naturally this has meant pressure on margins.

In the wholesale markets, the continuing effects of de-regulation and the excessive number of players in particular markets have proved challenging, while the perception of widespread opportunities for mergers and acquisitions has been a positive factor.

Internationally, markets have been volatile and particularly difficult to forecast. The potential for large banks and security houses to use their size aggressively has been increasingly demonstrated. In Europe, all businesses have had the task of assessing how best to take advantage of the coming single market. In Latin America, progress in solving domestic economic problems and stabilising or reducing the debt overhang has been mixed at best.

However, in one very important respect, conditions have been better than expected. Following the stock market collapses in October 1987, and largely as a result of concerted official action, economic activity in the major countries has, far from faltering, expanded strongly.

Looking ahead, I cannot see the conditions at home or abroad becoming any less difficult or demanding. Most of the competitive forces seem likely to continue unabated and the economic climate may well prove less benign. In the UK, the anti-inflationary policies which the authorities are committed to pursue are hardly likely to succeed without at least initial adverse effects on the business climate.

Abroad, the US twin deficits, whether or however the US authorities tackle them, are likely to have wide-ranging effects on interest rates, exchange rates and business activity generally.

In 1988 our efforts were directed towards putting Midland Group in a strong position to tackle these various challenges in the time ahead. The effort will be a continuing one as it will take some time to put ourselves where we want to be. But I am pleased with the progress we have already made.

The cost base

The cost base is the most fundamental issue for a large clearing bank with delivery mechanisms – most notably an extensive branch network – built up under completely different economic and competitive circumstances. It is crucial for us to provide, deliver and process our products and services at a low comparative cost. Traditional methods of cost-containment and cost-reduction, however vigilantly and single-mindedly they are pursued, are unlikely to be adequate to handle a problem of the magnitude faced by Midland and its peer banks. We need to alter radically the ways in which we carry out our business; this we are engaged in doing.

In last year's report I devoted considerable space to the major thrust we were making in information technology (IT). This has continued in 1988 when we spent £315m on numerous ways to rationalise procedures, improve the efficiency of support services and enhance the quality of the services we give our customers. Examples will be found later in the report.

But we have now gone further. Building on the success already derived from the better management and control of IT we have taken a number of important steps towards centralisation and rationalisation of operations as a whole. Group Operations was formed under the leadership of main board director Gene Lockhart and last spring successfully put together the back offices of all our wholesale and capital market businesses (then still carried out in two separate sectors).

Towards the end of the year we launched a far-reaching programme aimed at ultimately taking the processing out of our branches and putting it in a dozen centres across the country. We are starting with cheque clearing and hope to have

40% of cheque volume processed in these centres by the end of 1989. We have now decided that responsibility for all the operations activities of UK Banking is to be progressively assumed by Group Operations. I am confident that these moves will mean a substantial reduction in our unit costs over the next two to three years.

Serving customers better

If a low cost production and delivery mechanism is one essential prong of a strategy for tackling over-competition in commodity businesses, differentiation of the product and precise focus on the customer is the other.

In retail banking we have taken considerably further the development of branded accounts which combine a number of conventional banking products designed to appeal to particular, defined groups of people. And we have continued the major programme to convert our branches into modern, effective sales outlets.

We have achieved substantial success in reversing a decline in our market share of the middle corporate market through a dedicated approach, involving relatively few but well-trained people, operating from 63 corporate banking centres across the country, with an average of one computer terminal per person and virtually no paper at all. In personal financial services we are not yet as far advanced, but we have made a good start and are looking to achieve much-improved results in 1989.

In card services, whose production and sales we have centralised, probably the most important development has been the Switch point-of-sale debit card, developed with National Westminster Bank and Royal Bank of Scotland. Here we have followed a different approach from our principal competitors, based on detailed collaboration with the retailers. The reaction of major retailers has been very positive and the speed of installation of Switch terminals very gratifying.

In serving our large corporate, banking and institutional clients we have adopted an approach unique in the UK. In the summer of 1988, we combined our traditional commercial and international banking activities with our investment banking sector to form, under the name of Midland Montagu, a fully-integrated wholesale banking sector, able to meet all the needs of our large clients, from treasury products, through money transmission services, merchant banking and all forms of short and medium-term financing, to long-term export finance. Through the development of the relationship manager concept we aim to provide coherent, efficient, imaginative and fast services to all our large UK and overseas clients.

In the securities markets we have been encouraged by the improvement of Greenwell Montagu Gilt-Edged's already strong position. While the UK government bond market is currently declining and over-populated, we intend to develop an international fixed interest capability from this and a number of our overseas operations.

Europe

Like others, no doubt, we have been analysing the prospects in the run-up to 1992 and beyond and developing our strategy for Europe. The broad outlines of this are now clear.

With the purchase of a controlling interest in Euromobiliare in Italy and the acquisition or absorption of a number of HongkongBank's European branches, we believe we now have a stronger pan-European wholesale banking presence than any other British bank. Our policy, followed without exception in each continental country, is for our operations to be deeply embedded in the local markets: staffed almost entirely by local nationals, often locally quoted with local minority shareholders and often with their own distinctive names and traditions, as, for example, in the cases of Trinkaus & Burkhardt and Euromobiliare. We aim to coordinate further, but not centralise, these operations and in this way to provide unrivalled merchant banking and wholesale banking services across Europe for our customers.

Relations with HongkongBank

Our agreement with HongkongBank has progressed well. Substantially all of its continental European subsidiaries and branches have now been integrated into the Midland Group network, or closed; a comparable rationalisation has taken place in Asia where we have slimmed our own activities in favour of HongkongBank. In North America, Midland Bank Canada was sold to HongkongBank and amalgamated into HongkongBank of Canada.

This geographical rationalisation has, as already indicated and as intended, enabled us to concentrate on developing our presence in Europe while, at the same time, offering us the possibility, through joint business referrals, to gain over time many of the advantages of a major global bank without having to spread our financial and managerial resources over too wide an area.

In 1989 we intend to develop our relationships further through a programme of cross-secondments and mutual business referrals. In this context I see John Brooks' membership of both boards as very important. He is intending to spend considerable time in both centres and devote his efforts to developing closer relationships between the two Groups.

Developing countries

In 1988, the progress of debt-rescheduling countries was mixed. Mexico and Chile, among others, made real progress. On the other hand, there was a clear deterioration in Argentina.

During the summer of 1988 we saw the need to manage our exposure to the rescheduling countries with more focus and we set up Developing Countries Division. The division's objectives are to reduce our exposure to these countries and to convert parts of the loan portfolio, where value is potentially more volatile and at greater political risk, into more readily marketable and collectable assets. The problems faced vary widely and require an equally varied and individual response.

Board changes

The past year saw a number of changes in our board of directors. Hervé de Carmoy, who was director and chief executive of Global Banking, resigned to become director and chief executive of Société Générale de Belgique. In the ten years he was with us Hervé's energy and flair greatly improved our international operations, especially in France and Germany. The Group as a whole is also indebted to him for the quality of management he has helped provide for us through far-sighted recruitment and training. We are grateful to him for all his contributions and wish him every success in his important new role.

We also said goodbye to a number of our non-executive directors: Sir Trevor Holdsworth, now president of the Confederation of British Industry; Ian Hay Davison, following his appointment as chairman of Credit Lyonnais' subsidiary CL-Alexanders Laing and Cruickshank Holdings; and Kenneth Barker, upon his retirement from the board of HongkongBank. My thanks go to them all for the valuable service that each gave to the Group.

George Loudon, chief executive of Midland Montagu, joined the board during the year, as did Peter Wrangham, a director of HongkongBank. Sir Colin Marshall, chief executive of British Airways, is to join the board on 14 April.

On 14 February 1989, John Brooks was appointed a non-executive director of HongkongBank. At the same time we announced that on 30 April he would be relinquishing his executive duties at Midland though remaining a non-executive director. We thank him for the enormous contribution he has made to the Group over 40 years; but it is not yet time for a full appreciation of his services since we are looking to him, as a director of both Groups, to play a further important role for us in the development of the strategic relationship between our Groups.

Major Group appointments

John Brooks is to be succeeded as deputy group chief executive by Brian Goldthorpe. Michael Fuller succeeds Brian Goldthorpe as chief executive of UK Banking; Rodney Baker-Bates succeeds Michael Fuller as deputy chief executive of UK Banking; and Ian Mullen succeeds Rodney Baker-Bates as UK Corporate Banking director. Gene Lockhart, chief executive, Group Operations, has expanded responsibilities including UK Operations, Group Property and

Group Corporate Planning. He also becomes deputy chairman of The Thomas Cook Group. To all of these go our warm congratulations and good wishes.

Midland's social responsibilities

So far I have discussed business and organisational issues, but I do not want to close without saying something about how we see our wider responsibilities. I should like to mention, in particular, three areas where we are especially proud of what we are doing.

First, I am pleased at the significant role played by the Group in helping the highly successful Wishing Well Appeal for the redevelopment of Great Ormond Street Hospital to reach its £42m target one year ahead of schedule. We helped this appeal in many ways; through our role as banker to it, through secondments and Group donations and through countless individual money-raising activities by our staff.

Secondly, we continued during the past year to concentrate our charitable efforts on support for the rebuilding of the inner cities, particularly through the encouragement of small business and through helping unemployed and disadvantaged young people.

We are active sponsors of numerous initiatives to these ends such as the National Disabled Student Games, the National Association of Boys' Clubs' Fitness Scheme, and the Metropolitan Police Five-a-side Youth Football Competition.

Thirdly, we have demonstrated our commitment to do everything within our power to help iron out the disparity in attitude and opportunity existing between men and women, both within Midland Group and in the wider community.

Three of our major sponsorships in the past year were of the Midland Bank guide to 'Women and Money'; the exhibition 'Out of the Doll's House', a chronology of women's emancipation in the UK; and the booklet 'Daycare Trust: a Parent's Guide to Survival'. We have taken a widely-welcomed lead in plans to establish creches throughout the country to facilitate the return to work of those parents who have left to care for young children.

We are still not making the most of the potential of the women we employ; but there has been progress and we are determined to do much more. We have appointed an equal opportunities director to ensure that the potential of women in the Group is fully realised, and that our recruitment and subsequent treatment of people from all sections of the community, including ethnic minorities and the disabled, are even-handed. The introduction during 1988 of improved benefits and pension arrangements for part-time staff was another step towards complete consistency of treatment of staff members.

Staff

Our heartening progress during this past year has been achieved against a background of remorseless change, both within and without the organisation, which has placed heavy demands on all our staff. We have carried out a number of initiatives to help them with the challenges they have faced. We are stepping up training of all kinds, the spend on which is planned to increase by over 40% and will reach £30m during 1989.

We have set in place a programme of payment linked to performance for all staff at management level.

But I know it has been a difficult year for many of our staff and I am grateful for the quality and enthusiasm of the response that everyone has shown. The continued need to improve our shareholder value in an increasingly competitive environment is bound to mean that 1989 will be equally demanding. But I am confident the response will be equally positive. All of us are heartened by growing signs of improvement, not only in our financial performance, but in the way in which we are perceived by our customers, our competitors, and by the community as a whole.

In this way success can breed success; and we intend that it will continue to do so.

Kit McMahon

Sir Kit McMahon
Chairman and group chief executive

GROUP ACHIEVEMENTS & DEVELOPMENTS

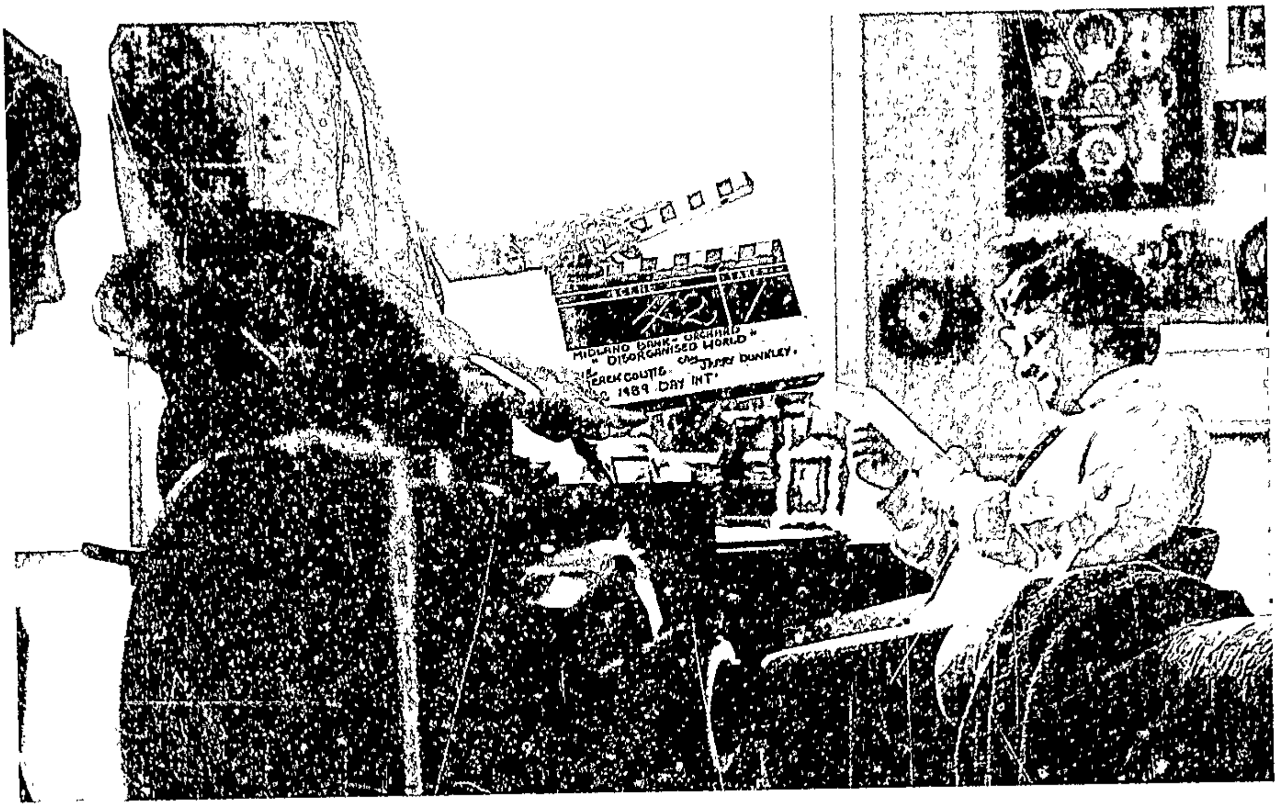
UK Banking

UK Banking earned significantly more in 1988 than in 1987 without any increase in staff numbers. There were many noteworthy developments, among which the following may be singled out.

- A national retail sales conference at the Birmingham National Exhibition Centre was held for the first time in April 1988, as a vehicle to communicate a new strategy direct to over 2,500 front line staff in UK Banking.
- A retail sales director was appointed to develop and coordinate the sales activities carried out across the whole of the UK network.
- Investment in training was sharply stepped up with new courses giving greater emphasis to selling skills and to personal development. The LEAP programme, a voluntary scheme of self-instruction, was introduced. Participants are able to choose from a wide variety of topics, ranging from management and selling skills to banking and finance knowledge. To date, over 21,000 out of 43,000 employees of UK Banking have joined the scheme.
- Over 20,000 employees have now attended the two day attitudinal Putting Customers First programme. Additionally, a great deal of effort is being placed on management training.
- As part of the push to demonstrate that it is an active equal opportunities employer, the Bank is committed to provide a widespread creche service, and a number will be opened during 1989. Anne Watts has been appointed Group equal opportunities director.
- The Midland Collection – a wardrobe of integrated clothing – was introduced for all staff throughout the retail network in 1988. In 1989 this will be extended to regional and area staff. The collection has been an unqualified success, appreciated by staff and customers alike.
- The network has been restructured by simplifying reporting lines and increasing delegated authorities, providing a better service for business customers.
- The branch refurbishment programme has been continued, progressing well on the way towards the target of 430 branches in the new retail image over a 3-5 year period.
- At the same time, the number of branches open for longer hours has been extended to 160. There will be 300 such branches by June 1989.
- 1988 was the year in which computerisation was extended beyond its traditional role of transaction-processing to tackle the more complex clerical functions and to press forward towards the fully-automated office. This process will be continued at an accelerated pace in 1989.

Product branding

Midland has chosen to distinguish its name and its products from the competition by a system of branding. Groups of products which best meet the needs of each market segment are


MIDLAND BANK - ORCHARD
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packaged together in the expectation that customers will associate themselves with the product ranges.

Three brands, each encompassing a different combination of services, have been created with particular retail customer profiles in mind.

The Orchard brand is intended for a householder, married with young or school-age children, whose salary is paid regularly into an account.

Such customers normally try to manage their mortgages and other commitments carefully, so that the accounts rarely go overdrawn.

Meridian is aimed at more mature individuals possessing quite substantial means. Such customers may be retired, with a grown-up and independent family. They are likely to be houseowners, probably with very low mortgage commitments, and will certainly have widespread savings and investments.

Vector users are likely to be younger, may be single or married, but in any case are very confident about their relationship with the bank. They see it as entirely normal to overdraw their accounts.

A fourth brand, Credo, has been designed for small businesses.

At the beginning of 1989 additional features, in the form of multiservice accounts, were launched under each of the personal product brand names.

Orchard and Meridian are attractive for people who rarely overdraw, in that the accounts carry no charges and pay highly competitive credit interest rates. The Vector account pays interest on credit balances and, in addition, gives flexibility to overdraw for a fixed monthly fee.

The Bank has also recently introduced a new Visa card, Midland Indigo, subsequent to becoming a full member of the Visa International payments system. The card is being offered to the public as a component of the Meridian and Vector multiservice accounts, and also as a stand-alone product.

Personal financial services

The introduction of a branding policy has been accompanied by the establishment of Midland Personal Financial Services (MPFS). Based upon an amalgamation of Midland Bank Insurance Brokers, Midland Bank Trust Company and Midland Unit Trusts, this is a dedicated team specialising in a range of personal investment and insurance products falling particularly under the Meridian brand.

Midland Life, a joint venture with Commercial Union in the provision of pensions and life assurance, and the increased range of unit trust portfolios, have shown excellent results in comparison with the activities of competitor organisations. Already Midland ranks among the major providers of pensions – 20,000 have been sold in the six months that Midland Life has been operational.

MPFS's manner of operation, relying on very close collaboration with the staff in the branches and dependent upon them for operational support, helps to spread the sales ethos across the whole of the network.

In consequence of the Financial Services Act, Midland Bank Insurance Brokers was formed as an independent intermediary to provide advice and sales service for non-Midland products.

The medium-sized corporate market

Over the past two years, Midland has changed fundamentally the way it manages its relationships with medium-sized companies in the UK.

Sixty-three corporate banking centres have been established to cover the country and are staffed with personnel trained to understand the needs of this sector of the market.

They are equipped with the latest technology, to make possible a much quicker analysis of, and response to, lending propositions.

Meetings between relationship managers and their clients occur regularly, and usually at the office of the client. The companies benefit from specialist skills being brought very much more closely to bear upon their particular requirements.

The resultant increase in volumes of business transacted has been very encouraging.

The centres rely on support from the 2,000 retail branches for all transaction processing; the same kinds of benefit derive from the close relationship between centre and branch as those pertaining to MPFS.

Asset finance

All areas of business of Forward Trust Group (FTG), Midland's asset finance subsidiary, grew in 1988. FTG is self-contained operationally, but works closely with retail and corporate sectors to provide comprehensive financial packages for a wide variety of customer requirements. During the year, two acquisitions were made. Concord Leasing (UK), previously owned by HongkongBank, continues to trade under the same name and has helped to place FTG amongst the market leaders in vendor and sales aid leasing programmes. The business of Comfort Finance, purchased from RTZ and absorbed into FTG, has augmented the Group's point of sale consumer credit activity.

Both acquisitions made a positive contribution to the growth in earnings of the Group.

Griffin Factors, which is part of FTG, celebrated its silver jubilee in July. It achieved record levels of new business turnover during the year, and of profit.

Cost saving and technology

Increases in volume and income bear out the fact that a new marketing approach and the efforts made across UK Banking to heighten its image are meeting with marked success. Activity on the sales side, though, represents only half the profit equation. Delivery systems and product development involving advanced technology must also keep a step ahead of the market; cost, reliability and product range are the critical variables. Significant developments are outlined in the following section on Group Operations.

Group Operations

The newly-formed Group Operations has the task of making the Group one of the lowest-cost producers of financial services. Really significant savings derive only from radical changes in the way that routine transactions are processed. Such changes are being applied throughout the branch network, in Midland Montagu, in head office functions, and at the interfaces between all three.

The procedures for transaction handling are being examined at every stage. The Group is making a heavy investment in new technology and constant attention is being paid to ensure that as new products are developed to satisfy the changing market place, so the systems for production and delivery also evolve.

A number of measures have already been introduced to remove back-office processing from branches and relocate it in regional centres. The effect will be to reduce the volume of paper in the network and to free up space within the branches so that it can be dedicated to customer service. Other improvements during 1988 include a 15% expansion of, and improvements to, the cash dispenser network, and the launch by Midland, National Westminster and Royal Bank of Scotland of Switch, a major new card scheme. The Switch debit card enables customers to pay retailers for goods and services electronically, without the need to write cheques or carry cash. Major retailers are committed and it is anticipated that by mid-1989 ten million consumers could be carrying cards bearing the Switch logo.

Automation processes have had a major impact on branches, area and corporate offices. During the year 1,100 new-generation IBM personal computers were installed and many more are planned in the coming months. They provide not only word processing capability but also an automated lending support system and will be the vehicle for major improvement in our information systems. An immediate benefit has been a swifter response to customer proposals. Five hundred retail branches now benefit from having counter terminals for cashiers. Additionally, the central despatch of plastic cards and the creation of a central mortgage processing unit have both released branch staff from traditional chores and allowed them to spend more time on business-generating activity.

Preceding the creation of Midland Montagu out of what were previously Investment and Global Banking Sectors, the complex task of combining two entirely separate operations functions was achieved within a very short period and with considerable savings in costs. Group-wide, improved computer systems have achieved a real reduction in cost while handling a 45% increase in volume.

The continuing objective is to provide a high level of service at the lowest possible cost.

Midland Montagu

A major development for the Group in 1988 was the integration of the Investment and Global Banking Sectors into an enlarged Midland Montagu. This new sector is responsible for a wide range of activities; managing treasury and capital markets operations, merchant banking activities, international banking (including correspondent banking, trade finance, and the overseas network), relationships with the largest corporate and institutional clients, and sovereign country exposure.

Midland Montagu provides a comprehensive range of financial services to its clients, and supplements the Group's core activities provided to the retail network. In creating a single management structure, client needs are identified more quickly. Products and services previously managed in different sectors are delivered to clients more efficiently, not just in the UK but internationally. The strategy of concentrating on businesses offering long-term profitability is beginning to pay off.

This last year saw the implementation of the Group's agreement with HongkongBank. Details of progress made thus far under the agreement appear later in this report, on pages 16 to 18. These developments have permitted a further concentration of strategy on expanding Midland Montagu's already strong presence in Europe, and on its growing activities in the principal financial centres of New York, Tokyo and Sydney.

Treasury

At the very core of Midland Montagu are its treasury activities. This business is an important contributor to the Group's overall asset and liability management and had an extremely successful year in the management of the Group's interest rate risk. Foreign exchange trading profits increased considerably over 1987 and Midland Montagu remains one of the largest market makers in London. During the year the treasury sales activities were substantially enhanced.

Securities

The international debt securities markets remained intensely competitive and the Group turned to its domestic strengths in the international network for further expansion.

In the UK, Greenwell Montagu Gilt-Edged (GMGE), a leading primary dealer in UK government bonds, almost doubled its market share. GMGE was also made a money market dealing counterparty of the Bank of England. Midland Montagu's Interest Rate Protection Instrument Trading team had an excellent year as clients sought to minimise the impact of rising interest rates.

Trinkaus & Burkhardt in West Germany performed strongly in the DM market and was rated fifth in the new issue league table, while in Australia, Dominguez Barry Samuel Montagu maintained its position as leader in the domestic fixed interest market.

Midland Montagu Securities Inc, the Group's US primary dealership, after an unprofitable year in 1988, is being transferred to New York, where it will be coordinated with other financial market activities.

With leading positions in the capital markets of the UK, West Germany and Australia along with its US primary dealership, Midland Montagu developed a multicurrency approach, serving the Group's worldwide investor and borrower clients.

Merchant banking

Midland Montagu's merchant banking activities consist of the Corporate Finance and Specialised Financing Divisions of Samuel Montagu, of venture capital and asset management. Profitability remained extremely satisfactory in 1988.

Samuel Montagu's Corporate Finance Division had another successful year. The most notable of the 134 transactions completed were the £2.5bn offer for sale, on behalf of HM Government, of British Steel, the


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largest primary issue in the UK in 1988; the £732m acquisition of Pleasurama by Mecca Leisure and the US$2.6bn acquisition of Macmillan by Maxwell Communication Corporation.

Samuel Montagu's Specialised Financing Division continues to top the sterling syndicated debt league tables, providing successful and imaginative financial packages. During 1988, four of these packages involved the arranging of underwritten debt in excess of US$1 bn each.

Midland Montagu Ventures, 'The Venture Catalysts', had an excellent year with growth in continental Europe, the USA and the UK. 43% of its new investments were based in the North of England, Scotland and the West Midlands.

Midland Montagu Asset Management is building on its established team of professional fund managers and is attracting new business in its target markets. Access to the Group's client base will play an important role in the future.

In merchant banking, additional benefits are expected to be derived from closer cooperation with other parts of the Group and the various international, especially European, merchant banking units. Improved access to the Group's balance sheet is ensuring the quick execution of complex transactions.

Corporate banking

A prime beneficiary of the enlarged sector is Midland Montagu Corporate Banking, which had a very satisfactory year. With responsibility for the relationship management of the largest corporate and institutional clients, Midland Montagu Corporate Banking liaises closely with all areas of the Group, providing its customers with a broad range of commercial and investment banking products and services, and travel facilities. It also acts as a conduit to the overseas corporate banking network. Organised in industry-based teams, the corporate bankers use a deep understanding of their customers' operations to meet their often complex needs. A number of major financings have been arranged during 1988, including a £500m Multiple Option Facility for Cable and Wireless which was managed jointly with HongkongBank.

International

Drawing together the overseas operations under a single management structure reinforced the Group's existing strengths in continental Europe, the US, Japan and Australia. Operating results from all these activities were quite satisfactory. Of particular significance was the positive contribution of Midland Montagu Securities' Japanese business against the background of only a handful of profitable foreign-owned securities houses.

At the end of 1988 Midland Montagu completed the acquisition of a 45% stake in, and effective management control (and therefore consolidation as a subsidiary) of, Euromobiliare, a leading Italian merchant bank. This complemented the Group's already extensive European network described in the feature, Midland in Europe, on pages 22 to 25 of this report and further expanded its range of merchant banking skills on the continent.

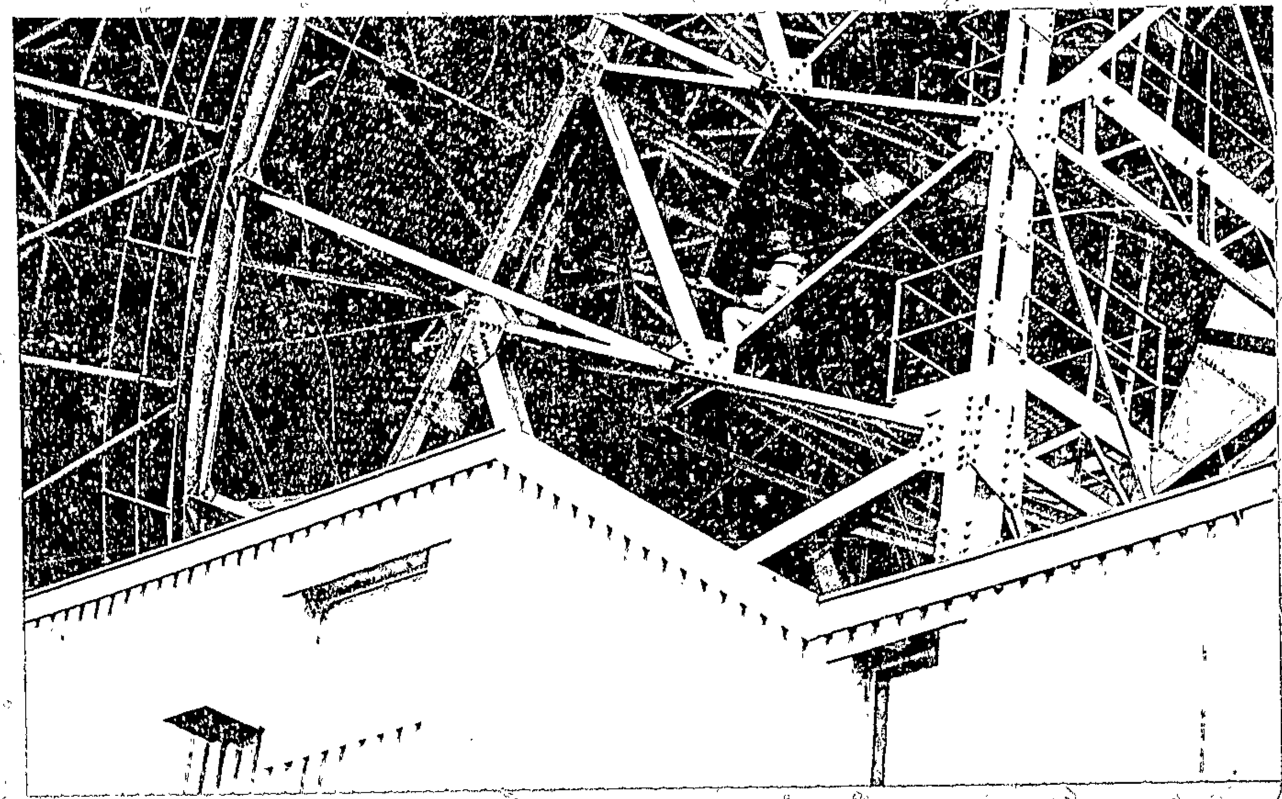
This network provided some very satisfactory results. In particular, the Greek and Spanish branches developed commercial and merchant banking businesses, resulting in a very profitable year. The major subsidiaries in France, West Germany and Switzerland continued to provide solid profit performances during 1988.

Both Correspondent Banking and Midland Montagu Trade Finance (MMTF) had an excellent year.

Relationship with HongkongBank

Following the agreement made with HongkongBank at the end of the previous year, considerable progress was achieved during 1988 in the rationalisation of areas of overlapping business activity, principally on a geographical basis. This has enabled Midland to reduce its operating costs in Asia and North America and to concentrate on the development of its presence in Europe.

In Europe, Trinkaus & Burkhardt, Midland's subsidiary in West Germany, opened a branch in Hamburg to take over HongkongBank's operation and also absorbed the mainstream business of HongkongBank's Frankfurt branch. Similarly, in Switzerland, Handelsfinanz Midland



Samuel Montagu were advisers to HM Government and sponsors of the largest-ever
United Kingdom flotation of an industrial company – British Steel. British Steel
was valued at £2.5 billion. Shares were offered and fully subscribed in the
UK, USA, Canada and Japan, and successfully placed in continental Europe.

Bank opened a branch in Zurich to take over HongkongBank's business there. HongkongBank's Amsterdam branch was taken over by Midland and the business of the Madrid branch absorbed within Midland's existing Madrid operations. In January 1989, HongkongBank's Dublin branch was taken over by Midland. In the Channel Islands, HongkongBank's branch in Jersey was closed and a substantial number of its customer accounts have transferred to Midland's branch in Jersey or to Midland Bank Trust Corporation there.

In the UK, HongkongBank's London-based export credit and project finance departments, including the confirming house subsidiary Wardley Export Finance, have been merged within Midland Montagu Trade Finance. The integration of the operation included the transfer to Midland Montagu of a team of executives previously with James Capel Bankers. As mentioned earlier, HongkongBank's UK asset finance subsidiary, Concord Leasing (UK), was acquired by Forward Trust Group in July. Midland also now handles HongkongBank's sterling clearing business and the majority of its property management needs in the UK.

In Asia, Midland sold its branch in Seoul to HongkongBank and closed its branch in Singapore, transferring the domestic business in those centres to HongkongBank. In their place, Midland Group representative offices have been opened to take advantage of the cross-border and export finance opportunities that arise. In Singapore and Hong Kong, the corporate finance teams of Samuel Montagu have been integrated within those of Wardley, HongkongBank's merchant banking subsidiary. More recently, agreement has been reached with HongkongBank for the establishment in Singapore of a joint venture with Midland Bank Aval, the Group's forfaiting subsidiary.

In North America, Midland Bank Canada was sold to HongkongBank in May and has been amalgamated with HongkongBank of Canada.

During the course of 1988, many other areas of potential cooperation have been discussed with HongkongBank, with the objective of utilising the two Groups' respective resources, expertise and customer bases to build profitable new business opportunities, particularly in those areas where, jointly, a significant global capability exists.

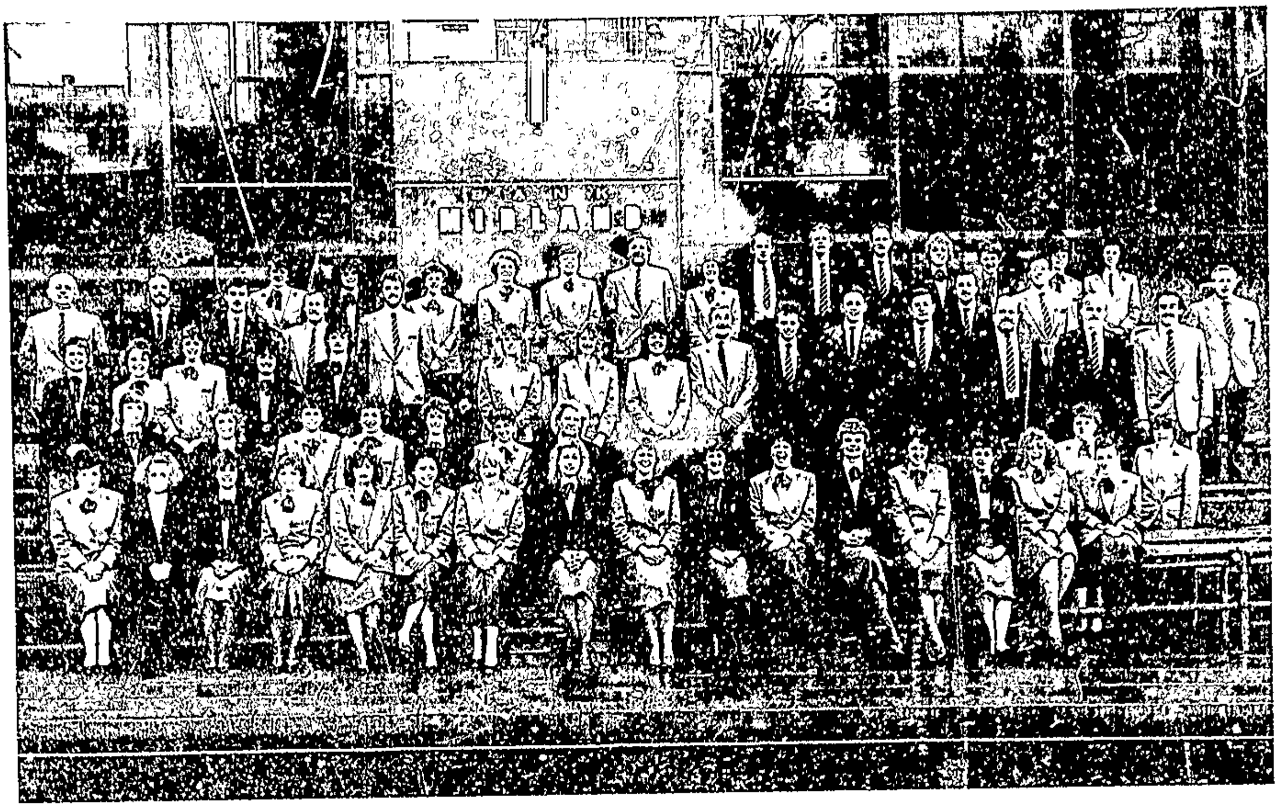
The Thomas Cook Group

1988 marked the beginning of an era for The Thomas Cook Group (TCG), one of the great names in worldwide travel. New top management, together with a number of the existing executive team, began to set in place a far-reaching strategy. This aims at regaining the position of Thomas Cook as a world leader in the travel-related service business, one of the few certain medium-term growth industries.

Particular attention is being paid to a number of business areas. Travel management services for large corporations, and travel services for small businesses are seen as a priority. Leisure sales are to be aimed at middle and upper income individuals, increasingly through direct marketing channels. Thomas Cook's worldwide network is being structured and staffed to meet the demands of its own customers and those of other organisations in need of contract service. Last but not least, expansion of the travellers cheque business, in which Thomas Cook is the leading participant outside North America, continues apace.

Performance in 1988 was excellent. Profit growth took place in virtually all regions of the world and 56% of profits were generated outside the UK. Travellers cheques achieved a 16% increase in sales and significantly increased profitability. Other factors contributing to the improvement were the closure of unprofitable business, including UK short-haul tour operations and foreign money operations in the Middle East and the west coast of the USA.

In early 1989 a 10-year agreement was negotiated with Pergamon AGB in respect of Thomas Cook Travel Inc (TCTI). TCTI is a US travel agency business using the Thomas Cook name under a franchise agreement. TCTI was sold by TCG in 1985 as part of the arrangements dictated by the US Federal Reserve Board in



connection with Midland Group's development in the US. The agreement will provide TCG with guaranteed franchise income and a much greater control over the use of the Thomas Cook name, and the worldwide service standards associated with it.

Compliance

A major piece of investor protection legislation, the Financial Services Act, came into effect in April 1988. It requires the authorisation of all investment businesses in the UK; nearly twenty such authorisations have been obtained for the Group. Even though Midland has always prided itself on maintaining the highest standards, a considerable investment was needed in order to implement the new regulatory requirements. Maintenance of effective compliance procedures also involves considerable ongoing costs.

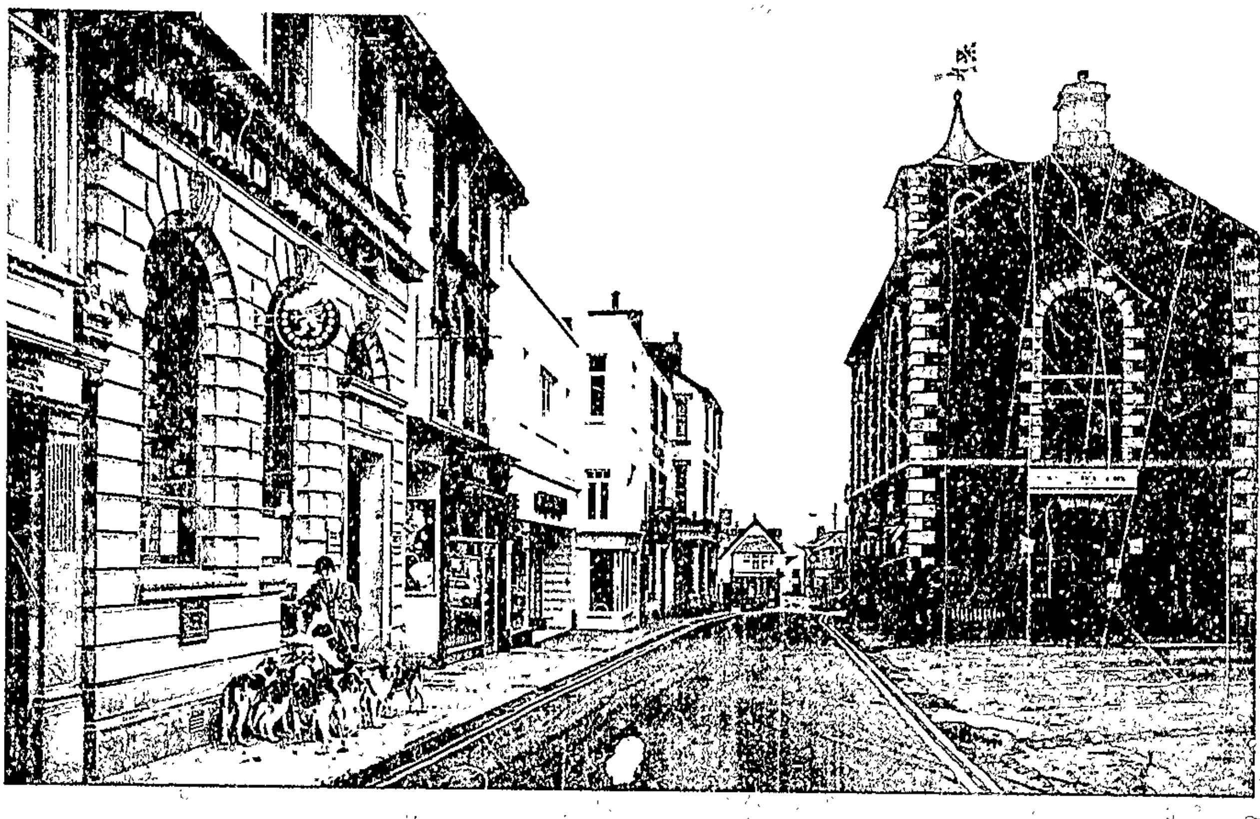
Whilst Midland supports fully the objectives of the new regulatory regime and is committed to making them work effectively, there would seem to be scope for fine tuning of its requirements so that costs are reduced and legitimate business is not inhibited. With this in mind, considerable effort has been made to encourage the regulators to improve and simplify their rules.

Staff

The factor common to all this progress has been the need to help staff adapt to the rapid pace of change, and to engender an enthusiasm in them for the steps that are being taken.

This is being achieved in two ways. The first is through a tremendous investment in training. New courses have been launched giving priority to customer service, to selling skills, and to coping with the additional burdens of compliance and, most importantly, with the advanced technology which is being introduced as a tool in every facet of the business. The emphasis placed on effective communication between all levels of staff has been increased still further and employees are encouraged strongly to contribute to product development, quality of service and cost containment initiatives.

Video and computer-based communications and training materials have played an important part in the process. Underpinning all this is a continued commitment towards payment linked to performance.



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MIDLAND IN EUROPE

Midland is deriving an increasing proportion of its non-UK revenues from its broad and established coverage while providing a growing range of services to UK and indigenous customers throughout Europe. Based on a long tradition of specialisation and service, the Group in Europe is able to provide its customers with local understanding of the individual national marketplaces in which it is established, together with the increasing benefits of membership of a unique merchant banking network.

Introduction

Midland Group's long tradition in the financial markets of Europe provides a powerful base from which to extend its network and the range of services it offers to its customers.

1988 has seen significant developments in the Group's European coverage, highlighted by the acquisition of a controlling interest in a major Italian merchant bank, Euromobiliare, and the absorption into the Group of HongkongBank's branches in Hamburg, Amsterdam and Madrid.

The Group aims to provide, through its branches and subsidiaries in Europe, a merchant banking, private banking and asset management service for corporate, institutional and wealthy personal clients.

The Group's European coverage now extends across both European Community and EFTA member states; the network consists of specialised banks in West Germany, France and Italy, quoted on their respective stock exchanges, together with Group subsidiaries and branches in a further ten countries.

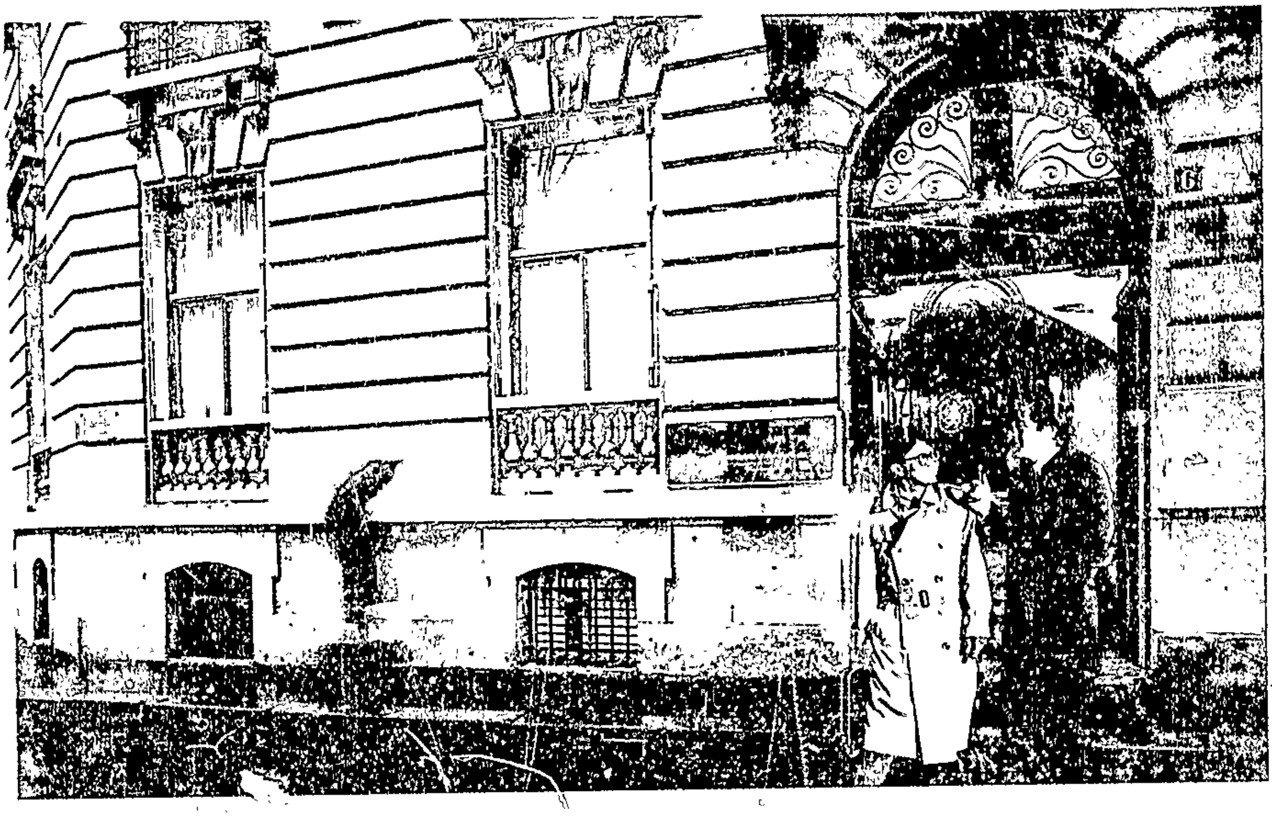
All these operations are active participants in their own domestic corporate markets. There is continuing effort, not only to build upon existing local reputations, but also to promote regular dialogue between the European centres so that corporate customers in each country have access to high quality services in every market in which the Group operates.

West Germany

Trinkaus & Burkhardt (TuB), a majority-owned subsidiary of the Group with a stock market capitalisation of about DM 750m, is one of the oldest and largest private banks in West Germany. It was founded over 200 years ago and obtained a listing on the German stock exchanges in 1985. Its five domestic branches, as well as subsidiaries in Luxembourg and Zurich, were augmented during 1988 by the addition of a branch in Hamburg from HongkongBank. Its main business focus is on corporate and institutional banking, private banking, money markets and capital markets. TuB enjoys a reputation for its market-making expertise in German securities and foreign exchange and for its first-class service to larger companies and individuals. It can justifiably claim to be one of Germany's premier professional private banks, while also serving the German banking needs of the Group's international customers.

France

Midland Bank SA (MBSA), a majority-owned subsidiary, with a stock market capitalisation of about Fr Frs 870m, is the Group's French 'banque d'affaires'. It is a commercial and merchant bank engaged in institutional, investment and personal banking, as well as foreign exchange, money market and domestic capital market operations and is also involved in real estate and financial asset management.



The bank in its current form was created in 1983 from the integration of the Group's French interests, to become the country's largest foreign-controlled bank with a full stock exchange quotation. MBSA, through its strategy of concentrating on selected specialist areas in a rapidly-changing financial environment, has been able to adapt quickly in its high-priority markets. MBSA plays a key role in meeting the banking requirements in France of the Group's UK and international customers.

Switzerland

In Switzerland, Midland is represented through separate, specialist institutions in the federation's principal cities. Handelsfinanz Midland Bank, majority-owned by the Group and based in Geneva with branches in Zurich and Lugano, specialises in commercial as well as private banking services; Guyerzeller Bank AG, also majority-owned, headquartered in Zurich with a branch in Geneva, concentrates on private investment management; and Samuel Montagu (Suisse) SA in Geneva, wholly-owned by the Group, is an active underwriter and distributor of Swiss Franc debt securities.

Italy

The acquisition at the end of 1988 of a controlling interest in one of Italy's leading investment banks, Euromobiliare, based in Milan and a member of the Milan stock exchange, with a stock market capitalisation of Lit 190bn., has greatly extended the Group's presence in Italy and its ability to provide a full range of investment and merchant banking services. The Group is also represented by its Milan branch, opened in 1985, which provides commercial banking and treasury services to Italian and multi-national corporate customers.

Spain and Greece

Madrid branch was founded in 1981: it offers a wide variety of wholesale banking services and was prominent in establishing the Spanish commercial paper market.

Athens and Piraeus branches, also established in 1981, comprise one of the leading foreign banking presences in the Greek market. Group activities in Greece were extended in 1988 by the acquisition of a minority interest in Alpha Finance and Advisory Services SA, a corporate advisory and venture capital specialist.

The branches in both Spain and Greece are increasing their activity in the provision of merchant banking services.

Netherlands and Ireland

In 1988, the Amsterdam branch of HongkongBank was transferred to Midland followed, in January 1989, by HongkongBank's Dublin branch.

The Nordic countries

The 1980s have seen the establishment of the Group's unique Nordic network, more extensive than that of any other foreign banking group.

In 1982, Montagu & Co AB was established as a corporate finance and domestic money market and securities house in Sweden, with the Group holding a 40% stake, increased to 100% in February 1989. This evolved into Midland Montagu Bank AB, the only UK-owned Swedish bank.

1985 saw the opening of Samuel Montagu AS (now Midland Montagu AS), the only UK-owned bank operating in Norway, which provides a range of investment, merchant banking, money market and foreign exchange services to institutions and corporate customers. In 1987, Sundal Collier became a wholly-owned subsidiary of Midland Montagu AS. This company specialises in stockbroking and is active in both equity and debt securities.

Foreign exchange, treasury and stockbroking services are provided in Finland by Midland Montagu Osakepankki, founded in Helsinki in 1986.

Each of the Group's operations in Stockholm, Oslo and Helsinki is a member of its respective local stock exchange.

Midland's major European subsidiaries and branches – date of establishment

1785
C G Jaegar founded a trading banking house (later C G Trinkaus) in Düsseldorf

1836
Midland Bank founded

1841
Burkhardt & Co founded in Essen

1853
Samuel Montagu & Co founded

1894
Guyerzeller Bank founded in Switzerland

1952
Handelsfinanz Bank established in Zurich

1957
Zurmont Bank established in Switzerland by Samuel Montagu

1959
Guyerzeller Bank and Zurmont Bank merged to become Guyerzeller Zurmont Bank – majority-owned by Samuel Montagu

1963
Midland was a founder member of the European Advisory Committee, a strategic union of banks from major European countries

1972
C G Trinkaus and Burkhardt & Co merged to become Trinkaus & Burkhardt

1978
Midland Bank France SA founded

1979
Midland acquired a controlling interest in Banque de la Construction et des Travaux Publics in France

1980
Midland acquired a controlling interest in Trinkaus & Burkhardt

1981
Midland opened a branch in Madrid
Midland opened branches in Athens and Piraeus

1982
Carnegie-Montagu & Co AB (now Midland Montagu Bank AB) established in Stockholm, Midland Group holding a 40% interest
Midland acquired a majority interest in Handelsfinanz Bank, Switzerland, now named Handelsfinanz Midland Bank

1983
Midland Bank SA, a majority-owned subsidiary, was established in France out of a restructuring of all the Group's French operations

1984
Samuel Montagu (Suisse) SA established in Geneva

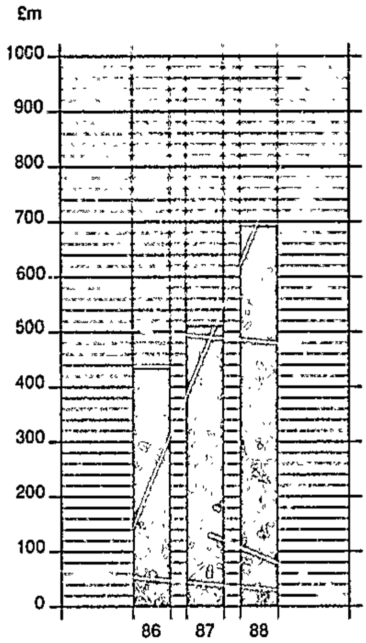
1985
Midland opened a branch in Milan

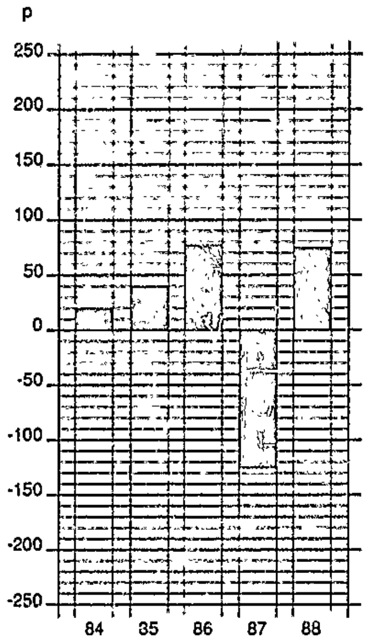
1986
Samuel Montagu AS (now named Midland Montagu AS) opened in Oslo
Midland Montagu Osakepankki established in Helsinki

1987
Midland, through Midland Montagu AS, acquired stockbrokers Sundal Collier of Oslo, now operating as Sundal Collier Montagu AS

1988
Midland, through Trinkaus & Burkhardt, took over the Hamburg branch of HongkongBank
Midland took over the Amsterdam branch of HongkongBank
Midland assumed control of Euromobiliare in Milan

1989
Midland took over the Dublin branch of HongkongBank
Midland acquired 100% of Midland Montagu & Co AB in Stockholm
Midland Montagu Bank AB was authorised to commence operating in Stockholm





PROFIT & LOSS ACCOUNT

Group profit before taxation (and exceptional item)

(figures in £m)	1986	1987	1988
UK Banking	294	432	509
Midland Montagu	7	44	173
Developing Countries Division	51	(27)	(3)
Thomas Cook	13	11	14
	365	460	693
Clydesdale/ Northern Banks	47	51	-
Crocker	22	-	-
Group	434	511	693

(1987 figures exclude the exceptional provisions of £1,016m)

Profit before tax (and exceptional item) for the Group rose by 35.6% in 1988 to £693m. When adjustment is made for:
- the share capital raised in 1987
- the sale of Clydesdale/Northern Banks
- major non-recurring items

the underlying improvement was about 20%.

There was a strong performance from the UK-based businesses reflecting rapid growth in volumes in UK Banking and substantially improved performance by Midland Montagu's treasury and securities businesses.

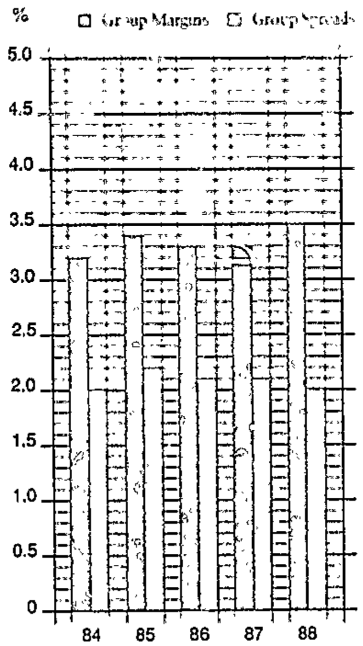
Developing Countries Division is reported separately for the first time in 1988. It was previously in Global Banking Sector, which was merged with Investment Banking Sector during 1988 to form an enlarged Midland Montagu.

Earnings per share

	1984	1985	1986	1987	1988
Average shares issued (m)	308	309	311	365	548
Earnings (£m)	62	122	242	(456)	412
Earnings/(loss) per share (p)	20.2	39.4	77.5	(125.3)	75.1

Group earnings have recovered strongly in 1988 from the substantial loss incurred in 1987, following the exceptional provisions of £1,016m against loans to developing countries.

More significantly, 1988 earnings are 70% above their 1986 level. At 75.1p per share, however, earnings per share are still slightly lower than was achieved in 1986. This reflects the higher level of share capital in the Group after the rights issue in September 1987 and the subscription by HongkongBank for new shares in December 1987. The impact of these share issues is mirrored in the very much stronger capital ratios reported at end-1987 and end-1988.



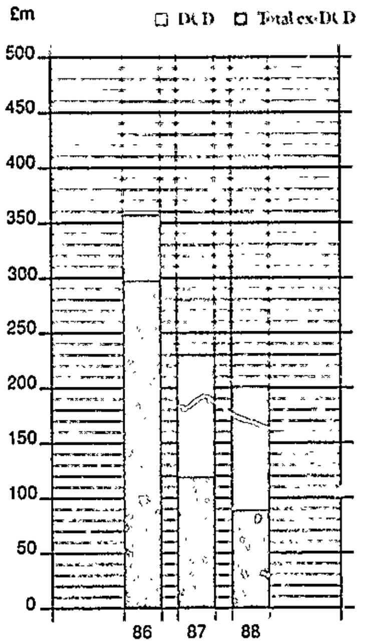
Net interest margins and spreads

	1984	1985	1986	1987	1988
Net interest margin (%)					
Domestic	5.7	5.7	5.2	5.3	4.9
International	2.2	2.3	2.0	1.6	2.2
Group	3.2	3.4	3.3	3.3	3.5
Net interest spread (%)					
Domestic	3.3	3.4	3.3	3.6	3.1
International	1.5	1.5	1.3	0.8	1.0
Group	2.0	2.2	2.1	2.1	2.0

Group interest margins benefited from increased average shareholders' funds (33% higher than in 1987) and the continuation of the strong relative growth of higher margin domestic assets (up 22% on average excluding Clydesdale/Northern Banks) while lower margin international assets declined by 3%.

International margins improved as a result of the higher level of international provisions, created in 1987, which provide interest-free funding for international assets.

Group margins improved despite pressure on interest spreads, particularly in the second half of the year when competitive markets were combined with rising interest rates. Group international spreads were improved by reducing fine margin lending.

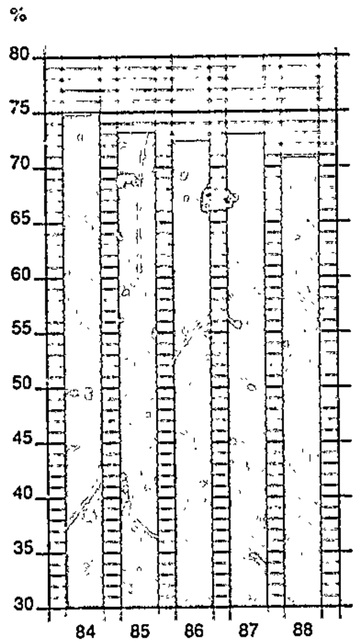


Charge for bad and doubtful debts

(figures in £m)	1986	1987	1988
UK Banking	83	62	51
Midland Montagu	142	20	35
Developing Countries Division	60	111	112
Thomas Cook Group	1	0	3
	286	193	201
Clydesdale/ Northern Banks	34	37	-
Crocker	37	-	-
Total	357	230	201

(1987 figures exclude the exceptional provisions of £1,016m)

The improving trend in corporate default, evident in recent years both in the UK and internationally, continued during 1988 as most major corporate customers achieved higher profitability and strong cash flow. Consumer and small business default was not a significant problem and despite the high UK interest rates from mid-year there were few signs of distress amongst personal house mortgage customers. International provisions in 1988 were reduced by recoveries of previous years' provisions as the economic health of a number of industry sectors, particularly energy and shipping, improved. Provisions against LDC loans are reviewed later as part of the review of Developing Countries Division (DCD).



Cost/income ratio

	1984	1985	1986	1987	1988
Operating expenses (£m)	2,151	2,073	2,007	1,985	2,024
Operating income (£m)	2,877	2,832	2,770	2,717	2,858
Cost/income ratio (%)	74.8	73.2	72.4	73.0	70.8

Adjusting for the sale of Clydesdale/ Northern Banks, growth in operating income was 16.0% and in operating expenses 11.2%, resulting in an improvement in the cost/income ratio.

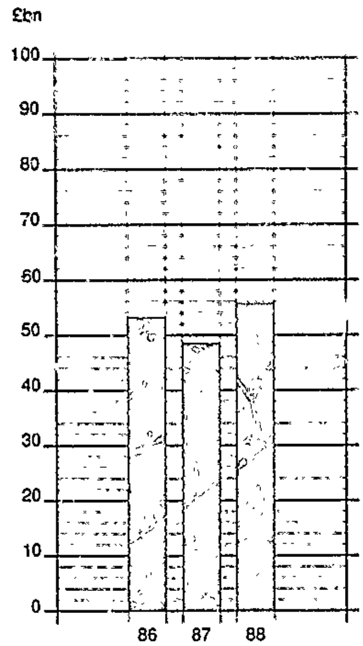
The comparison of the cost/income ratios between 1987 and 1988 is complicated by the inclusion of Thomas Cook (for which 14 months' results were consolidated in 1988). Travel services have an inherently higher cost structure than banking.

Excluding Thomas Cook, the comparable ratios are:

1987	1988
71.3%	68.2%

After allowing for the benefit of the increase in share capital the underlying improvement is 1.5%.

BALANCE SHEET

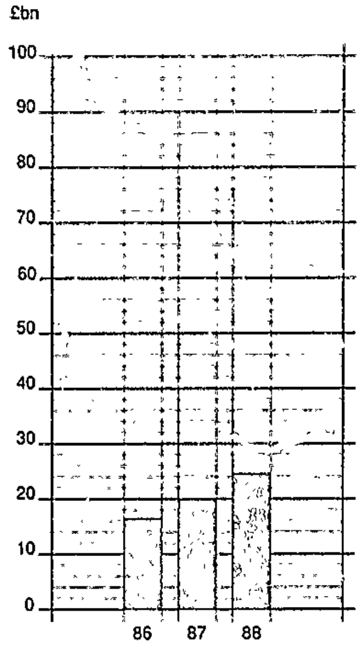


Group total assets
(period-end balances)

(figures in £bn)	1986	1987	1988
UK Banking	20.5*	19.9	24.6
Midland Montagu	27.2	25.0	27.2
Developing Countries Division	4.8	2.9	2.9
Thomas Cook	0.7	0.7	1.0
Total	53.2	48.5	55.7

*Includes Clydesdale/Northern Banks £4.0bn

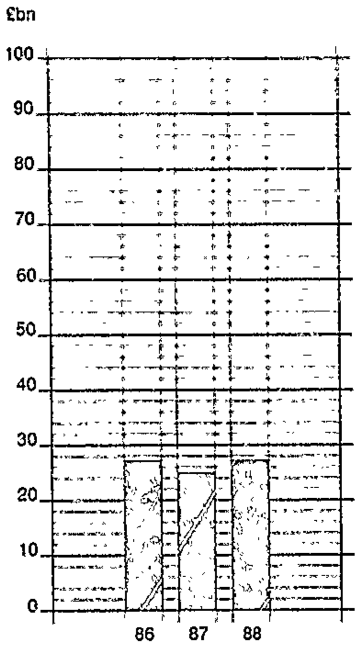
The Group balance sheet grew by 15% during 1988 with the major part of this growth coming from UK Banking (up 24% from 1987). Midland Montagu grew at a much slower 9%. Developing Countries Division achieved a static position in sterling terms and in the underlying currency of the business (US dollars) provisionable exposure fell by 3%.



Total assets in UK banking
(period-end balances)

(figures in £bn)	1986	1987	1988
Mortgage advances	2.7	3.6	4.5
Personal/corporate overdrafts	7.6	9.2	11.3
Other advances	4.4	5.1	6.1
Other assets	1.8	2.0	2.7
Total	16.5	19.9	24.6

In a fast growing UK economy, UK Banking's assets increased by £4.7bn (or 24%) in 1988. Mortgage advances grew most rapidly (25%) although much of this growth occurred in the first six months of the year. There was strong growth in corporate overdrafts and term loans, particularly in the middle market, and also, but to a lesser extent, in non-mortgage personal lending.



Total assets in Midland Montagu

(period-end balances)

(figures in £bn)	1986	1987	1988
Total assets	27.2	25.0	27.2

Overall, Midland Montagu's assets grew in 1988 by 9%. In the UK, the development of Midland Montagu's acknowledged strengths in UK wholesale markets meant that assets grew strongly. In Europe, although there was an increasing commitment of the sector to European markets, building on the Group's existing operations in Germany, France and Switzerland, a stronger sterling exchange rate and a reduction in the Group's involvement in the mortgage market in France led to no significant alteration in sterling asset levels. The consolidation of Euromobiliare, acquired in December 1988, added £0.4bn to the Midland Montagu assets. Growth in total risk weighted assets (including off-balance-sheet commitments) was a faster 11%, reflecting the increasing emphasis in Midland Montagu on off-balance-sheet markets in general and treasury/foreign exchange products in particular.

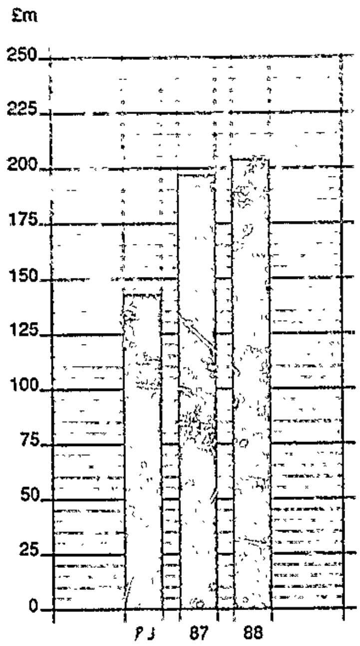
GROUP FUNDING MIX
(Based on average balances)

	1986 %	1987 %	1988 %
Demand deposits:			
Customer accounts			
– interest bearing	9	11	13
– non interest bearing	12	12	12
Money market (overnight and call deposits)	9	9	9
Time deposits:			
Savings accounts	13	9	7
Money market and other	43	42	42
Capital and other	14	17	17
Total	100	100	100

Group funding mix

During the year, the average funding mix remained substantially unchanged. Average balances on non-interest bearing customer accounts remained at 12% of total funding but this proportion was slightly lower in the second half of the year, reflecting rapid growth of the Group balance sheet and increasing competition for personal account business.

The established declining trend of time savings deposits (predominantly sterling 7-day deposit accounts) was continued but there was again a matching increase in high interest demand accounts. Taken together, there was little overall change in the proportion of customer savings in Group funding.



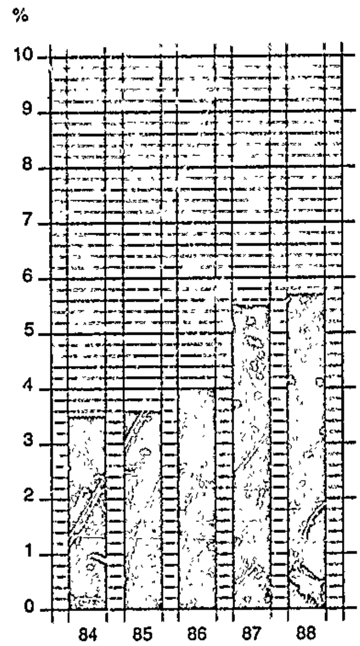
Group capital spending

(figures in £m)	1986	1987	1988
Property	52	[illegible]	83
Equipment	85	115	105
Other	6	9	16
Total	143	197	204

Capital expenditure on the Group's infrastructure, which increased markedly in 1987, was sustained in 1988. Expenditure rose by 38% in 1987 and by 2% in 1988 but this understates current spending as, at year-end, capital expenditure commitments were £109m (1987: £49m). Expenditure on premises increased as the programme of branch refurbishing and restyling gathered momentum. By the end of 1988, 105 major branches had been converted to the new retail image, along with many smaller refurbishments. In excess of 200 further major refurbishments are planned for 1989.

Equipment expenditure in 1988 reflects the impact of the drive to reduce costs and improve customer service through the provision of improved technology and its effective utilisation. A major programme for installation of networked personal computers began in 1988 and will continue during 1989.

CAPITAL ADEQUACY at 31 December 1988	
Capital ratios	%
Total capital/risk assets	11.8
Tier 1 capital/risk assets	6.5
Composition of capital	
Tier 1:	£m
Shareholders' funds and minorities (excl. property revaluation reserve)	2,723
Tier 2:	
Property revaluation reserve	457
General provisions	190
Perpetual subordinated debt	861
Subordinated term debt	945
	2,453
Unconsolidated investments	(214)
Total capital	4,962
Risk weighted assets	£m
On-balance-sheet	35,164
Off-balance-sheet	6,903
Total	42,067



CAPITAL ADEQUACY

Group capital

During 1988, the Bank of England, in line with international guidelines for capital adequacy agreed in Basle by the bank supervisory authorities of the Group of Ten countries, announced a new measure for the regulation of bank capital. The precise basis of implementation of these guidelines has still to be determined. The measure provides for two tiers of capital and applies differing risk weightings to asset categories. In contrast to earlier measures of risk assets, recognition is given to a wide range of off-balance sheet commitments.

At an estimated 11.8%, Midland Group's ratio is well in excess of the internationally agreed minimum of 8%. The new capital standards will be introduced for UK banks in 1989 and gradually for other countries in the period to end-1992.

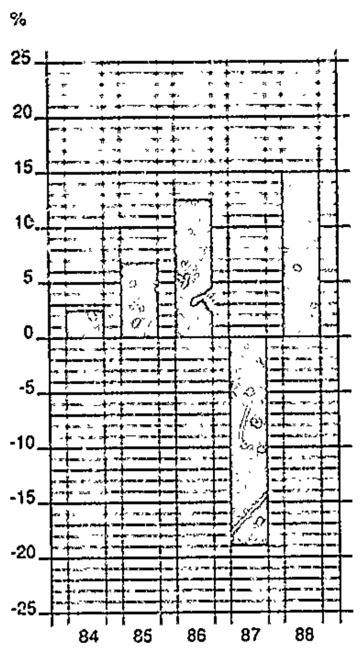
The effect of the proposed capitalisation of part of property revaluation reserves would be to increase the Tier 1 capital ratio from 6.5% to 7.0% within an unchanged total capital ratio.

Equity/assets ratio

	1984	1985	1986	1987	1988
Shareholders' funds and minorities (£m)	2,171	2,082	2,111	2,685	3,180
Total year-end assets (£bn)	61.5	58.1	53.2	48.5	55.7
Total equity to total assets ratio (%)	3.5	3.6	4.0	5.5	5.7

The Group's equity position remains very strong. Equity benefited from retentions of £286m, which, at 11% of opening shareholders' funds, is the highest level in the recent history of the Group. In addition, the quinquennial revaluation of the Group's UK properties added £203m to shareholders' funds. As a result, the Group's equity/assets ratio improved to 5.7% notwithstanding the 15% growth in total assets.

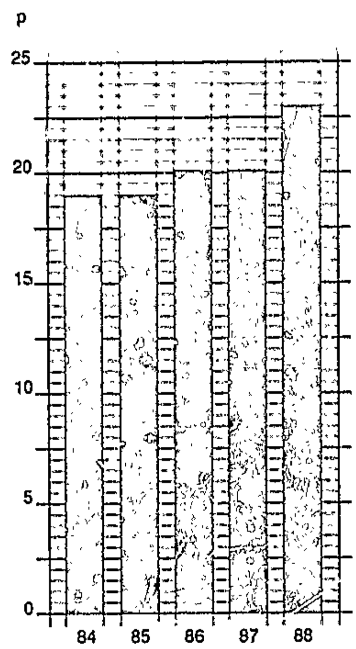
SHAREHOLDERS' RETURN



Return on shareholders' funds

	1984	1985	1986	1987	1988
Average shareholders' funds (£m)	1,792	1,798	1,938	2,074	2,748
Profit/(loss) attributable (£m)	45	122	242	(393)	412
Return on average shareholders' funds (%)	2.5	6.8	12.5	(18.9)	15.0

Improving the overall return on equity is central to achievement of the Group's objectives. During 1988, progress was made in this regard with Midland Montagu in particular increasing its return. At the same time, UK Banking has expanded its business considerably and now has 44% of total Group assets (1987: 41%). This business has historically yielded high returns and, although the intensity of competition in the main UK markets has lowered the average return on equity in 1988, the Group's overall return on shareholders' funds has benefited from the increased relative importance of UK Banking.



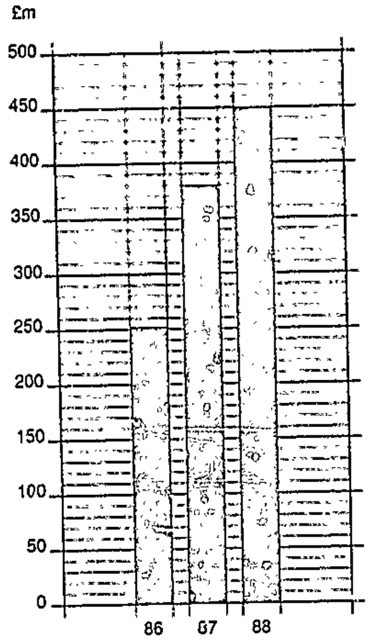
Dividend per share

	1984	1985	1986	1987	1988
First interim (p)	8.2	8.2	8.6	8.6	9.5
Second interim (p)	10.8	10.8	11.5	11.5	13.5
Total dividend per share (p)	19.0	19.0	20.1	20.1	23.0

(Figures have been adjusted for the 1987 rights issue)

Dividends increased by 14.4% in 1988 to 23.0p per share with dividend covered 3.3 times by earnings. With the increased number of shares in issue following the capital raising in 1987, the annual cost of dividend payments increased by 40% in 1988 from £90m to £126m.

INDIVIDUAL OPERATIONS



UK Banking (excluding Forward Trust Group) – Profit before taxation

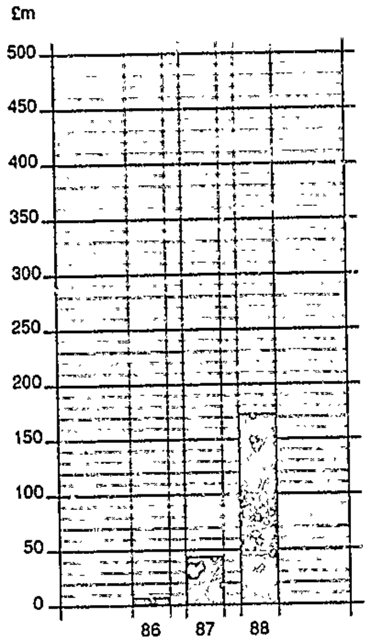
(figures in £m)	1986	1987	1988
Profit before taxation	252	380	449

1988 saw very substantial growth in the main product lines of UK Banking and this is reflected in a profits advance of 18% over 1987. A major part of this increase came in the first part of the year when the sector benefited from widening margins, funding costs falling more quickly than lending rates as Base Rate touched a low of 7.5%.

In contrast, the second half of 1988 has seen Base Rate rise sharply to 13% by year-end and the lagged effect on interest income has reduced margins, particularly on the mortgage book.

UK Banking has not benefited directly from the high base rate environment since interest rate positions are managed by the Group's treasury, which forms part of Midland Montagu.

Total costs increased by 11%. Within this increase, high costs associated with the restructuring of operations, staff training and the promotion of new products were partially offset by a lower pension contribution rate. The underlying cost increase is approximately 7%.



Midland Montagu – Profit before taxation

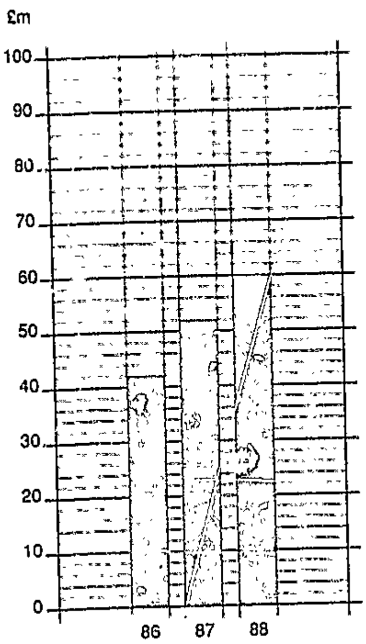
(figures in £m)	1986	1987	1988
Profit before taxation	7	44	173

All principal areas of activity showed profit improvements over 1987. Treasury and securities in particular had a very strong year, especially through profit improvements in its money markets activities. Although difficult market conditions existed in the securities markets worldwide, Midland Montagu overall achieved a positive contribution in this aspect of its activities in 1988.

In merchant banking, Samuel Montagu's corporate finance and specialised financing activities and venture capital had another good year.

The profit contribution from corporate banking increased strongly as a result of higher fee income and an improved level of bad debt recoveries.

In the international banking areas, correspondent banking and trade finance showed strong profit improvement over 1987 but results overall were affected by restructuring costs associated with US and Australian activities.



Forward Trust Group (FTG) – Profit before taxation

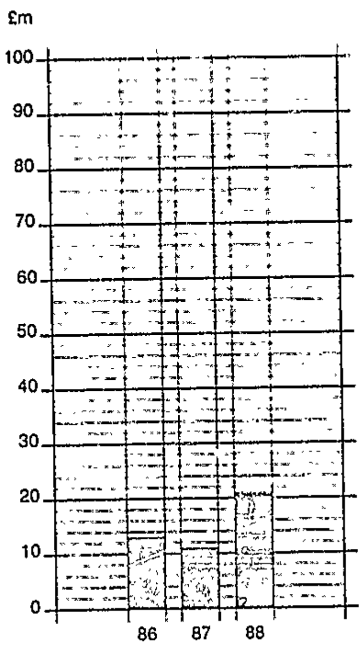
(figures in £m)	1986	1987	1988
Profit before taxation	42	52	60

Profits before tax in 1988 of £60m are 15% higher than 1987. The strong performance stemmed from the 23% growth of new business volumes, maintenance of margins and an improved cost/income ratio.

The Group's activities in leasing, instalment finance and factoring for industry all performed strongly, whilst bad debt and default remained at an acceptable level.

During the year, FTG purchased Concord Leasing (UK) from HongkongBank for £14m (total assets £225m). By merging FTG's similar business into Concord, the Group has created what is considered the largest specialist sales-aid leasing operation in the UK.

During the year, FTG made substantial progress towards its objective of increasing its consumer finance activities as a proportion of total business.



Thomas Cook Group (TCG) – Profit before taxation

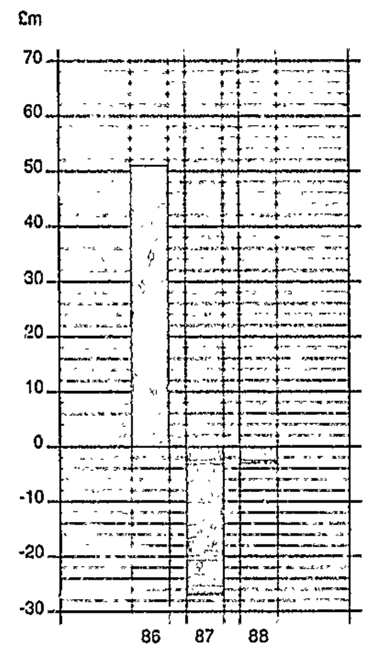
(figures in £m) 12 mths to 31 October	1986	1987	1988
Profit before taxation	13	11	21

(Midland Group accounts include profits of £14m for the 14 months to December 1988)

Profits before tax for the 12 months to 31 October 1988 rose to £21m (88% higher than for the 12 months to 31 October 1987). For 1988, the accounting period consolidated into Midland Group covered the 14 months to 31 December 1988, bringing TCG into line with the Group's accounting period end. The November/December period is traditionally a low point in the profitability of the highly seasonal travel industry and this change has depressed Midland Group profits by £7m.

Travellers cheque sales reached record levels in 1988 with strong performance in European and African markets while foreign money operations returned to profitability after a period of losses.

Additionally, there were withdrawals from products and markets where there were inadequate returns. For example, the shorthaul tour operations ceased during the period.



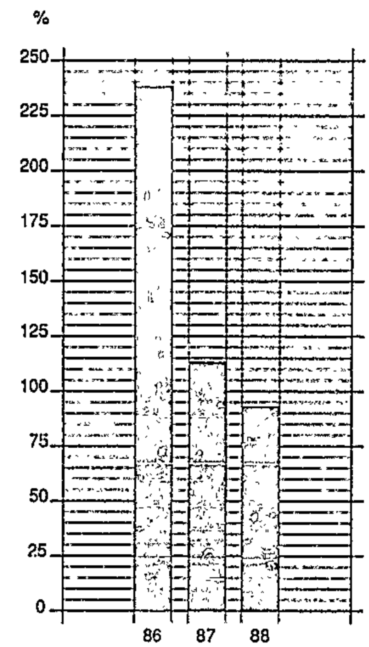
Developing Countries Division – Profit/(loss) before taxation

(figures in £m)	1986	1987	1988
Net contribution to trading profit	111	84	109
Charge for bad and doubtful debts	(60)	(111)	(112)
Profit/(loss) before taxation	51	(27)	(3)

(1987 figures exclude the exceptional provisions of £1,916m)

This division was formed to allow the Group to develop a more closely focused approach to the management of loans to developing countries.

These loans are predominantly US dollar denominated and during 1988 total provisionable exposure to such countries fell by 3% to US$7,521m despite new money, amounting to US$166m (£92m), provided to Brazil under a rescheduling agreement. In sterling terms, exchange rate changes meant that provisionable exposure increased by £42m.



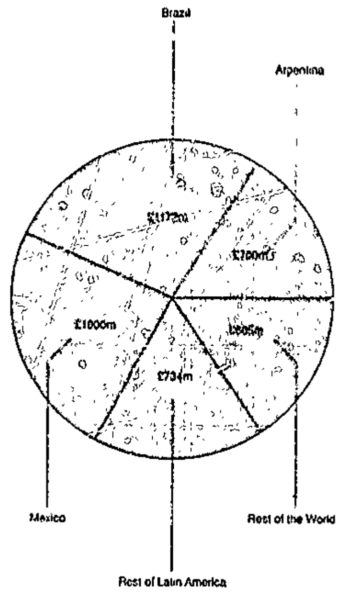
Developing country exposure as a proportion of shareholders' funds

	1986	1987	1988
Provisionable exposure (£m)	5,112*	4,134	4,176
Provisions (£m)	300	1,206	1,363
Net provisionable exposure (£m)	4,812	2,928	2,813
– as a % of shareholders' funds	238%	113%	93%

*Gross outstandings – provisionable exposure not available for 1986

Total provisions increased by £157m in 1988, reflecting net new provisions of £112m and £45m through the impact of exchange rate changes on the sterling translation of dollar provisions. At end-1988, total provisions represent 32.6% (1987: 29.2%) of provisionable exposure. Of the new provisions raised in 1988, £96m reflects the economic difficulties of Argentina, which have led to a significant level of arrears of interest (£46m reserved in 1988) and an increase of £50m in provisioning against principal.

Smaller increases in provisions have also arisen in respect of other countries. In part, these charges have been offset by the receipt of interest due from Brazil and reserved in 1987.



Analysis of developing country exposure (gross outstandings)

	1987	1988
Gross outstandings	$7,745m/ £4,140m	$7,692m/ £4,271m
Provisionable exposure	$7,734m/ £4,134m	$7,521m/ £4,176m

In determining the level of overall provisionable exposure to countries with payment difficulties, contingencies and undrawn commitments are recognised as provisionable while secured or voluntary short-term outstandings are not. Previously, Group exposure was indicated by reference only to gross outstandings. Provisionable exposure provides a more meaningful basis for assessment of the Group's developing country debt portfolio.

CONTENTS OF THE ACCOUNTS

Midland Bank plc

BOARD OF DIRECTORS

Chairman and group chief executive
Sir Kit McMahon*

Deputy chairmen
Sir Alex Jarratt CB
Sir Patrick Meaney
The Rt Hon Sir Michael Palliser GCMG

Directors
J A Brooks*
E W Brutsche*
Sir Kenneth Corfield
T J Cunningham
Sir Archibald Forster
B L Goldthorpe*
H E Lockhart*
G E Loudon*
G Maitland Smith
D O'Cathain OBE
Sir Eric Pountain DL
W Purves CBE DSO
I N Tegner*
P J Wrangham

Secretary
J R Skae

**Executive directors*

Group executive committee

Group chief executive
Sir Kit McMahon

Deputy group chief executive
J A Brooks

Chief executive, UK Banking
B L Goldthorpe

Chief executive, Group Operations
H E Lockhart

Chief executive, Midland Montagu
G E Loudon

Deputy chief executive, Midland Montagu
E W Brutsche

Director, Group Finance
I N Tegner

Group personnel director
G P White

Secretary
J R Skae

Sir Kit McMahon
Age 61 – appointed a director and group chief executive in 1986 and became chairman in 1987. Formerly deputy governor of the Bank of England. He is a director of The Hongkong and Shanghai Banking Corporation and Eurotunnel.

Sir Alex Jarratt CB
Age 65 – a director and a deputy chairman since 1980, he is chairman of Smiths Industries, a deputy chairman of the Prudential Corporation and a director of ICI.

Sir Patrick Meaney
Age 63 – a director since 1980 and a deputy chairman since 1984, he is chairman of the Rank Organisation and a director of ICI and MEPC.

The Rt Hon Sir Michael Palliser GCMG
Age 66 – a director and a deputy chairman since 1987, he is chairman of Samuel Montagu & Co and a director of BAT Industries, Booker and Shell.

J A Brooks
Age 60 – joined Midland Bank in 1949 and was appointed a director in 1980 and deputy group chief executive in 1981. He is chairman of The Thomas Cook Group and a director of The Hongkong and Shanghai Banking Corporation and Mastercard International.

E W Brutsche
Age 51 – joined Trinkaus & Burkhardt in 1981. A director of Midland since 1986, he is deputy chief executive, Midland Montagu.

Sir Kenneth Corfield
Age 65 – a director since 1979, he is an experienced industrialist.

T J Cunningham
Age 46 – formerly the senior international adviser to Midland, he became a director in 1988. He is vice-chairman of Kissinger Associates and a director of P J Carroll.

Sir Archibald Forster
Age 61 – a director since 1986, he is chairman and chief executive of Esso UK and a director of the American Chamber of Commerce.

B L Goldthorpe
Age 55 – a director since 1983, he joined Midland in 1949 and [illegible] chief executive UK Banking and chairman of Forward Trust Group.

H E Lockhart
Age 39 – a director since January 1988, he is chief executive, Group Operations.

G E Loudon
Age 46 – a director since June 1988, he joined Midland from Amsterdam-Rotterdam Bank. He became chief executive of Midland Montagu in September 1988.

G Maitland Smith
Age 56 – a director since 1986, he is chairman of Sears and a director of Asprey and Courtaulds.

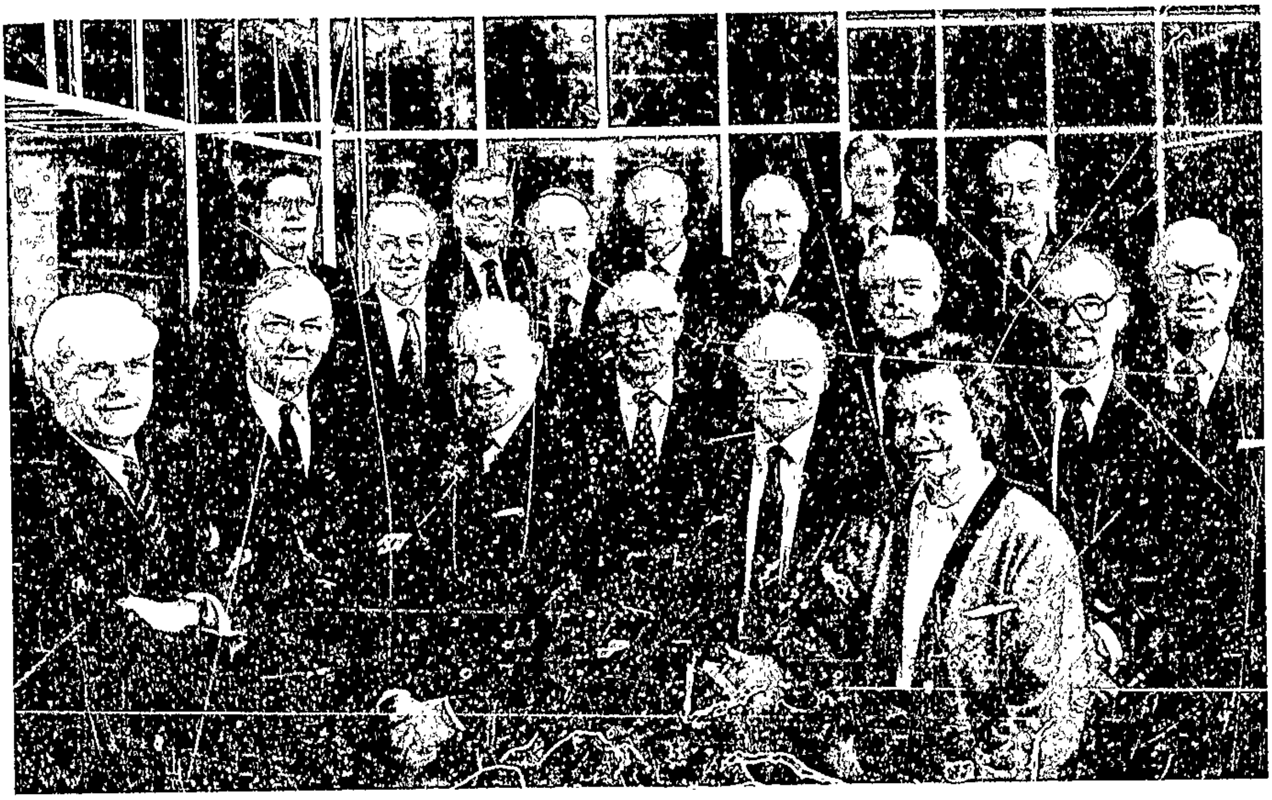
Miss D O'Cathain OBE
Age 51 – a director since 1984, she is a director of Sears and Tesco.

Sir Eric Pountain DL
Age 55 – a director since 1986, he is chairman of Tarmac and James Beattie and a director of IMI.

W Purves CBE DSO
Age 57 – a director since 1987, he is chairman of The Hongkong and Shanghai Banking Corporation and of the British Bank of the Middle East and a director of Marine Midland Banks Inc.

I N Tegner
Age 55 – joined Midland in 1987 as director, Group Finance. He was formerly finance director of Bowater Industries.

P J Wrangham
Age 54 – appointed a director in 1988, he is a director of The Hongkong and Shanghai Banking Corporation.



Left to right, front row: *JA Brooks, W Purv's, Sir Kenneth Corfield, Sir Archibald Forster, Miss D O'Cathain.*

Middle: *Sir Patrick Meaney, Rt Hon Sir Michael Palliser, Sir Kit McMahon, Sir Alex Jarratt.*

Back: *GE Loudon, BL Goulthorpe, EW Brutsche, KW Barker, Sir Eric Pountain,*

G Maitland Smith, HE Lockhart, IN Tegner.

REPORT OF THE DIRECTORS

Results for the year

The profit of the Group attributable to members of Midland Bank plc for the year ended 31 December 1988 amounted to £412 million and has been dealt with as shown in the consolidated profit and loss account on page 45.

A first interim dividend of 9.5p per share was paid on 10 October 1988. The directors have declared a second interim dividend amounting to 13.5p per share payable on 12 May 1989 in respect of 1988 instead of recommending a final dividend at the annual general meeting. The interim dividends total 23.0p per share (20.1p per share in 1987).

Group activities

The Bank and its subsidiaries, operating in the United Kingdom and in other parts of the world, provide a comprehensive range of banking, financial and related services.

Share capital

During the year the issued share capital of the Bank was increased from 546,626,383 shares to 549,587,734 shares as follows:

1,120,006 shares issued under the Midland Bank Group Employee Profit Sharing Scheme at £3.948 per share.

1,441,364 shares issued under the Midland Bank Group Employee and Executive Share Option Schemes at prices ranging from £1.9894 to £4.1971 per share.

399,981 shares issued in lieu of cash by way of scrip dividend in respect of the first interim dividend for 1988.

The Bank has been notified that The Hongkong and Shanghai Banking Corporation and its subsidiaries have a 14.9% interest in the share capital of the Bank. The Bank has also been advised that Hanson PLC and its subsidiaries and The Kuwait Investment Office have interests in the share capital of the Bank of 5.2% and 5.1% respectively.

The close company provisions of the Income and Corporation Taxes Act 1988 do not apply to the Bank.

Premises

The properties of the Group were revalued at 31 December 1988 and a surplus of £203 million is reflected in the accounts. This is more fully described on page 58 in note 18.

Special business at the annual general meeting

Shareholders will see from the notice of the annual general meeting that they are asked to consider and, if thought fit, pass a number of resolutions as special business, further details of which are as follows:

Resolution No 10: Scrip dividend scheme

At last year's annual general meeting, shareholders authorised the directors to offer the scrip dividend alternative in respect of dividends declared before this year's annual general meeting.

Over 16,000 shareholders and 5,000 members of staff participating in the Group's employee profit sharing scheme took advantage of the opportunity to receive shares instead of cash in connection with the first interim dividend paid in October 1988. Regrettably, many others were prevented from taking shares as a direct result of the disruption in the postal services. However, a similar arrangement will be available for the second interim dividend payable in May 1989 and shareholders will have received a separate letter about this. Those shareholders who wish to take shares rather than cash on a regular basis are being offered the additional facility of being able to complete a Scrip Dividend Mandate.

The scrip dividend alternative is attractive to many individual shareholders as it enables them to increase their shareholdings in a simple way without incurring dealing costs. Accordingly, the directors now seek shareholders' approval for the extension of the scheme to cover dividends declared before the annual general meeting to be held in 1990.

By voting in favour of the resolution shareholders are not committing themselves to a personal decision on whether to take shares or cash in respect of future dividends.

Resolution No 11: Capitalisation issue

As already announced, the directors have decided to propose a capitalisation issue out of the Bank's property revaluation reserves. Shareholders on the register on 7 April 1989 will receive two fully paid shares of £1 each for every five shares held. Shares allotted pursuant to valid elections to receive the scrip dividend alternative in lieu of the second interim dividend for 1988 will also rank for participation in the capitalisation issue. The maximum number of new shares to be issued in the capitalisation issue will be 227 million. Fractions of new shares will not be allotted to shareholders but will be aggregated and sold in the market. Proceeds of sale (less expenses of sale and distribution) will be distributed among shareholders in proportion to their respective entitlements, if any, except that sums of less than £2.50 will be retained for the benefit of the Bank. (In calculating fractions, entitlements arising in respect of shares held on 7 April 1989 will be aggregated with those arising in respect of elections to receive scrip dividend shares). Subject to shareholders' approval and admission of the new shares to the Official List of the International Stock Exchange, it is expected that (1) definitive share certificates in respect of those new shares to which shareholders are entitled by reason of their holdings on 7 April 1989 will be posted to shareholders on 27 April 1989 and dealings in those new shares will begin on 28 April 1989;

and (2) definitive share certificates in respect of those new shares to which shareholders are entitled by reason of valid scrip dividend elections will be posted to shareholders on 12 May 1989 and dealings in those new shares will begin on 15 May 1989. All the new shares will rank *pari passu* in all respects with the existing shares except that they will not participate in the second interim dividend for the year ended 31 December 1988.

The resolution proposes to increase the authorised share capital of the Bank from £750 million to £1,000 million by the creation of 250 million shares of £1 each and authorises the implementation of the capitalisation issue. The increase in the authorised capital will permit the capitalisation issue and the maintenance of a reasonable margin of unissued capital. Dependent upon the number of valid elections received in respect of the scrip dividend alternative to the second interim dividend for 1988, the Bank's authorised share capital remaining unissued after the capitalisation issue will be within the range of £205 million (20%) and £228 million (23%). No issue will be made which would effectively alter the control of the Bank without prior approval of shareholders in general meeting.

Resolution No 12: Authority of directors to allot shares
At last year's annual general meeting the directors were given general authority for five years to allot up to one third of the issued share capital. It is proposed that this general authority be rolled forward for a further period of five years. The maximum amount for which the authority is sought is up to £183,195,911 (representing one third of the Bank's issued share capital at 31 December 1988), or, if the capitalisation issue is approved by shareholders, £205,173,656 (representing the authorised but unissued share capital of the Bank immediately following the capitalisation issue).

Resolution No 13: Disapplication of pre-emption rights
It is proposed to ask shareholders to renew the power granted to directors at last year's annual general meeting to allot shares for cash within certain limits. If approved, this proposal would empower the directors to allot shares for cash provided that, except in a rights issue, the new shares did not exceed 5% of the issued share capital. The power would last until the next annual general meeting (or 26 July 1990, if earlier) except that, in relation to rights issues, it would last for five years.

The directors believe that the proposals in resolutions 12 and 13 would continue to provide the board with a prudent measure of flexibility for them to act in the Bank's interests.

Loan capital
During the year Midland International Financial Services BV, a wholly-owned Dutch subsidiary of the Bank, entered into an agreement for a loan of Japanese Yen 9.4 billion, of which Yen 6.3 billion had been drawn down at the year end. The loan is guaranteed by the Bank on a subordinated basis as to payment of principal and interest.

The proceeds of the loan will be employed in the conduct of the business of Midland Group.

Directors
The following directors have retired from the board:
Sir John Cuckney and Sir Derrick Holden-Brown in April 1988; Sir Trevor Holdsworth in June 1988; Mr I F H Davison in August 1988; Mr H P de Carmoy in September 1988 and Mr K W Barker in December 1988.

Appointments to the board have been made as follows:
Mr H E Lockhart in January 1988; Mr T J Cunningham in March 1988; Mr G E Loudon in June 1988; Mr P J Wrangham in December 1988 and Sir Colin Marshall in April 1989. In accordance with the articles of association of the Bank, Mr G E Loudon, Mr P J Wrangham and Sir Colin Marshall will retire at the forthcoming annual general meeting and, being eligible, offer themselves for re-appointment. Mr H E Lockhart and Mr T J Cunningham were re-appointed by shareholders at the 1988 annual general meeting.

Sir Patrick Meaney, Sir Alex Jarratt, Miss D O'Cathain and Sir Kit McMahon retire by rotation in accordance with the articles of association of the Bank and, being eligible, offer themselves for re-election.

Sir Kit McMahon and Mr G E Loudon have service contracts which expire on 6 April 1993 and 31 May 1993 respectively.

Sir Patrick Meaney, Sir Alex Jarratt, Miss D O'Cathain, Mr P J Wrangham and Sir Colin Marshall have no service contracts with the Bank or any of its subsidiaries.

Under the terms of a trust deed executed on 17 February 1989 one of the Bank's overseas subsidiaries purchased from Mr G E Loudon for a consideration of £395,000 one half of the beneficial interest in a residential property in London occupied by Mr Loudon. An independent firm of valuers has determined that the consideration payable for such interest was fair and reasonable.

No director had a material interest in any contract of significance, other than a service contract, with the Bank or any of its subsidiaries at any time during the year.

The names of the present directors of the Bank and brief biographical notes are shown on page 36.

Group audit committee and Group remuneration committee
At 31 December 1988 membership of these committees was as follows:

Group audit committee
Mr G Maitland Smith (chairman), Sir Archibald Forster, Miss D O'Cathain and Sir Michael Palliser.

Group remuneration committee
Sir Patrick Meaney (chairman), Sir Kenneth Corfield, Sir Alex Jarratt and Sir Michael Palliser.

Subsidiary Companies
The Group received £22.9 million in May 1988 upon the sale of its 100% interest in Midland Bank Canada (excluding Thomas Cook Canada) to HongkongBank of Canada.

In July 1988, Forward Trust Group Limited acquired the entire issued share capital of Concord Leasing (UK) Limited from Euroconcord Finance BV, part of The Hongkong and Shanghai Banking Corporation, for a cost of £14.4 million. Concord is principally involved in the provision of asset finance for commercial customers.

In December 1988 the Bank purchased approximately 42% of the ordinary share capital of Euromobiliare S.p.A. (the Company) for a consideration of £42.3 million. This increased the Group's shareholding to just over 45%. The Bank has also entered into an option agreement with management of the Company and management companies giving the Bank the option to purchase ordinary shares representing approximately 6% further shares in the Company. In addition, there is a management agreement between the Bank, management of the Company and management companies regarding the exercise of director and shareholder votes in the Company.

Greenwell Montagu Stockbrokers (GMS), a wholly-owned subsidiary of the Bank, purchased the whole of the issued capital of Smith Keen Cutler Limited (SKC), a stockbroking business, in April 1986. Part of the consideration given by GMS for the shares in SKC was the issue of loan stock to certain shareholders of SKC who were also SKC directors. All stockholders have the benefit of a Deed of Undertaking of the Bank under which they are entitled to sell their stock to the Bank from a specified date prior to maturity. During 1988 the terms of the Deed of Undertaking and the loan stock were varied by acceleration of the specified date and by fixing the variable element of the redemption value at an amount which could be up to £500,000 more than the original redemption value.

Employees
The full-time equivalent of staff employed in the Group at 31 December 1988, on a world-wide basis, was 59,093 of whom 53,375 were employed in the United Kingdom. The average number of staff employed (including part-timers) each week by the Group, in the United Kingdom, was 57,915 and their aggregate remuneration was £723 million.

Employee communication and involvement

United Kingdom
Midland Group has continued to show its commitment to effective communication between management and employees. Extensive use of video and computer-based communication and training materials has complemented our overall effort in these areas, and has encouraged employees to contribute directly to product development, quality of service, and cost containment initiatives.

While responsibility for day-to-day communication rests with line management, the Group regularly uses such media as the in-house Group newspapers and bulletin to keep all employees involved in strategic and tactical business decisions. A further review of the framework of management/employee communications will be conducted in 1989 to ensure that it remains fully effective and responsive to our changing business needs.

The employee share schemes were reviewed in 1988 and a revised Profit Sharing Scheme was approved by shareholders at the annual general meeting on 28 April 1988. The new scheme will increase significantly the number of employees who receive their profit sharing in shares. In 1988, as a result of the special profit sharing payment approved by shareholders, almost 8,600 employees elected to invest in the future of the Group by taking shares instead of cash. Also, nearly 6,000 eligible staff accepted options under the Savings-Related Share Option Scheme.

During the year, the Group introduced a range of initiatives designed to promote equal opportunities for all employees including improved remuneration, benefit and pension arrangements for part-time staff. In addition, the Group has recently announced the intention to introduce a substantial number of workplace nurseries over the next four years; a radical step amongst clearing banks.

Consultation and negotiations have continued on a range of issues between management and representatives of recognised unions within the Group. The principal unions involved during 1988 were the Banking, Insurance and Finance Union, and the Manufacturing, Science and Finance Union (MSF) in which the Association of Scientific, Technical and Managerial Staffs was merged in 1988. However, in February 1989 the Bank gave notice of termination of its agreements with MSF because their membership level within the Bank was considered too small to justify continued recognition for collective bargaining purposes.

Overseas

During the year Handelsfinanz Midland Bank (HMB), a Swiss subsidiary in which Midland holds 85% of the shares, entered into a profit sharing agreement with certain of its senior employees. They are to be given the opportunity of purchasing shares in HMB through a profit sharing reserve to which HMB will contribute 5% of its annual profits. The agreement covers a period of 15 years. The number of HMB shares involved will never exceed a maximum of 10% of the share capital of HMB. The employees concerned do not participate in any other Group profit sharing scheme.

Employment of disabled persons

The Bank continues to develop its policy of full and fair consideration to applications from people with a disability, having regard to their individual aptitudes and abilities and their suitability for particular vacancies. Training and career development opportunities are available to all staff, including those with a disability.

Wherever feasible, existing employees who become disabled are retained in suitable jobs, and equipment provided. Some disabled people prefer, for personal reasons, not to be registered, so each case receives individual attention.

Donations

During the year the Group made donations in the United Kingdom for charitable purposes amounting to £693,441. Included in this sum is an amount of £224,474 which relates to the £1 for £1 Staff Charity Scheme launched in 1986 to celebrate the Bank's 150th anniversary. No donations for political purposes were made.

Directors' interests in the shares of Midland Bank plc

Beneficial interests	Shares at 31 December 1988	Shares at 1 January 1988 (or date of appointment if later)
Sir Kit McMahon	3,626	2,360
J A Brooks	11,370	10,182
E W Brutsche	1,000	1,000
Sir Kenneth Cortield	2,500	2,500
T J Cunningham	9,140	9,140
Sir Archibald Forster	2,000	2,000
B L Goldthorpe	7,140	5,990
Sir Alex Jarratt	3,624	3,624
H E Lockhart	1,182	–
G E Loudon	102	100
G Maitland Smith	1,000	1,000
Sir Patrick Meaney	638	624
D O'Cathain	2,[illegible]45	2,000
Sir Michael Palliser	613	600
Sir Eric Pountain	3,0[illegible]8	3,000
W Purves	746	746
I N Tegner	2,150	1,153
P J Wrangham	5,000	5,000

Shares for which directors have options to subscribe under share option schemes

	Shares at 31 December 1988	Shares at 1 January 1988
Sir Kit McMahon	126,894	26,894
J A Brooks	114,021	82,333
E W Brutsche	50,000	–
B L Goldthorpe	11[illegible],357	49,357
H E Lockhart	86,136	16,136
I N Tegner	109,258	46,258

At 31 December 1988 no director had any non-beneficial interest in the shares of Midland Bank plc or any interests in the shares of subsidiaries and no director had any interests in the loan stocks of Midland Bank plc or its subsidiaries.

No changes in any of the above interests occurred between 31 December 1988 and 23 February 1989.

Auditors

Ernst & Whinney have informed the Bank of their willingness to continue in office as auditors. A resolution proposing their re-appointment as auditors and giving authority to the directors to fix their remuneration will be submitted to the annual general meeting.

By order of the board
J R Skae Secretary

Poultry, London
23 February 1989

ANALYSIS OF SHAREHOLDERS

At 31 December 1988

Category of shareholder	Number of shareholders	Percentage of total	Number of shares held	Percentage of total
Individuals	101,280	95.23	98,685,884	17.96
*Trustee of Midland Bank Group Employee Profit Sharing Scheme	1	–	4,224,280	0.77
Assurance and insurance companies	593	0.56	41,816,553	7.61
Commercial and industrial companies	663	0.62	83,606,808	15.21
Charities, local authorities, hospitals, colleges, etc.	394	0.37	7,992,621	1.45
Nominee companies	2,925	2.75	276,151,447	50.24
Pension funds and pension trustees	119	0.11	17,075,772	3.11
Investment trusts	386	0.36	20,034,369	3.65
	106,361	100.00	549,587,734	100.00

*The trustee of the Midland Bank Group Employee Profit Sharing Scheme held shares on behalf of 17,795 participants.

Shares held	Number of shareholders	Percentage of total	Number of shares held	Percentage of total
1–100	11,690	10.99	542,292	0.10
101–250	15,463	14.54	2,727,214	0.49
251–500	21,727	20.43	8,225,549	1.50
501–1,000	27,486	25.84	20,503,883	3.73
1,001–5,000	27,410	25.77	51,979,912	9.46
5,001–10,000	1,211	1.14	8,538,629	1.55
10,001–25,000	503	0.47	8,116,068	1.48
25,001–50,000	234	0.22	8,829,714	1.61
50,001–250,000	396	0.37	48,796,127	8.88
250,001 and over	241	0.23	391,328,346	71.20
	106,361	100.00	549,587,734	100.00

REPORT OF THE AUDITORS

To the members of Midland Bank plc

We have audited the accounts set out on pages 43 to 64 in accordance with approved auditing standards. The accounts have been prepared under the historical cost convention as explained in accounting policy (a).

In our opinion the accounts give a true and fair view of the state of affairs of the company and of the Group at 31 December 1988 and of the profit and source and application of funds of the Group for the year then ended and comply with the Companies Act 1985.

Ernst & Whinney

Ernst & Whinney
Chartered Accountants

London
23 February 1989

ACCOUNTING POLICIES

The principal accounting policies adopted by the Group are set out below and are consistent with those adopted in 1987.

(a) Accounting convention. The accounts are prepared in accordance with the requirements of the UK Statements of Standard Accounting Practice under the historical cost convention modified by the revaluation of freehold and long leasehold properties.

(b) Basis of consolidation. The Group accounts are prepared in accordance with sections 258 and 259 of, and Schedule 9 to, the Companies Act 1985 and deal with the state of affairs and profits and losses of Midland Bank plc and all its subsidiaries and the attributable share of profits and reserves of its associated companies.

(c) Bad and doubtful debts. Specific and general provisions for bad and doubtful debts are based on the year-end appraisal of advances. The specific element relates to individual banking relationships; the general element relates to other positions not separately identified but known from experience to exist in any portfolio of banking relationships. Interest on bad and doubtful loans continues to be charged to the customer's account and credited to interest income where insolvency law permits, although in most instances a corresponding specific provision is made. When it becomes apparent that recovery is unlikely, interest ceases to be accrued and the outstanding debt is written off.

(d) Instalment finance. Income from fixed rate instalment finance business, after making a deduction for certain initial expenses, is credited to profit and loss account in proportion to the reducing balance outstanding. These balances are stated in the balance sheet after deduction of unearned charges and interest.

(e) Equipment leased to customers. Income from leasing contracts, other than those with major recourse or similar agreements, is credited to profit and loss account in proportion to the funds invested. The great majority of such leases relates to finance leases since substantially all the risks and rewards attaching to the assets leased are transferred to the lessee. Where leasing contracts are covered by major recourse or other similar agreements, income is released to maintain the book amount of the asset at a value consistent with the contractual arrangements.

(f) Depreciation of premises and equipment. The directors consider that, except for certain specialised properties, residual values of freehold and long leasehold buildings (50 years and over unexpired) are such that a nil rate of depreciation should be currently applied. Specialised properties are depreciated on an individual basis having regard to their anticipated useful lives. Other leasehold land and buildings are written off on the straight-line basis over ten years, or the period of the lease whichever is the shorter. Obsolescence of buildings is charged to profit as it arises. Furniture, fittings and equipment are depreciated on the straight-line basis over their estimated useful lives at rates ranging from 5% to 50%.

(g) Dealing assets. Where assets are acquired with the intention of reselling them in the short term at a profit, they are stated in the balance sheet at market value. Income from dealing assets arises in two ways, interest income and dealing income, and is analysed between 'interest receivable' and 'other operating income'.

(h) Fixed interest investments. Where fixed interest investments with fixed redemption dates have been purchased for the long term at a premium or discount, these premiums and discounts are amortised through the profit and loss account over the period from date of purchase to date of maturity. If the date of maturity is at the borrower's option within a specified range of years, the maturity date which gives the more conservative result is adopted. These investments are included in the balance sheet at amortised cost. Profits and losses on the realisation of these investments are dealt with in the profit and loss account as they arise.

(i) Retirement benefits. Annual contributions are made to UK pension schemes on the advice of actuaries for funding of retirement benefits in order to build up reserves for each full-time employee during the employee's working life to pay to the employee or dependant a pension after retirement. The costs of providing these benefits are charged to the profit and loss account on a regular basis. Certain overseas subsidiaries make provisions for pensions in accordance with local law and practice.

(j) Deferred taxation. Deferred taxation is calculated, using the liability method, on all timing differences to the extent that they are likely to crystallise in the future.

(k) Currency translation. Assets and liabilities of UK resident companies maintained in foreign currencies, including investments in associated companies and trade investments financed by loans in foreign currencies and commitments for future purchases or sales, are translated into sterling at the exchange rates ruling at the balance sheet dates of those companies and any difference is taken to profit and loss account. On consolidation, the accounts of overseas subsidiaries and associated companies are translated into sterling at the exchange rates ruling at their balance sheet dates and the consequential adjustments to the opening balances are dealt with through reserves.

(l) Premium on acquisition of shares in associated and subsidiary companies. Premiums on acquisition of shares in associated and subsidiary companies are written off to reserves in the year of acquisition.

(m) Investments in associated and subsidiary companies. Midland Bank plc's investments in associated and subsidiary companies are stated at its share of their net tangible assets.

ANALYSIS OF INTEREST RECEIVABLE, INTEREST PAYABLE, OTHER OPERATING INCOME AND OPERATING EXPENSES

Year ended 31 December 1988

	1988 £m		1987 £m	
INTEREST RECEIVABLE				
Short-term funds		690		594
Dealing assets		195		165
British Government securities (listed)		61		70
Other investments – listed	33		33	
unlisted	57		67	
		90		100
Advances to customers		3,486		3,321
Placings with banks (over 30 days)		407		382
Finance leases and instalment finance		326		275
		5,255		4,907
INTEREST PAYABLE				
Deposits		3,340		3,123
Perpetual floating rate notes, subordinated loan capital and long-term borrowings –				
wholly repayable within five years		25		22
other		169		169
		3,534		3,314
OTHER OPERATING INCOME				
Service charges, fees and other banking income		853		847
Foreign exchange earnings		120		132
Travel income		144		106
Income from trade investments (listed)		1		1
Profit on sale of investments – fixed interest	(10)		18	
other	22		21	
		12		39
Profit/(loss) on disposal of fixed assets		7		(1)
		1,137		1,124
OPERATING EXPENSES				
Staff				
Salaries and other staff costs	1,067		1,029	
Pension costs	115		155	
		1,182		1,184
Premises and equipment				
Depreciation and amortisation	101		90	
Hire of computers and other equipment	12		7	
Rents payable	74		65	
Other	204		183	
		391		345
Audit fees		3		3
Other		448		453
		2,024		1,985

Midland Group

CONSOLIDATED PROFIT AND LOSS ACCOUNT

Year ended 31 December 1988

	Notes	1988 £m	1987 £m
Interest receivable		5,255	4,907
Interest payable		3,534	3,314
Net interest income		1,721	1,593
Other operating income		1,137	1,124
Operating income		2,858	2,717
Operating expenses		2,024	1,985
Trading profit before charge for bad and doubtful debts		834	732
Charge for bad and doubtful debts		201	230
Trading profit		633	502
Share of profits of associated companies	4	60	9
Profit before exceptional item		693	511
Exceptional item	5	-	(1,016)
Profit/(loss) before taxation		693	(505)
Taxation	6	273	(58)
Profit/(loss) after taxation		420	(447)
Minority interests		(8)	(9)
Profit/(loss) before extraordinary items		412	(456)
Extraordinary items	7	-	63
Profit/(loss) attributable to members of Midland Bank plc		412	(393)
Dividends	8	126	90
Retained profit/(deficit)		286	(483)
Earnings/(loss) per share	9	75.1p	(125.3)p

Movements in reserves are set out in note 26.

Midland Group

CONSOLIDATED BALANCE SHEET

31 December 1988

	Notes	1988 £m	1987 £m
ASSETS			
Liquid assets	10	7,619	6,316
Items in course of collection		781	690
Certificates of deposit		852	1,186
Dealing assets	11	2,700	2,603
Investments	12	1,381	1,463
Debtors	13	806	864
Advances and other accounts	14	40,273	34,355
		54,412	47,477
Trade investments	15	24	21
Investments in associated companies	16	171	106
Premises and equipment	18	1,122	846
		55,729	48,450
LIABILITIES			
Current, deposit and other customer accounts	19	47,983	41,679
Other liabilities	20	2,132	1,895
		50,115	43,574
Deferred taxation	21	198	71
Long-term borrowings	22	378	317
Subordinated loan capital	23	970	945
Perpetual floating rate notes	24	888	858
Minority interests		141	99
Shareholders' funds			
Share capital	25	550	547
Share premium	25	1,042	1,036
Reserves	26	1,447	1,003
		3,039	2,586
		55,729	48,450

Kit McMahon, chairman and group chief executive
Ian Tegner, director, group finance

× Kit McMahon
Ian Tegner.

23 February 1989

Co. NO. 14259.

Midland Bank plc

BALANCE SHEET

31 December 1988

	Notes	1988 £m	1987 £m
ASSETS			
Liquid assets	10	4,608	4,062
Items in course of collection		766	686
Certificates of deposit		214	848
Dealing assets	11	424	506
Investments	12	574	692
Debtors	13	169	76
Deferred taxation	21	87	206
Advances and other accounts	14	31,486	25,643
Balances due by subsidiaries		1,544	1,442
		39,872	34,161
Trade investments	15	17	10
Investments in associated companies	16	147	96
Investments in subsidiary companies	17	1,458	1,441
Premises and equipment	18	906	668
		42,400	36,376
LIABILITIES			
Current, deposit and other customer accounts	19	35,292	30,529
Other liabilities	20	565	343
Balances due to subsidiaries		2,257	1,703
		38,114	32,575
Subordinated loan capital	23	386	386
Perpetual floating rate notes	24	861	829
Shareholders' funds			
Share capital	25	550	547
Share premium	25	1,042	1,036
Reserves	26	1,447	1,003
		3,039	2,586
		42,400	36,376

Kit McMahon, chairman and group chief executive
Ian Tegner, director, group finance

23 February 1989

Kit McMahon
Ian Tegner.

Midland Group

STATEMENT OF SOURCE AND APPLICATION OF FUNDS

Year ended 31 December 1988

	1988 £m	1987 £m
SOURCE OF FUNDS		
Profit/(loss) attributable to members of Midland Bank plc	412	(393)
ADJUSTMENTS FOR ITEMS NOT INVOLVING THE MOVEMENT OF FUNDS		
Profit on disposal of Clydesdale and Northern Banks	-	(60)
Depreciation of premises and equipment	101	90
Deferred taxation	127	(202)
Minority interests	42	9
Amount retained by associated companies	(31)	2
Other items	(5)	(59)
Funds generated from operations	646	(613)
FUNDS FROM OTHER SOURCES		
Net proceeds from disposal of Clydesdale and Northern Banks	-	415
Disposal of trade investments and associated companies	4	34
Disposal of premises and equipment	25	36
Increase in share and loan capital	125	746
	800	618
APPLICATION OF FUNDS		
Dividends paid	115	63
Purchase of trade investments and associated companies	41	15
Purchase of goodwill on acquisition of subsidiaries	35	6
Purchase of premises and equipment	204	197
	395	281
Working capital	405	337
	800	618
WORKING CAPITAL		
Advances and other customer accounts	5,918	655
Liquid assets	1,303	(1,037)
Debtors and other assets	(286)	(413)
Current and deposit accounts and other liabilities excluding dividends	(6,530)	1,132
	405	337

Funds movements for 1987 exclude the effects of the di[illegible] [illegible]iesdale and Northern Banks.

NOTES ON THE ACCOUNTS

1 Turnover

The turnover of the Group as a whole is not shown as it results mainly from the business of banking. Non-banking turnover consists of commissions on travel arrangements and sales in respect of tour operations amounting to £385m (1987 £281m). Aggregate leasing rentals were £644m (1987 £498m) the majority of which related to finance leases. Aggregate hire purchase instalments were £392m (1987 £295m).

2 Retirement benefits

The Midland Bank Pension Scheme, the assets of which are held in a separate Trust Fund, is the principal pension scheme within the Group covering 84% of the Group's UK employees. The Midland Bank Pension Scheme is a funded 'defined benefit scheme'.

Actuarial valuations of the assets and liabilities of the scheme are carried out triennially by external professional actuaries to determine the financial position of the scheme and to enable the Bank to determine the level of contributions to be made to the scheme.

The latest valuation was made as at 31 December 1987 at which date the market value of the scheme assets was £1,784m. This valuation was prepared on the attained age method and showed that the level of funding at that date was 95%, significantly higher than at 31 December 1984, the date of the last actuarial valuation. The actuaries recommended future contributions of 20% of pensionable salary (1984 27%) of which 1.4% (1984 7.7%) represents the amount expected to be necessary to achieve a funding level of 100% by 31 December 2006. Participating companies have agreed to make these contributions from 1 January 1988.

The main financial assumptions used in the latest valuation, which, except for small increases of ½% per annum in the effective allowances made for equity dividend and post retirement pension increases, are consistent with those used in the previous valuation, were

	Percentage per annum
Long-term investment return	9
General salary increases	7
Equity dividend increases	4.5
Post retirement pension increases	4

The actuaries also confirmed that, on the basis of the actuarial assumptions and methods used, the scheme's assets at 31 December 1987 fully covered its liabilities based on then current salary levels and service to the valuation date.

The pension schemes of the Thomas Cook Group and the Samuel Montagu Group, which cover 9% of the Group's UK employees, are similarly constituted and are fully funded.

The reduction in pension costs of £40m from the charge in 1987 of £155m mainly reflects the results of the actuarial valuation carried out at 31 December 1987 and the disposal of Clydesdale and Northern Banks (£17m in 1987).

3 Emoluments

The aggregate emoluments of the directors of the Bank amounted to £2,992,000 (1987 £3,035,000) and consisted of fees £172,000 (1987 £128,000) and other emoluments £2,820,000 (1987 £2,907,000). In addition, pensions in respect of past services of £228,000 (1987 £204,000) were paid.

The chairman's emoluments totalled £238,554 (1987 £47,161 in respect of Sir Donald Barron up to 30 April and £129,349 in respect of Sir Kit McMahon from 1 May onwards).

The emoluments of the highest paid director amounted to £640,827 (1987 £748,458).

During the year, four directors waived emoluments totalling £30,254 (1987 nil).

Some of the directors served on the board for part of the year only.

The tables show the number of directors and employees of Midland Bank plc, other than employees who discharged their duties wholly or mainly outside the United Kingdom and the highest paid director, whose emoluments receivable from the Bank and, in the case of directors only, its subsidiaries, fell within the bands stated.

Directors £	1988	1987
1 – 5,000	5	3
5,001 – 10,000	2	2
10,001 – 15,000	4	5
15,001 – 20,000	1	1
30,001 – 35,000	1	–
35,001 – 40,000	–	2
40,001 – 45,000	–	1
45,001 – 50,000	2	3
50,001 – 55,000	–	1
60,001 – 65,000	–	1
95,001 – 100,000	1	–
115,001 – 120,000	–	1
120,001 – 125,000	1	–
130,001 – 135,000	1	–
135,001 – 140,000	–	1
155,001 – 160,000	1	–
190,001 – 195,000	–	1
215,001 – 220,000	1	–
235,001 – 240,000	1	1
395,001 – 400,000	1	–
475,001 – 480,000	1	–
625,001 – 630,000	–	1

Employees £	1988	1987
30,000 – 35,000	742	589
35,001 – 40,000	508	361
40,001 – 45,000	289	243
45,001 – 50,000	145	94
50,001 – 55,000	72	20
55,001 – 60,000	59	21
60,001 – 65,000	20	12
65,001 – 70,000	10	4
70,001 – 75,000	9	2
75,001 – 80,000	5	2
80,001 – 85,000	5	5
85,001 – 90,000	2	3
90,001 – 95,000	4	2
95,001 – 100,000	2	–
115,001 – 120,000	1	2
120,001 – 125,000	1	–
210,001 – 215,000	1	–

4 Associated companies

Dividends receivable during 1988 from associated companies, all of which are unlisted, amounted to £5m (1987 £7m).

5 Exceptional item

	1988 £m	1987 £m
Exceptional provisions against loans to borrowers in countries identified as having actual or potential payment difficulties	–	1,016

6	Taxation	1988 £m	1987 £m
	The charge/(credit) for taxation is made up as follows		
	United Kingdom corporation tax		
	Current at 35% (1987 35%)	211	40
	Deferred	(5)	(183)
	Transfer to tax credit equalisation	4	6
	Notional tax charge on tax credit equalisation release	4	5
		214	(132)
	Less relief in respect of overseas taxation	19	–
		195	(132)
	Overseas taxation		
	Current	58	67
	Deferred	(3)	2
		250	(63)
	Associated companies	23	5
		273	(58)

7	Extraordinary items	1988 £m	1987 £m
	Profit on sale of Clydesdale and Northern Banks	–	60
	Profit on sale of Avis Car Leasing, an associated company	–	14
	Provision for closure costs of Greenwell Montagu Securities	–	(11)
		–	63

8	Dividends	1988 pence per share	1987 pence per share	1988 £m	1987 £m
	First interim	9.5	8.6*	52	27
	Second interim	13.5	11.5	74	63
		23.0	20.1	126	90

*adjusted for 1987 rights issue

9 **Earnings per share**

Earnings per share have been calculated on the profit before extraordinary items of £412m (1987 loss £456m) related to the weighted average of 548m shares (1987 365m shares adjusted for the rights issue in 1987) in issue during the year.

10 **Liquid assets**

	Group 1988 £m	Group 1987 £m	Midland Bank plc 1988 £m	Midland Bank plc 1987 £m
Coin, bank notes, balances with central banks and gold	761	726	470	349
Money at call and short notice	6,745	5,188	4,043	3,342
Bills discounted	113	402	95	371
	7,619	6,316	4,608	4,062

Coin, bank notes, balances with central banks and gold includes gold bullion, amounting to £187m (1987 £231m) at current market value.

11 **Dealing assets**

	Group 1988 £m	Group 1987 £m	Midland Bank plc 1988 £m	Midland Bank plc 1987 £m
Bullion other than gold	160	156	–	–
Bills	280	283	135	117
Certificates of deposit	210	484	31	214
Investments				
Listed –				
Securities of, or guaranteed by, the British Government	449	479	61	122
Others listed in Great Britain	157	59	69	–
Others listed elsewhere	921	887	31	21
	1,527	1,425	161	143
Unlisted –				
United States authorities and agencies	20	35	–	29
Other	440	172	97	3
	460	207	97	32
	1,987	1,632	258	175
Properties	63	48	–	–
	2,700	2,603	424	506

Listed investments are valued at middle market prices and unlisted investments at directors' valuation.

12 Investments

	1988 £m Book amount	1988 £m Valuation	1987 £m Book amount	1987 £m Valuation
Group				
Listed –				
Securities of, or guaranteed by, the British Government	338	326	492	495
Others listed in Great Britain	153	162	130	157
Others listed elsewhere	213	208	299	300
	704	696	921	952
Unlisted –				
United States authorities and agencies	231	228	255	255
Other	446	453	287	307
	1,381	1,377	1,463	1,514
Midland Bank plc				
Listed –				
Securities of, or guaranteed by, the British Government	306	293	451	452
Others listed in Great Britain	46	48	43	43
Others listed elsewhere	125	125	175	175
	477	466	669	670
Unlisted –				
United States authorities and agencies	94	93	14	14
Other	3	3	9	9
	574	562	692	693

Where fixed interest investments with a fixed redemption date are held for the long term, they are stated at amortised cost amounting to £1,234m (1987 £1,393m) for the Group and £572m (1987 £688m) for Midland Bank plc.

All other investments are stated at cost less provision.

Listed investments are valued at middle market prices and unlisted investments at directors' valuation.

13 Debtors

Sundry debtors include securities trading assets arising in the market-making subsidiaries; related liabilities are included under 'Other liabilities' – see note 20.

14 Advances and other accounts

	Group 1988 £m	Group 1987 £m	Midland Bank plc 1988 £m	Midland Bank plc 1987 £m
Lendings to customers				
Advances	32,597	28,956	28,188	23,999
Instalment finance	1,140	845	-	-
	33,737	29,801	28,188	23,999
Finance leases	2,158	1,745	-	-
Total lendings	35,895	31,546	28,188	23,999
Less provisions	1,854	1,740	1,636	1,510
	34,041	29,806	26,552	22,489
Placings with banks (over 30 days)	4,485	3,293	3,381	2,070
Accrued interest and other customer accounts	1,747	1,256	1,553	1,084
	40,273	34,355	31,486	25,643
Of which				
Sterling	27,433	21,388	22,517	17,172
Currency	12,840	12,967	8,969	8,471
	40,273	34,355	31,486	25,643

Advances are stated after deduction of amounts refinanced with the Export Credits Guarantee Department and the Department of Trade and Industry.

Included in instalment finance above are amounts in respect of hire purchase contracts amounting to £688m (1987 £497m).

The cost of assets acquired in 1988 for the purpose of letting under finance leases and hire purchase contracts amounted to £939m (1987 £702m) and £685m (1987 £523m) respectively.

14 Advances and other accounts – *continued*

Movements on provisions for bad and doubtful debts were as follows

	1988 £m			1987 £m		
	Specific	General	Total	Specific	General	Total
Group						
Provisions at 1 January	1,607	133	1,740	756	227	983
Currency translation and other adjustments	37	11	48	(219)	(21)	(240)
Charge for the year	155	46	201	285	(55)	230
Exceptional charges (see note 5)	–	–	–	1,016	–	1,016
Amounts written off	(165)	–	(165)	(164)	–	(164)
Less recoveries of amounts written off in previous years	30	–	30	18	–	18
	(135)	–	(135)	(146)	–	(146)
Less provisions relating to Clydesdale and Northern Banks	–	–	–	85	18	103
Provisions at 31 December	1,664	190	1,854	1,607	133	1,740
Midland Bank plc						
Provisions at 1 January	1,447	63	1,510	490	119	609
Currency translation and other adjustments	44	1	45	(176)	(12)	(188)
Charge for the year	144	27	171	200	(44)	156
Exceptional charges (see note 5)	–	–	–	1,016	–	1,016
Amounts written off	(107)	–	(107)	(93)	–	(93)
Less recoveries of amounts written off in previous years	17	–	17	10	–	10
	(90)	–	(90)	(83)	–	(83)
Provisions at 31 December	1,545	91	1,636	1,447	63	1,510

The Group makes specific provisions against loans to and interest due from borrowers in countries identified as having actual or potential payment difficulties. The level of such provisions is reviewed against exposure on a country by country basis and adjusted when the economic, political or regional circumstances of a country change, assessed by a scoring system consistent with Bank of England guidelines. In addition, interest is normally reserved when it is more than 90 days overdue.

15 Trade investments

At cost less provisions	1988 £m Book amount	1988 £m Valuation	1987 £m Book amount	1987 £m Valuation
Group				
Listed elsewhere than in Great Britain	-	-	3	3
Unlisted	24	27	18	25
	24	27	21	28
Midland Bank plc				
Unlisted	17	17	10	11

Listed investments are valued at middle market prices and unlisted investments at directors' valuation.

The principal trade investments at 31 December 1988, all of which were held directly by Midland Bank plc, were as follows

	Country of incorporation	Interest
The Agricultural Mortgage Corporation PLC	Great Britain	
Issued share capital £13.5m		13%
BCH Property Limited	Great Britain	
Issued share capital £1.5m		18%

16 Investments in associated companies

Share of net tangible assets	1988 £m Book amount	1988 £m Valuation	1987 £m Book amount	1987 £m Valuation
Group				
Listed elsewhere than in Great Britain	7	7	3	3
Unlisted – Equity	141	180	88	133
Other	23	23	15	15
	171	210	106	151
Midland Bank plc				
Unlisted – Equity	124	148	82	115
Other	23	23	14	14
	147	171	96	129

Listed investments are valued at middle market prices and unlisted investments at directors' valuation.

16 Investments in associated companies – *continued*

The principal associated companies at 31 December 1988 were as follows

	Country of incorporation and operation	Accounts made up to	Direct interest of Midland Bank plc
3i Group plc	Great Britain	30.9.1988*	
Issued share capital £232m			18%
The Joint Credit Card Company Limited	Great Britain	31.10.1988	
Issued share capital £400			30%
Loan capital £55.8m			30%
UBAF Bank Limited	Great Britain	31.12.1988	
US $ share capital $93m			25%
£ sterling share capital £46m, of which £15m 67% paid up			25%
Subordinated unsecured loan stock US $28.7m			25%
Subordinated loan stock £10m			12.5%

*unaudited interim accounts

17 Investments in subsidiary companies

	1988 £m	1987 £m
Midland Bank plc		
Shares in subsidiaries at Bank's share of net tangible assets	843	713
Loans to subsidiaries	615	728
	1,458	1,441

The principal subsidiaries at 31 December 1988, all of whose accounts were made up to 31 December 1988, were as follows

	Country of incorporation and operation	Equity interest of Midland Bank plc	
		Direct	Indirect
Forward Trust Limited	Great Britain		100%
Griffin Factors Limited	Great Britain		100%
Midland Bank SA°	France		74%
Midland Bank Trust Company Limited	Great Britain	100%	
Samuel Montagu & Co. Limited	Great Britain		100%
The Thomas Cook Group Limited	Great Britain	100%	
Trinkaus & Burkhardt KGaA#°	West Germany		71%

All the above subsidiaries are engaged in the business of banking and financial services with the exception of The Thomas Cook Group Limited which is engaged in the business of world travel, tour operations, foreign exchange dealings and the issue of travellers cheques.

° minority shareholding listed
limited partnership

18 Premises and equipment

Group	£m Freehold land and buildings	£m Leasehold land and buildings 50 years and over unexpired	£m under 50 years unexpired	£m Furniture, fittings and equipment	£m Total
Cost or valuation					
At 1 January 1988	455	38	141	541	1,175
Currency translation adjustments	(5)	–	–	–	(5)
Additions	36	13	20	135	204
Surplus on revaluation	188	15	–	–	203
Disposals	(12)	(3)	(2)	(57)	(74)
At 31 December 1988	662	63	159	619	1,503
Accumulated depreciation	(8)	–	(63)	(310)	(381)
Net book amount					
At 31 December 1988	654	63	96	309	1,122
At 31 December 1987	442	36	91	277	846
Midland Bank plc					
Cost or valuation					
At 1 January 1988	370	38	111	396	915
Additions	25	13	14	95	147
Surplus on revaluation	161	15	–	–	176
Disposals	(10)	(3)	(1)	(39)	(53)
At 31 December 1988	546	63	124	452	1,185
Accumulated depreciation	(5)	–	(53)	(221)	(279)
Net book amount					
At 31 December 1988	541	63	71	231	906
At 31 December 1987	361	36	67	204	668

	Group	Midland Bank plc
Cost or valuation of premises and equipment at 31 December 1988 comprises		
Land and buildings at valuation 1988	662	604
at cost	222	129
	884	733
Furniture, fittings and equipment, at cost	619	452
	1,503	1,185

The depreciable amounts for leaseholds under 50 years unexpired for the Group and for Midland Bank plc were £159m (1987 £141m) and £124m (1987 £111m) respectively.

The Group's freehold and long leasehold (50 years and over unexpired) properties in the United Kingdom have been valued at 31 December 1988 by professionally qualified staff or by the Group's professional valuers, Messrs. Healey & Baker, in respect of Midland Bank plc and certain subsidiaries. Freehold and long leasehold properties in the United Kingdom owned by The Thomas Cook Group Limited have been valued by Messrs. Jones Lang Wootton, Chartered Surveyors. The basis of valuation is open market value for existing use. The values of certain specialised properties have been reviewed and, as a result, their existing book amounts have been maintained.

The resultant surpluses of £203m for the Group and £176m for Midland Bank plc have been credited to reserves. Other leasehold land and buildings have also been reviewed and as a result their existing book amounts have been maintained.

19 Current, deposit and other customer accounts	Group 1988 £m	Group 1987 £m	Midland Bank plc 1988 £m	Midland Bank plc 1987 £m
Sterling				
Current and demand accounts	15,608	14,026	14,411	12,884
Deposit and savings accounts	2,259	2,126	2,231	2,097
Money market and other time deposits	11,584	6,919	7,863	4,075
Accrued interest	298	215	244	155
Items in transit and other customer accounts	542	555	427	432
	30,291	23,841	25,176	19,643
Currency				
Current and demand accounts	4,916	4,136	1,794	1,647
Deposit and savings accounts	1,444	1,883	936	1,264
Money market and other time deposits	10,365	10,801	7,007	7,544
Accrued interest	296	286	201	198
Items in transit and other customer accounts	671	732	178	233
	17,692	17,838	10,116	10,886
	47,983	41,679	35,292	30,529

Included in the Group figures above are secured bank overdrafts of subsidiaries amounting to £12m (1987 £161m).

20 Other liabilities	Group 1988 £m	Group 1987 £m	Midland Bank plc 1988 £m	Midland Bank plc 1987 £m
Taxation	205	115	107	49
Creditors and securities trading liabilities	1,853	1,717	384	231
Dividend	74	63	74	63
	2,132	1,895	565	343

Securities trading liabilities arise in the market-making subsidiaries and reflect the level of activity in the securities markets. The related assets are included under 'Debtors' – see note 13.

21 Deferred taxation

	1988 £m Potential deferred tax	1988 £m Balance at 31 December	1987 £m Potential deferred tax	1987 £m Balance at 31 December
Group				
Short-term timing differences	(9)	(9)	1	1
Accelerated capital allowances	23	23	29	29
Leasing transactions	342	253	341	252
Premises revaluation	42	2	64	2
Tax losses arising from exceptional provisions	–	–	(183)	(183)
Other items	21	18	15	10
Advance corporation tax recoverable	(89)	(89)	(40)	(40)
	330	198	227	71
Midland Bank plc				
Short-term timing differences	(19)	(19)	(4)	(4)
Accelerated capital allowances	17	17	18	18
Premises revaluation	33	–	60	–
Tax losses arising from exceptional provisions	–	–	(183)	(183)
Other items	4	4	3	3
Advance corporation tax recoverable	(89)	(89)	(40)	(40)
	(54)	(87)	(146)	(206)

22 Long-term borrowings

	1988 £m	1987 £m
Subsidiaries		
5% Debenture 1987/92 DM 9m	3	3
Borrowings at fixed and variable rates between 6¼% and 15.9% repayable 1989/98* Fr Frs 1,998m (1987 Fr Frs 1,577m)	183	157
3¾% Bonds repayable 1991/92 Sw Frs 20m	7	8
6% Bonds repayable 1996 DM 100m	30	34
13⅛% Note repayable 1997	25	25
Guaranteed Floating Rate Notes 1997 Fr Frs 900m#	82	90
6% Bonds repayable 1993 DM 75m	24	–
5½% Bonds repayable 1993 DM 75m	24	–
	378	317
Repayable within 1 year	1	–
1 – 2 years	8	2
2 – 5 years	95	76
Over 5 years	274	239
	378	317

* repayable by instalments

\# the interest rate on the notes is related to the *in fine* interest rate corresponding to the latest published weighted average discount rate for 13 week French Treasury Bills; at 15 December 1988 the interest rate was set at 8.38% for the period to 15 March 1989

23 Subordinated loan capital	1988 £m	1987 £m
Midland Bank plc		
7½% Subordinated Unsecured Loan Stock 1983/93	5	5
10¼% Subordinated Unsecured Loan Stock 1993/98	31	31
Subordinated Floating Rate Notes 2001	250	250
14% Subordinated Unsecured Loan Stock 2002/07	100	100
	386	386
Subsidiaries		
8¾% Guaranteed Bonds 1992* US $36m (1987 US $45m)	21	24
11½% Guaranteed Bonds 1992 US $150m	83	80
Guaranteed Floating Rate Notes 1992 US $150m	83	80
6½% Guaranteed Bonds 1986/96 DM 200m	63	68
Guaranteed Floating Rate Notes 1986/98 DM 300m	94	102
7.55% Guaranteed Loan 1998 Yen 6.3bn	28	–
Guaranteed Floating Rate Notes 1999 US $200m	111	107
Guaranteed Floating Rate Unsecured Loan Stock 2001	17	17
Guaranteed Floating Rate Series A to C Unsecured Loan Stock 2001	1	1
12¾% Guaranteed Notes 2003 US $150m	83	80
	584	559
	970	945
Repayable within 1 year	4	4
1 – 2 years	4	4
2 – 5 years	184	176
Over 5 years	778	761
	970	945

Subordinated loan capital is repayable at par at maturity but some is repayable prior to maturity at the option of the borrower, in certain cases at a premium over par.

The interest rates on the floating rate subordinated loan capital are related to relevant London interbank rates.

*repayable by instalments

24 **Perpetual floating rate notes**

	1988 £m	1987 £m
Midland Bank plc		
Undated Floating Rate Primary Capital Notes US $750m	417	401
Undated Floating Rate Primary Capital Notes US $500m	278	267
Undated Floating Rate Primary Capital Notes (Series 3) US $300m	166	161
	861	829
Subsidiaries		
Convertible Undated Floating Rate Subordinated Notes Fr Frs 300m	27	29
	888	858

The Undated Floating Rate Primary Capital Notes have characteristics which render them similar in certain circumstances to preferred shares.

The interest rates on the Undated Floating Rate Primary Capital Notes are related to London Interbank Offered Rates. The annual interest rate on the Convertible Undated Floating Rate Subordinated Notes is related to the average monthly bond rates for new issues in the Paris market.

The right to convert the Convertible Undated Floating Rate Subordinated Notes may be exercised at any time from 1 January 1990 until 31 December 2005 on the basis of 3.6 ordinary shares of Midland Bank SA each with a nominal value of Fr Frs 100 for each Fr Frs 1,000 note.

25 **Share capital and share premium**

The authorised share capital of Midland Bank plc is £750m.
The movements in issued share capital and share premium were as follows

	Share capital		Share premium	
	1988 £m	1987 £m	1988 £m	1987 £m
At 1 January	547	232	1,036	276
Rights issue	–	233	–	466
Subscription by The Hongkong and Shanghai Banking Corporation	–	81	–	302
Shares issued under share option schemes	2	1	2	1
Shares issued in lieu of cash – 1988 interim dividend	–	–	1	–
Share and loan capital issue expenses	–	–	–	(12)
Shares issued under employee profit sharing scheme	1	–	3	3
At 31 December	550	547	1,042	1,036

26 Reserves

	£m	£m	£m	£m
	Midland Bank plc and subsidiaries	Associated companies	Group	Midland Bank plc
At 1 January 1988	961	42	1,003	1,003
Currency translation adjustments	(9)	(1)	(10)	–
Retained profit	255	31	286	195
Surplus on revaluation of freehold and long leasehold properties	203	–	203	176
Premium written off on acquisition of subsidiary companies	(35)	–	(35)	–
Net increase in net tangible assets of subsidiary and associated companies	–	–	–	73
At 31 December 1988	1,375	72	1,447	1,447

Group reserves at 31 December 1988 include £457m in respect of revaluation of freehold and long leasehold properties, of which £413m relates to Midland Bank plc. In addition, the reserves of Midland Bank plc at 31 December 1988 include £526m in respect of post acquisition retained reserves of subsidiary and associated companies.

27 Contingent liabilities

	1988 £m	1987 £m
There were the following contingent liabilities in respect of		
Acceptances		
Group	1,092	1,382
Midland Bank plc	968	1,131
Engagements		
Group	5,686	4,498
Midland Bank plc	5,079	3,705

In addition there were outstanding financial contracts, agreements and other financial instruments entered into in the normal course of business. Midland Bank plc has guaranteed the performance of a subsidiary in respect of certain of these items, and certain exposures to banks by a subsidiary.

	1988 £m	1987 £m
Midland Bank plc has guaranteed		
Subordinated loan capital and long- and short-term borrowings of certain subsidiaries	851	958
Lendings to customers by certain subsidiaries	471	54

28 Capital and other commitments

	1988 £m	1987 £m
Contracts for outstanding capital expenditure not provided for in these accounts amounted to		
Group	109	49
Midland Bank plc	78	40

In addition, the Board has authorised capital expenditure amounting approximately to £128m (1987 £48m) for the Group and £111m (1987 £43m) for Midland Bank plc.

29 Share options

Options outstanding to UK employees of the Group under the Midland Bank plc savings-related and executives' share option schemes were as follows

		1988
Options	Period	Price
13,981,271	1989/98	£1.9894/4.6634

		1987
Options	Period	Price
12,194,167	1988/97	£1.9894/4.6634

30 Directors' and officers' loans

In accordance with the requirements of sections 233 and 234 of the Companies Act 1985, the aggregate amounts outstanding at 31 December 1988 from persons who were directors or officers (or connected with directors or officers) during the year, and the number of persons concerned, were as follows

	£m Aggregate amount outstanding	Number of persons
Directors		
Loans	1.5	11
Quasi-loans	*	27
Credit transactions	–	–
Officers		
Loans	0.1	2
Quasi-loans	#	1
Credit transactions	–	–

* aggregate amount outstanding was £15,839

aggregate amount outstanding was £375

Midland Group

FIVE YEAR SUMMARY

		1988 £m	1987 £m	1986 £m	1985 £m	1984 £m
Profit before exceptional item and taxation		693	511	434	351	135
Profit/(loss) before taxation		693	(505)	434	351	135
Taxation charge/(credit)		273	(58)	172	207	160
Profit/(loss) before extraordinary items		412	(456)	242	122	62
Profit/(loss) attributable		412	(393)	242	122	45
Shareholders' funds		3,039	2,586	2,021	1,847	1,685
Minority interests		141	99	90	235	486
Perpetual floating rate notes		888	858	1,082	892	–
Subordinated loan capital		970	945	1,094	998	1,294
Total capital resources		5,038	4,488	4,287	3,972	3,465
Current, deposit and other customer accounts		47,983	41,679	46,082	52,461	56,598
Advances and other accounts		40,273	34,355	36,641	41,473	44,858
Total assets		55,729	48,450	53,169	58,074	61,483
Return on average shareholders' funds						
– profit attributable		15.0%	(18.9)%	12.5%	6.8%	2.5%
Return on average equity						
– profit before exceptional item and taxation		24.3%	23.6%	20.8%	16.4%	5.9%
– profit before taxation		24.3%	(23.3)%	20.8%	16.4%	5.9%
Total equity/total assets		5.7%	5.5%	4.0%	3.6%	3.5%
Average shares in issue (millions)	a	548	365	311	309	308
Earnings (loss) per share						
– adjusted for 1987 rights issue	a	75.1p	(125.3)p	77.5p	39.4p	20.2p
– before adjustment		–	–	104.2p	53.0p	27.1p
Dividends per share	a	23.0p	20.1p	20.1p	19.0p	19.0p
Dividend cover	b	3.3	–	3.9	2.1	1.1
Shareholders	c	106,361	106,387	104,494	110,331	98,750
Average base rate		10.1%	9.7%	10.9%	12.2%	9.7%

a 1984-1986 (and first interim for 1987) adjusted for 1987 rights issue

b Dividend cover is calculated by dividing adjusted earnings per share by adjusted dividends

c Number of shareholders registered at year-end

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P L Brooke: *special projects director*

D G McLachlan: *group audit director*

H G O'Brien: *head of group financing*

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Midland Montagu Securities Inc
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156 West 56th Street
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NOTICE OF MEETING

Notice is hereby given that the 153rd annual general meeting of Midland Bank plc will be held at Merchant Taylors' Hall, 30 Threadneedle Street, London EC2, on Thursday, 27 April 1989 at 11.00 am for the following purposes:

Ordinary business

1 To receive the report of the directors and audited accounts for the year ended 31 December 1988.

To reappoint the following directors:

2 G E Loudon.
3 P J Wrangham.
4 Sir Colin Marshall
5 Sir Patrick Meaney.
6 Sir Alex Jarratt.
7 D O'Cathain.
8 Sir Kit McMahon.
9 To reappoint Ernst & Whinney as auditors and to authorise the directors to fix their remuneration.

Special business

To consider and, if thought fit, to pass the undermentioned resolutions:

10 Ordinary Resolution (Scrip dividend)
That the directors of the Bank be and hereby are authorised to exercise the powers conferred on them by article 114A of the Bank's articles of association in respect of any dividend to be declared by the directors before the annual general meeting of the Bank in 1990.

11 Ordinary Resolution (Capitalisation issue)
That:

(a) the authorised share capital of the Bank be increased from £750,000,000 to £1,000,000,000 by the creation of 250,000,000 shares of £1 each;

(b) such part of the sum standing to the credit of the Bank's property revaluation reserves as shall equal two fifths of the aggregate nominal value of:

(i) the shares of the Bank in issue at the close of business on 7 April 1989 ('the record date'); and

(ii) the shares of the Bank allotted pursuant to valid elections to receive the scrip dividend alternative in lieu of the second interim dividend for 1988 ('the scrip dividend shares')
be capitalised and applied in paying up in full new shares of £1 each in the capital of the Bank to be allotted at par as fully paid up and distributed to and amongst the registered holders at the record date of the shares then in issue in the proportion of two new shares for every five shares then held and to and amongst the allottees of the scrip dividend shares in the proportion of two new shares for every five scrip dividend shares allotted (save that fractions of new shares will not be allotted but will be aggregated and sold in the market and the proceeds of sale, less expenses of sale and distribution, will be distributed among shareholders in proportion to their respective entitlements, if any, except that sums of less than £2.50 will be retained for the benefit of the Bank) and so that the new shares shall rank *pari passu* with the shares in issue at the record date save that they shall not rank for any dividend declared or payable in respect of the year ended 31 December 1988;

(c) the directors be and hereby are authorised in accordance with section 80 of the Companies Act 1985 to allot shares having a maximum aggregate nominal value of £227 million in connection with the capitalisation issue referred to in paragraph (b) of this resolution and so that this authority shall expire on 31 May 1989 and shall be in addition to the authority conferred on the directors by resolution 10 passed at the annual general meeting of the Bank held on 28 April 1988 and any renewal of such authority effected by the passing of resolution 12 comprised in this notice.

12 Ordinary Resolution (Directors' authority to allot shares)
That the general authority conferred on the directors by article 8(B) (1) of the articles of association of the Bank be renewed for a period of five years from the date of the passing of this resolution and that for such period the prescribed amount (as referred to in that article) be £183,195,911 or, if resolution 11 comprised in this notice shall be passed, £205,173,656.

13 Special Resolution (Disapplication of pre-emption rights)
That for the purposes of article 8 of the articles of association of the Bank:

*(a) the power conferred by paragraph (B) (2) (a) of that article (disapplication for small cash issues) be renewed and the special prescribed period (as referred to in that article) be the period from the date of the passing of this resolution to the conclusion of the annual general meeting in 1990 (or 27 July 1990, if earlier) provided that (notwithstanding anything in the articles of association of the Bank), if resolution 12 comprised in this notice shall be passed, the maximum aggregate nominal value of shares which the directors shall be empowered to allot for cash pursuant to this resolution shall be £39,743,817; and

(b) conditionally upon the passing of resolution 12 comprised in this notice, the power conferred by paragraph (B) (2) (b) of that article (five year disapplication for rights issues) be renewed.

A member entitled to attend and vote at the meeting is entitled to appoint one or more proxies to attend and, on a poll, to vote instead of him. A proxy need not be a member. The completion and return of the form of proxy will not preclude a member from attending the meeting and voting in person.

*This paragraph empowers the directors to allot for cash up to 27,479,386 shares (equivalent to 5% of the Bank's issued share capital at 31 December 1988) or, if the capitalisation issue is approved by shareholders, up to 39,743,817 shares (equivalent to 5% of the Bank's current issued share capital as enlarged by the capitalisation issue).

By order of the board
J R Skae, secretary

Poultry, London
28 March 1989

Notes

1 Only holders of shares are entitled to attend or be represented at the meeting. A form of proxy is enclosed with the annual report.

2 Copies of directors' service contracts of more than one year's duration or memoranda of the terms thereof will be available for inspection at the registered office of Midland Bank plc during usual business hours from the date of this notice until the date of the meeting and at the place of the meeting from 10.45 am on the day of the meeting until the conclusion of the meeting.

3 No changes in any of the directors' interests in the shares of the Bank as shown on page 41 of the annual report occurred between 23 February 1989 and 1 March 1989.