# CITY OF LONDON
INVESTMENT GROUP PLC

ANNUAL REPORT & ACCOUNTS
2007

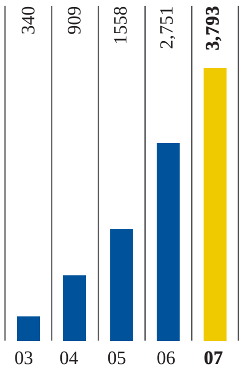
City of London Investment Group PLC is a leading emerging market and natural resource asset management group, specialising in the provision of products and services predominantly to institutional clients who include some of the US's leading institutions and endowment funds. City of London operates its business from offices in London, the US and Singapore.

## Contents

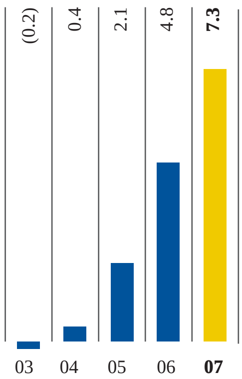
# Highlights

- First full year as a publicly listed company following Admission to AIM in April 2006.
- Funds under management increased by 38% to US$3.79 billion at the year end and by a further 8% to US$4.09 billion at the end of the first quarter at 31st August 2007.
- Profit before tax up 55% to £7.3 million.
- Basic earnings per share up 47% to 19.9p, fully diluted earnings per share up 50% to 17.5p.
- Recommended final dividend of 7p per share payable on 15th November 2007 to shareholders on the register on 2nd November, making a total for the year of 10p.

Funds under management US$m




Pre-tax profit £m




"These record results demonstrate the strength and cash generation characteristics of the Group. Together with the strong ungeared balance sheet, they provide us with a secure platform from which to grow our traditional business lines and to diversify carefully and cautiously into new ones."
Andrew Davison, Chairman

"Since its inception, we have run our business in a manner that is both conservative and relatively unfashionable. We don't manage hedge funds. We don't manage any money from an absolute return perspective, preferring to manage money relative to a benchmark. We manage money using a team approach. We do not encourage the cult of the individual.

"Due to the outperformance of the emerging market asset class we have experienced significant rebalancing. These rebalancings totalled approximately US$269 million. Fortunately, as a result of ongoing good investment performance, these lost assets were replaced. In my opinion this puts us in a good position for a bear market because this will mean that clients are, to a significant extent, *presently* adjusting their exposure to emerging markets, reducing the need for this to occur when markets are falling."
Barry Olliff, Chief Executive

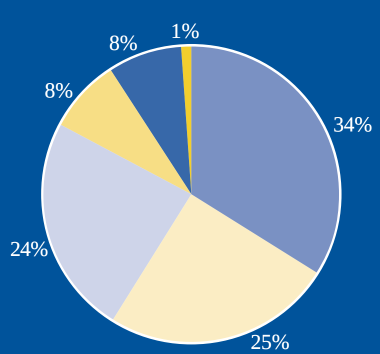
# City of London at a glance

City of London has developed its simple operating philosophy over a number of years. This philosophy can best be represented by the six key drivers we have identified for our business:

1. Our investment performance drives our business
2. We use technology to leverage our capabilities
3. We maintain focus on profits, margins and costs
4. We have an aversion to risk in the management of our business
5. By focussing on the first four drivers, we create opportunities for further growth
6. We maintain our differentiation from competitors and continue to diversify our business.

## Client type

As a percentage of total assets




Endowment
Corporate pension
Foundation
Other institutions
Public pension
Retail

## United Kingdom

The London office, our first, has been based in the City of London since 1991. In London we undertake investment management for our clients and research into our global markets from the European time zone.

## USA

The Group's second office was established near Philadelphia in the United States in 1994 to better service the growing client base in North America and to provide investment management from the Americas time zone.

## Singapore

The third office, to cover Far East emerging markets in real time, opened in central Singapore in 2000, thus positioning the Group to cover our worldwide target investment markets 24 hours a day.

# Chairman's statement

We expect to continue to grow City of London Investment Group for the benefit of its clients and shareholders, managers and staff around the world.

A J Davison
Chairman

I am pleased once again to report a year of good progress for City of London Investment Group, the first full year for which the Group's shares have been quoted on the AIM market of the London Stock Exchange. Since the financial year end in May, the volatility in all markets in which we invest for our clients has increased significantly as a result of the problems first encountered in US credit markets. Although this additional volatility has affected our investment activities in the first quarter of the current financial year, Funds under Management at the end of August totalled some US$4.093 billion compared to the 31st May figure of US$3.793 billion.

Our markets have always been volatile and our performance to date in the new financial year provides, I believe, endorsement that our business model is sufficiently robust to continue to generate outperformance against benchmarks even in recent market conditions. In order to provide some financial protection to the Group from the worst of the volatility, we have this year instituted a limited hedging programme which is described more fully, along with our view of the Group's target investment markets, in the Chief Executive's Review and the Accounts that follow my statement.

## Results

Funds under management during the period under review increased by 38% to US$3.8 billion (2006: US$2.8 billion) reflecting both our outperformance in growing emerging markets and additional funds from existing and new clients. As a result of the growth in funds under management, turnover increased by almost 30% to £18.3 million (2006: £14.1 million). The higher turnover figure translated, due to the operational gearing inherent in our business, into a 55% increase in profit before tax to £7.3 million (2006: £4.7 million after AIM listing costs of £483,000). Net profit for the period after a 34% tax charge (2006: 38%) was £4.9 million (2006: £2.9 million), producing basic earnings per share up 47% to 19.9p (2006: 13.5p) and fully diluted earnings per share of 17.5p (2006: 11.7p).

Retained profit for the year, after the paid and proposed dividend payments set out below was £4.1 million (2006: £0.7 million). As a result of the substantially higher level of retained profits for the year, shareholders' funds almost doubled to £8.6 million (2006: £4.3 million), including cash balances at the year end of £6.6 million (2006: £2.7 million). The Group has no borrowings. A more detailed explanation of the accounts for the year is contained in the Financial Review.

## Dividends

The Board is recommending a final dividend in respect of the financial year to 31st May 2007 of 7p per share. Subject to approval by shareholders at the Annual General Meeting, the dividend will be paid on 15th November 2007 to shareholders on the register on 2nd November 2007. Together with the interim dividend of 3p per share paid in March, this makes a total for the year of 10p. No dividend was paid as a publicly listed company in 2006 reflecting the fact that City of London listed on AIM less than two months before the financial year end.

The Group's dividend policy is based on paying dividends to shareholders that are twice covered by earnings and to pay one third of the annual total as an interim dividend and two thirds as a final dividend. This year's interim dividend of 3p per share therefore implied a final dividend of 6p. In the event, the Board decided to recommend a final dividend of 7p per share taking into account the year end cash balances and the continuing satisfactory financial performance of the Group. Going forward, we intend to maintain our current dividend policy and to declare or recommend dividends with the interim and full year results announced in January and September respectively followed by payments in February and November.

## Review

City of London's investment management services, provided predominantly to institutional clients, are focused on closed-end funds investing in the world's emerging markets. In addition, the Group manages investments in direct equities in both emerging and natural resource markets. We provide our services currently from three offices in the United States, London and Singapore.

The emerging market universe in which we principally invest began the financial year at relatively depressed levels but recovered strongly during the first half and this momentum was maintained during the second half as investment fundamentals in many of the territories remained strong. The positive emerging market performance ended abruptly after the year end as international investors shied away from perceived higher risk investments and markets, following the problems disclosed by lenders in the US mortgage markets. Shareholders should take comfort from the fact that the higher volatility of markets now is an environment we are used to and have successfully dealt with over our history as an investment manager specialising in emerging markets.

Good progress has been made towards our strategic objective to diversify our business. A number of new mandates were won during the period and it is pleasing to report that such success is continuing not only in our traditional core market of North America but also in Europe where we have invested in increased marketing of the Group's services. At the same time, we have been planning the addition – when market conditions are appropriate – of two new funds for European distribution, a natural resources fund and an emerging markets high yield fund. These will provide further diversification from our original investment management activities.

The Group's geographical presence will be expanded with the planned opening of an office in the increasingly important emerging markets of the Middle East. Subject to the necessary regulatory approvals, we expect to open an office in Dubai by the end of the fourth quarter of calendar 2007. Initially this office will have a staff of two.

## Investor Relations and Corporate Governance

As a Company we set great store by being as open as possible with our shareholders and one of the principal means of communication is, of course, the web site (www.citlon.co.uk). This has recently been upgraded so that the Investor Relations section now complies fully with AIM Rule 26, which came into force in August.

## Outlook

We expect to continue to grow City of London Investment Group for the benefit of its clients and shareholders, managers and staff around the world. These record results demonstrate the strength and cash generation characteristics of the Group. Together with the strong ungeared balance sheet, they provide us with a secure platform from which to grow our traditional business lines and to diversify carefully and cautiously into new ones. The current year has started positively with the Group in good shape to deliver further progress, subject only, and always, to the performance of our investment markets.

I am confident that the excellence of our staff combined with the strength of our process will enable us to continue to capitalise to the maximum extent on the opportunities that lie ahead.

Andrew Davison
Chairman
14th September 2007

**The City of London Dragon**
The dragon bearing the shield of St George, with the sword of St Paul in its first quarter, stands as protector at each of the City of London's seven ancient gates, and has become a symbol of the City's strength and security.

# Investment

Starting in London in 1991, the Group has built on its specialist investment expertise in emerging market closed end funds to deliver strong performance for over 15 years.

# Chief Executive Officer's review

The past year has been eventful. Funds under management have increased from \$2.750bn to \$3.793bn. Or measured in sterling from £1.471bn to £1.916bn.

B M Olliff
Chief Executive Officer

### The listing

This is our first full year as a listed company and it's been a surprise to me the extent that, as far as our company is concerned, it's been business as usual. We have not found being listed a distraction. Possibly this was as a result of us having most of the required internal controls in place for many years prior to listing. Neither have there been changes in our Governance. The Board appointed a further Independent Director, David Cardale at the point of listing, but apart from this there has been no noticeable difference in the way we are running the Group.

One item of City of London Investment Management Company's publications that might be of interest to Group shareholders is our Statement on Corporate Governance and Voting Policy for Closed-End Funds, 2007. This is the sixth edition of this document that was first issued in 1999. Where relevant we follow the principles within this document in the running of the Group.

### The past financial year

The past year has been eventful. Funds under management ("FUM") have increased from \$2.750bn to \$3.793bn. Or measured in sterling from £1.471bn to £1.916bn. Due to the ongoing out performance of the emerging market asset class we have experienced significant rebalancing. These rebalancings totalled approximately \$269mn. Fortunately as a result of ongoing good investment performance these lost assets were replaced. In my opinion this puts us in a good position for a bear market because this will mean that clients are, to a significant extent, *presently* adjusting their exposure to emerging markets, reducing the need for this to occur when markets are falling. Please refer to the Financial review on pages 14 to 15 for more information regarding our currency hedging strategy, together with a table on page 15 showing the sensitivity of our income to moves in the \$/£ exchange rate.

In April we started to hedge (you could say) our P&L, but in reality we were hedging our FUM against a fall in world stock markets. Rather than believing that our asset class was expensive we were attempting to take into account that world stock markets seemed expensive (the emerging markets are to some extent priced off world markets), that the move upwards had been very sharp and that our profits were significantly ahead of budget. Our concern was to get a significant percentage of these profits into shareholders hands in the form of dividends. Whilst believing that we remain in an emerging markets secular bull market, we decided to place \$100,000 at the end of April and May (and we continued with this program with similar amounts in June and July) into the purchasing of out of the money puts. As at the end of August the profit on this investment was \$171,325. We review this exposure and value it daily, reflecting its valuation on a monthly basis through our management accounts.

At the point of listing we did not make a forecast regarding dividends for y/e 2007. At the interim stage we declared a dividend of 3p and stated that based upon present conditions we intended to pay a twice covered dividend. At that time that could have been projected as a potential final dividend of 6p. In the event as a result of increased FUM and profits, and subject to ratification by shareholders it is intended to pay a final dividend of 7p.

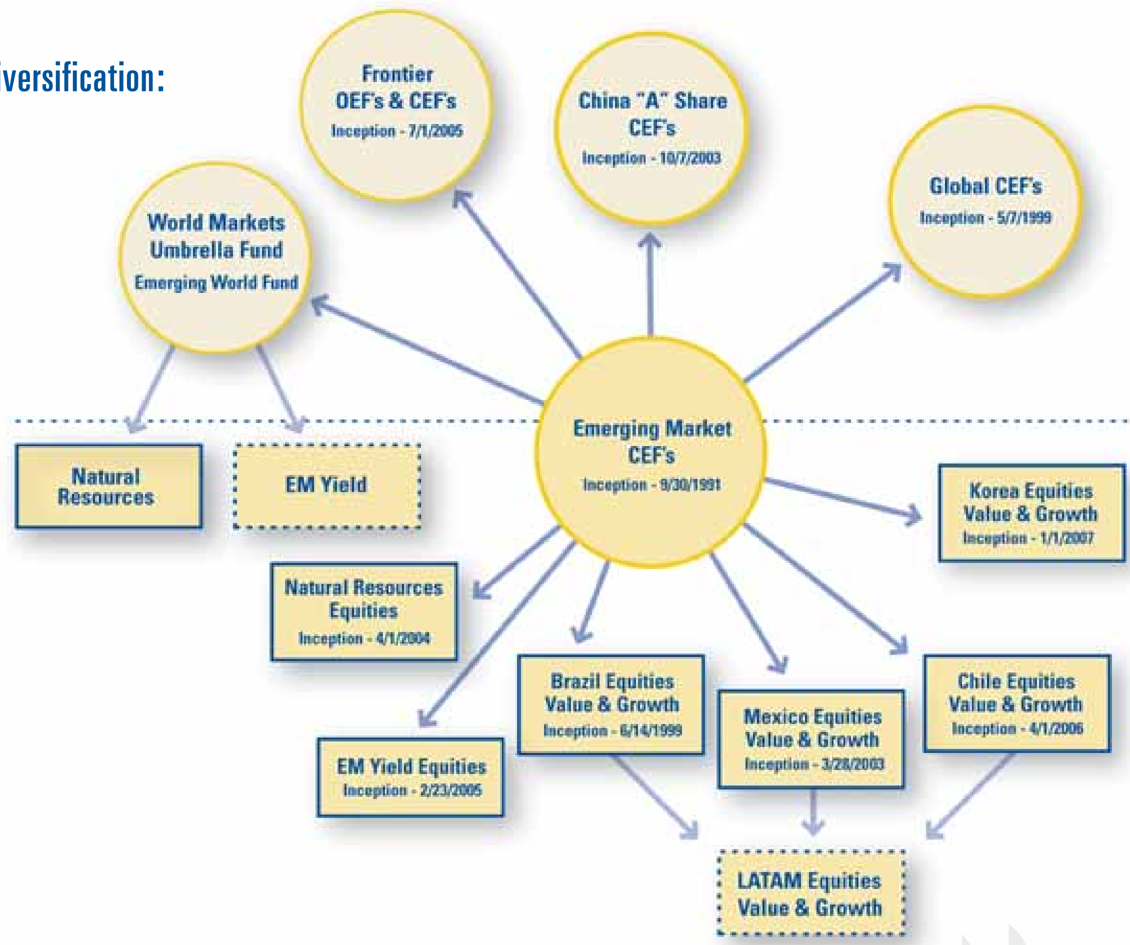
### Diversification

We have developed our diversification plans significantly over the past year and would expect them to continue to develop and bear fruit during the next year. The basis of our diversification plans relate to risk. At the beginning of the decade (31st December 1999), 89% of our assets were US based. If we were to go back even two years, close to 81% of our business was US based and nearly all of the growth was coming from the US too.

A further risk was that we had all of our eggs, you might say, in the Emerging Markets basket.

However, I would point out that when we say we are going to diversify we are not setting targets, we are not going to spend a lot of shareholders' money attempting to achieve an objective in a given time frame, or in a difficult (stock) marketplace. Rather we are going to be opportunistic and, most important, we are not going to

## Diversification:



# Chief Executive Officer's review

Continued

As I reported last year we are focused on developing our business in such a way that enables a significant percentage of any increase in income to flow through to shareholders.

market products that are not either first or second quartile, for to do so would mean that we would be undermining the reputation of the company we work for.

As a result of the above our present diversification, which we plan to be organic, falls into three categories:

1) To diversify our core emerging markets business geographically.

   Since January 2006, the percentage of assets that are sourced outside of the US has increased from 17% to 23%.

2) To use our investment trust discipline in other areas separate from the emerging markets.

   We have recently (in our new financial year) been awarded our first ACWI (ex US) mandate.

3) To develop our emerging markets equities (as compared with closed end funds) business.

### A possible new office

In my previous review I mentioned that we were considering the opening of an office in Dubai. This was principally to add value to our investment process but, I stated, we would hope that over a period of time it could assist in the selling of City of London products. These plans have developed over the past year to the extent that this office will, other things being equal, open during October this year. It will be staffed initially by two existing City of London employees. This office will round out for the foreseeable future our coverage geographically, effectively allowing us to trade in all of the various emerging markets efficiently.

### Business continuity plans

Another year of testing was successfully completed at our off-site disaster recovery centre in London. We extensively tested recovery of mission critical servers from backup tape onto different hardware platforms following our previously tried and tested procedures. We are also in the process of signing up with a leading disaster recovery centre based in Philadelphia, which would provide us with instant desk space for our US office in the event of a disaster type scenario, replicating the London arrangements.

### Cost income ratio

As our FUM grows, so we expect our cost income ratio to fall, and so it has this year, from 56% in fiscal 2006 to 52% in the current year (treating third party marketing commission and custody as a deduction from fees rather than as an expense). We take some pride in the fact that this level is significantly lower than the average for our sector, and it is a fundamental element of our strategy to maintain the focus on costs that enables us to consistently differentiate City of London in this respect. I make no apology for repetition on this point; our ethos would simply not allow us to relax our stance on cost control.

### Operational leverage

As I reported last year we are focused on developing our business in such a way that enables a significant percentage of any increase in income to flow through to shareholders. We do not spend large amounts of shareholders' money on fancy offices, or on travel, or accommodation when on the road. As I mentioned earlier, neither do we intend to throw shareholders' money at diversification. Over many years I've watched financial service companies do this often with very little added value being achieved in terms of measurable success.

The other point about operational leverage that I would like to make is that if you don't spend frivolously you don't have to change habits in the event of a bear market. In other words, keeping expenses low results in higher dividends for shareholders.

### Authorisation and regulation

It seems to me that we, by which I mean our wholly owned subsidiary City of London Investment Management Company Limited ("CoLIM"), are one of the most regulated firms of our size. CoLIM is authorised and regulated by the Financial Services Authority in the UK, is registered as an adviser with the US Securities and Exchange Commission, and is also registered as required by the regulatory authorities in Singapore and Canada. Additionally, CoLIM is currently seeking authorisation from the Dubai Financial Services Authority against the background of the Dubai office intentions as outlined above.

### End of first quarter FUM

At the end of August total FUM were $4.093bn. This compares with $2.815bn at the same point last year. Both FUM and pre-tax profit for the quarter are significantly ahead of our budget.

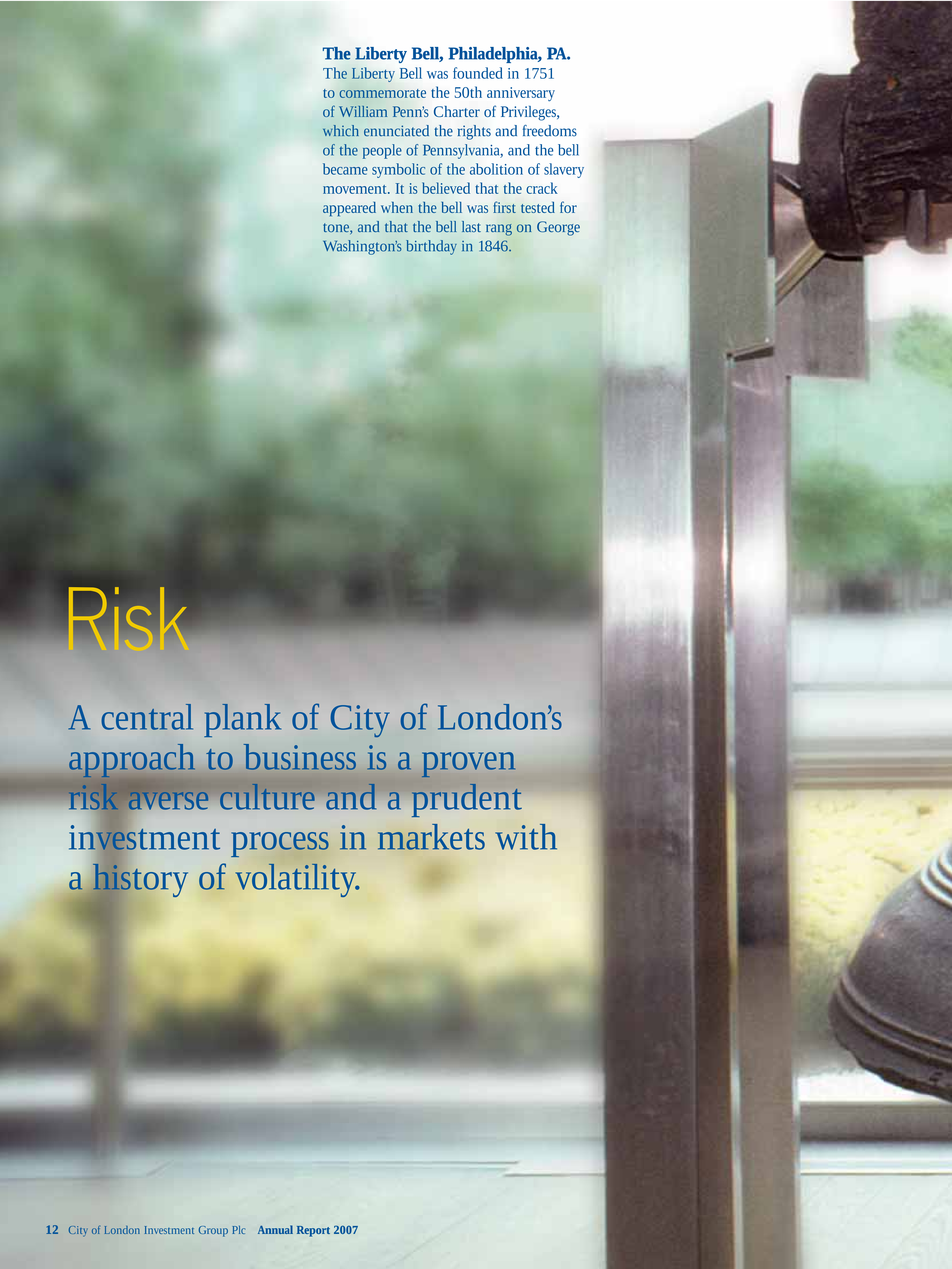
### CoL core values

By now you will be aware of the fact that since our company's inception, we have run our business in a manner that is both conservative and might seem relatively unfashionable. We don't manage Hedge Funds. We don't manage any money from an Absolute return perspective (neither do we participate in out performance), preferring to manage money Relative to a benchmark. We manage money using a team approach. We do not encourage the cult of the individual. The reason that we maintain these core values is that we believe that by doing so we provide better returns for our clients which leads to employment continuity for employees and better returns for our shareholders.

### Thanks to CoL employees.

Finally I would like to thank all of my colleagues for their hard work over the past year in what remains a challenging environment.

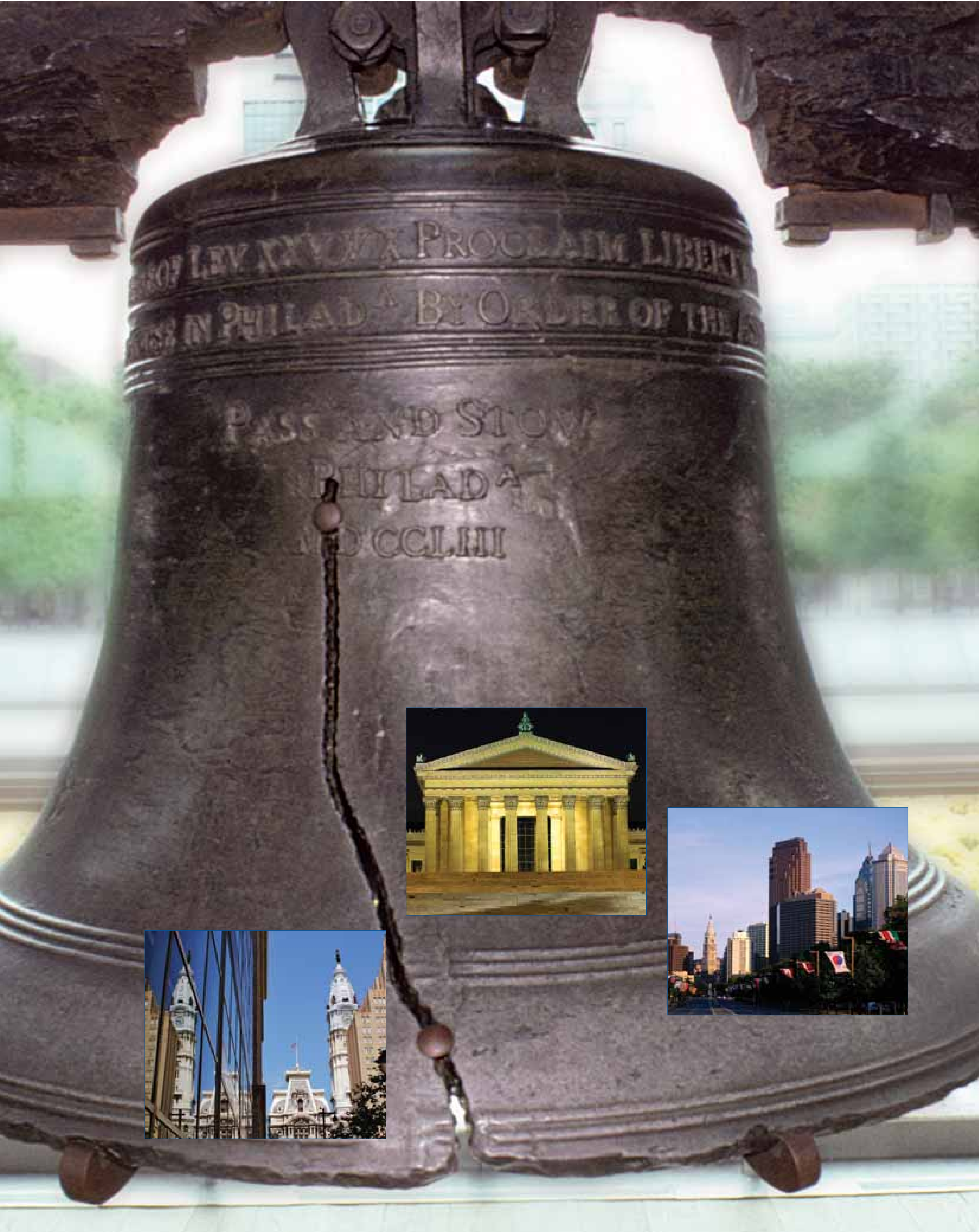
B M Olliff
Chief Executive Officer
14th September 2007



**The Liberty Bell, Philadelphia, PA.**
The Liberty Bell was founded in 1751 to commemorate the 50th anniversary of William Penn's Charter of Privileges, which enunciated the rights and freedoms of the people of Pennsylvania, and the bell became symbolic of the abolition of slavery movement. It is believed that the crack appeared when the bell was first tested for tone, and that the bell last rang on George Washington's birthday in 1846.

# Risk

## A central plank of City of London's approach to business is a proven risk averse culture and a prudent investment process in markets with a history of volatility.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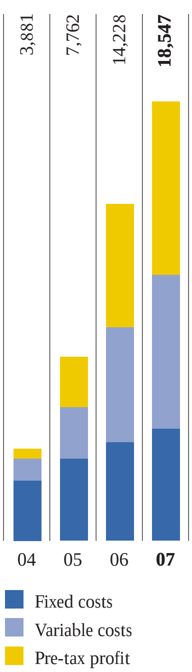
# Financial review

The major change compared to last year is the higher level of retained profit, and consequently cash, arising from the Group's increased profitability during the year.

**Total income £k**




Note: excludes AIM listing costs

D F Allison
Finance Director

### Profit and loss account

Group turnover, management fees charged as a percentage of funds under management (FUM), increased by almost 30%, reflecting the 38% uplift in FUM to a period end figure of US$3.793 billion. As last year, by far the largest proportion of turnover – £16.8 million (2006: £13.2 million) representing 92% (2006: 93%) of the total – was generated in North America. However, progress was made in growing the level of business derived from Europe and turnover generated here doubled to £1.1 million, representing 6% (2006: 4%) of the total for the year.

Administrative Expenses increased by 18% to £11.2 million (2006: £9.5 million). The increase is principally accounted for by higher wage costs resulting from six additional members of staff and the higher levels of bonuses paid during the year, reflecting the Group's increased profitability. Over 50% of Administrative Expenses for the period (2006: 46%) are represented by costs that vary with turnover levels, principally commissions payable to marketing agents at £2.72 million (2006: £2.18 million) and staff profit sharing at £3.15 million (2006: £2.20 million), representing 53% (2006: 47%) of total staff costs.

The dividend for 2007 is the £735,864 cost of the interim dividend of 3p per share paid in March 2007, while the 2006 figure comprises the final dividend for 2005 and the interim and final dividends for 2006, paid before the Company was listed on AIM, which together total £2,282,675.

The Group's tax charge is normally higher than the 30% prevailing rate of UK corporation tax because net income attributable to the US operations attracts the higher US corporate tax rate of marginally in excess of 40%. The overall charge rate this year was 34% (2006: 38% restated), reflecting that most of our managed funds and segregated accounts had a higher weighting towards non-US investments during the period.

### Recognised gains and losses

The revaluation reserve increased by £511,323 to a year end balance sheet figure of £645,829 (2006: £134,506), reflecting the increase in the value of investments made by the Group in order to seed new funds, plus the investment in the options hedging programme referred to in the Chairman's Statement and the Chief Executive's Review. These investments had a market value of £2.30 million (2006: £1.36 million) at the year end, with the increase of £940,000 being attributable approximately 50:50 to net new investments and to the increase in market value.

### Balance sheet

The major change in the consolidated balance sheet compared to last year is the higher level of retained profit, and consequently cash, arising from the Group's increased profitability during the year. As is historically the case for the Group, net current assets of £8.3 million (2006: £4.0 million) represent, at 97% (2006: 93%), by far the largest proportion of total net assets of £8.6 million (2006: £4.3 million).

Debtors and creditors both increased roughly in proportion with the growth in turnover. Cash at bank and in hand at £6.6 million (2006: £2.7 million) represented 77% (2006: 63%) of total net assets.

Investment in own shares increased by £0.55 million to a year end figure of £1.57 million (2006: £1.03 million), representing loans made by the Company to the employee benefit trust to acquire shares for the share option schemes. These loans are repaid on the exercise of options issued by the trust.

### Currency exposure

In line with previous years, some 90% of the Group's income is sourced in US$, but its expenses are roughly evenly divided between sterling and US dollars (with a small Singapore dollar element). As a result, reported sterling net income is significantly exposed to movements in the sterling/US dollar exchange rate, which during the year moved within an approximate range of US$1.80 – 2.00 to £1 (2006: US$1.70 – 1.90 to £1).

The following table illustrates the approximate effect across a range of funds under management assumptions, given the current geographical distribution of the expense base:

| | Average FUM – US$bn | | | |
|---|---|---|---|---|
| | 3.0 | 3.5 | 4.0 | 4.5 |
| US$/£ | Pre-tax, £m | | | |
| 1.90 | 6.4 | 8.0 | 9.7 | 11.3 |
| 1.95 | 6.2 | 7.8 | 9.4 | 11.0 |
| 2.00 | 6.0 | 7.5 | 9.1 | 10.7 |
| 2.05 | 5.8 | 7.3 | 8.8 | 10.4 |
| 2.10 | 5.6 | 7.1 | 8.6 | 10.1 |

Assumes:
1 Average net fee 0.90%.
2 Annual operating costs of £2.5 million plus US$4.2 million plus Singapore $1.2 million.
3 Profit share equivalent to 30% of operating profits.

For example, if funds under management were constant at US$4.0 billion throughout the year, then the impact on sterling pre-tax profit of a move in the exchange rate from US$2.00 to US$2.05 to £1 would be approximately £0.3 million on an annualised basis, if one assumes that none of the exposure is hedged. That said, it is worth repeating that there is a significant degree of natural hedge inherent in our investment process, given that a weaker US dollar gives uplift to our funds under management.

As in previous years, we continue to hedge our balance sheet currency exposure by forward sales, with a total of US$4.5million sold forward at the balance sheet date.

### Share options

The Group regards share options as a vital tool in recruiting, motivating and retaining staff and management. At the period end there were 4,797,675 options on ordinary shares outstanding (2006: 4,747,050), representing 17.9% of the current issued share capital. 2,297,675 of the outstanding options (48% of the total) are over shares held by the Employee Share Option Trust and their eventual exercise will therefore result in no dilution to existing shareholders' interests.

### Change in accounting policy

The Group has adopted accounting standard FRS 20, Share-based Payments. The effect of this was to increase Administrative Expenses in the year to 31st May 2007 by £124,520 and by £64,026 for 2006, which has meant that the 2006 comparative figures have been restated to reflect the adoption. Corresponding amounts have been credited to a Share Option Reserve on the Consolidated Balance Sheet. The charges arise because under FRS 20, the fair value of the employee services received in exchange for share options is recognised as an expense. More detail on the adoption of FRS 20 is contained in Note 1 to the Accounts.

### International Financial Reporting Standards

City of London Investment Group is required to adopt International Financial Reporting Standards (IFRS) for the year ended 31st May 2008. These accounts have been produced in line with UK GAAP. The interim results for the six months to 30th November 2007 will be the first results prepared under IFRS.

D F Allison
Finance Director
14th September 2007

**The Merlion of Singapore**

The Merlion was designed by Fraser Brunner for the Singapore Tourism Board in 1964 and was used as its logo up to 1997 but is still the accepted trademark symbol of Singapore. The lion's head upon a fish's body relates to the story of Sang Nila Utama, the legendary prince and founder of Singapore, who upon finding the mouth of the Singapore River in 11AD and beginning to hunt, saw a strange beast which he took to be a lion, giving the name Singapore, "Singa" lion and "Pura" city. The fish's tail symbolises the city's humble beginnings as a fishing village.

# Technology

## We have consistently used technology to leverage our capabilities across our three offices, to reduce risk and to improve investment performance.

# Board of directors

## A J Davison

NON EXECUTIVE CHAIRMAN

Andrew Davison, a Chartered Accountant, joined County Bank Limited in 1972 and by 1984 had become Managing Director of NatWest Ventures. In 1987 he became Chairman and CEO of Business Mortgages Bank which was sold in 1991. He subsequently joined the Boards of a number of listed and unlisted companies.

## B M Olliff

CHIEF EXECUTIVE OFFICER

Barry Olliff's career has spanned over 40 years within the investment trust (closed-end fund) sector. He began his career in 1964 with Denny Brothers, ultimately Pinchin Denny, as a market maker in the sector. In 1979 he moved to Laing & Cruickshank as a member of their investment trust department, and became a director in 1984. In 1987 he established Olliff & Partners, the stockbroker business from which City of London was founded in the early 1990's.

## D F Allison

FINANCE DIRECTOR

Doug Allison qualified as a Chartered Accountant with Ernst & Young in 1980, and has worked in the financial services sector since 1984, joining City of London in 1997. He is also an Associate of the Chartered Institute of Bankers.

## C M Yuste

BUSINESS DEVELOPMENT DIRECTOR

Carlos Yuste holds a BS in International Relations from the University of Ottawa, and an MA in International Political Economy from Carleton University, also in Ottawa. He worked at the International Development Research Centre in Ottawa from 1994 to 1998, leaving to undertake an International MBA at York University, Toronto, which he completed in 2000 before joining City of London in the same year.

## T W Griffith

CHIEF OPERATING OFFICER

Prior to joining City of London Group in 2000, Thomas Griffith held various positions in the institutional client division of The Vanguard Group including roles as both a Client Relationship Manager and a Marketing Executive. In 1986 he obtained a bachelor's degree in Corporate Finance and Investment Management from the University of Alabama.

## O I Ashur

NON EXECUTIVE DIRECTOR

Omar Ashur is the chief financial officer of FMH, one of the Company's major shareholders and has an MBA and PhD from the Wharton School of the University of Pennsylvania, in Philadelphia.

## D M Cardale

NON EXECUTIVE DIRECTOR

David Cardale is the co-founder and Chairman of Global Investor Relations. He has worked extensively in both Corporate Finance and Private Equity. He has advised a number of fund management groups including Gartmore, Ivory & Sime and NIM, and ran the European operations of NatWest Equity Partners. He has been a director of two London listed Investment Trusts. David Cardale holds an MBA from INSEAD.

## G A Robb

NON EXECUTIVE DIRECTOR

George Robb qualified as a solicitor before becoming fully involved with the asset management sector in 1971. In 1994 he established Asset Management Investment Company PLC as a specialist vehicle investing in the asset management sector and was appointed managing director on its flotation. He is a non-executive director of several companies in which AMIC is invested.

# Officers and Board Committees

| | Board | Audit Committee | Remuneration Committee | Other |
|---|---|---|---|---|
| D F Allison | *Executive* | | | *Secretary* |
| O I Ashur | *Non-executive* | • | • | |
| D M Cardale | *Non-executive* | • | • | |
| A J Davison | *Chairman Non-executive* | • *Chairman* | • | |
| T W Griffith | *Executive* | | | |
| B M Olliff | *Executive* | | | |
| G A Robb | *Non-executive* | • | • *Chairman* | |
| C M Yuste | *Executive* | | | |

# Professional advisers

**Nominated advisers and brokers**
Landsbanki
Beaufort House
15 St Botolph Street
London
EC3A 7QR

**Bankers**
The Royal Bank of Scotland plc
London City Office
62-63 Threadneedle Street
London
EC2R 8LA

**Auditors**
Moore Stephens LLP
Chartered Accountants
St. Paul's House
Warwick Lane
London
EC4M 7BP

**Registrars**
Capita Registrars
The Registry
34 Beckenham Road
Beckenham
Kent
BR3 4TU

**Financial communications**
Tavistock Communications
13 Finsbury Pavement
London
EC2A 1NT

# Registered Office

10 Eastcheap
London
EC3M 1LX

# Report of the directors

The directors present their annual report and the audited financial statements for the year ended 31st May 2007.

## Principal activity and review of business

City of London Investment Group Plc is the holding company for a number of investment management subsidiaries. The principal operating subsidiary is City of London Investment Management Company Limited, which acts as an investment adviser and which advises on 27 accounts (2006 – 22 accounts) with a total of £1,916m (2006 – £1,471m) under management as at the end of the year.

The Report of the directors should be read in conjunction with the Chairman's statement, the Chief Executive Officer's review, and the Financial review on pages 4 to 15, which together provide a commentary on the operations of the Group.

## Future prospects

The Board is optimistic as to the future and is committed to increasing the Group's funds under management.

## Results and dividend

The results of the Group for the year, together with details of amounts transferred to reserves, are set out on page 28. The Company has paid dividends of £735,864 during the year (2006 – £2,282,675). The final dividend for the year to 31st May 2007 will be paid in November 2007, subject to approval.

## Corporate governance

(a) The Board of directors

The Board recognises the importance of good corporate practice and is committed to maintaining high standards of corporate governance throughout the Group. The Board comprises four executive directors and four non-executive directors. The directors intend to comply with the Combined Code in such respects as are appropriate for a company of this size, nature and stage of development.

The Board meets regularly and has overall responsibility for ensuring that the Group is properly led and controlled, and is accountable to shareholders for financial and operational performance. These responsibilities include the overall strategy of the Group, approval of significant items of expenditure and consideration of significant financing matters pertaining to the Group.

The Board has established an Audit Committee, a Remuneration Committee and a Nominations Committee (each comprising the four non-executive directors, who will invite other members of the Board to join meetings) with formally delegated duties and responsibilities.

(b) The Remuneration Committee

The Remuneration Committee is chaired by George Robb. It reviews the performance of executive directors and sets the scale and structure of their remuneration and reviews the basis of their service agreements with due regard to the interests of the shareholders. The Remuneration Committee also makes recommendations to the Board concerning the allocation of share options to directors and employees. The remuneration and terms of appointment of non-executive directors will be set by the Board.

The Company has a remuneration policy, the aim of which is to provide, in the context of the Group's business strategy, remuneration that will attract and retain high calibre executives and staff. In order to achieve this, total rewards are set at levels that are competitive within the relevant market. Rewards are earned through the achievement of objectives based on measures consistent with shareholder interests.

(c) The Audit Committee

The Audit Committee is chaired by Andrew Davison. It meets at least twice each year and is responsible for monitoring the quality of internal control, ensuring that the financial performance of the Company is properly measured and reported on, meeting with the auditors and reviewing reports from the auditors relating to accounting and internal controls.

The finance director is invited to attend meetings but the committee meets with the auditors at least once a year without the finance director being present.

# Report of the directors

Continued

(d) The Nominations Committee
The Nominations Committee is chaired by Andrew Davison. It is responsible for reviewing and proposing appointments to the Board and the various Board committees. In addition, the committee has responsibility for reviewing the composition of the Board and for selecting candidates for appointment, to meet the desired composition.

(e) Corporate Governance in Investee Closed-End Funds
Since 1999, City of London has produced a detailed statement outlining the corporate governance procedures and policies it expects to be employed by closed-end funds in which we invest. The sixth edition of our "Statement of Corporate Governance and Voting Policy for Closed-End Funds" was circulated in June 2007. In publishing this statement we attempt to capture the current best practices in the corporate governance of closed-end funds.

Corporate governance is an integral part of our investment process because it is our firm belief that a closed-end fund with poor corporate governance will generally trade at a wide discount over time. Poor corporate governance in a closed-end fund results in fund price under-performance via the widening of the discount to the Net Asset Value at which the fund trades.

Our statement is addressed to Boards, Managers, Shareholders, and the Professional community. It attempts to define the responsibilities of all the parties involved within a closed-end fund, with the ultimate aim of promoting shareholder value and the long-term interests of the closed-end fund sector.

A copy of our statement is distributed to the members of the Boards of the closed-end funds in which we invest and is available on our website.

## Directors interests and remuneration

(a) Shareholdings
The directors who served throughout the year and their interests in the Company were as follows:

| | Ordinary Shares of 1p each 2007 | Ordinary Shares of 1p each 2006 |
|---|---|---|
| A J Davison *(Chairman) (non-executive)* | 49,000 | 49,000 |
| B M Olliff | 3,763,250 | 3,763,250 |
| D F Allison | 175,625 | 165,625 |
| T W Griffith | 16,575 | 14,075 |
| C M Yuste | 16,575 | 16,575 |
| G A Robb *(non-executive)* | – | – |
| O I Ashur *(non-executive)* | 5,000 | – |
| D M Cardale *(non-executive)* | – | – |

(b) Share options

At 31st May 2007 share options were held by the following directors:

| | Number | Exercise price £ | Date from which exercisable | Expiry date |
|---|---|---|---|---|
| B M Olliff | 62,500 | 0.45 | 10th January 2004 | 10th January 2008 |
| | 62,500 | 0.45 | 13th September 2004 | 13th September 2008 |
| | 189,000 | 0.29 | 14th May 2007 | 14th May 2009 |
| | 311,000 | 0.26 | 14th May 2007 | 14th May 2014 |
| | 25,000 | 1.40 | 31st March 2009 | 31st March 2016 |
| | 5,000 | 2.61 | 30th January 2010 | 30th January 2017 |
| | 5,000 | 2.73 | 30th March 2010 | 30th March 2017 |
| D F Allison | 52,500 | 0.45 | 10th January 2004 | 10th January 2008 |
| | 62,500 | 0.45 | 13th September 2004 | 13th September 2008 |
| | 250,000 | 0.26 | 14th May 2007 | 14th May 2014 |
| | 18,750 | 1.40 | 31st March 2009 | 31st March 2016 |
| | 5,000 | 2.61 | 30th January 2010 | 30th January 2017 |
| | 5,000 | 2.73 | 30th March 2010 | 30th March 2017 |
| T W Griffith | 50,000 | 0.45 | 10th January 2004 | 10th January 2011 |
| | 33,350 | 0.45 | 13th September 2004 | 13th September 2008 |
| | 16,650 | 0.45 | 13th September 2004 | 13th September 2011 |
| | 250,000 | 0.26 | 14th May 2007 | 14th May 2014 |
| | 12,500 | 1.40 | 31st March 2009 | 31st March 2016 |
| | 5,000 | 2.61 | 30th January 2010 | 30th January 2017 |
| | 5,000 | 2.73 | 30th March 2010 | 30th March 2017 |
| C M Yuste | 50,000 | 0.45 | 10th January 2004 | 10th January 2011 |
| | 33,350 | 0.45 | 13th September 2004 | 13th September 2008 |
| | 16,650 | 0.45 | 13th September 2004 | 13th September 2011 |
| | 250,000 | 0.26 | 14th May 2007 | 14th May 2014 |
| | 12,500 | 1.40 | 31st March 2009 | 31st March 2016 |
| | 5,000 | 2.61 | 30th January 2010 | 30th January 2017 |
| | 5,000 | 2.73 | 30th March 2010 | 30th March 2017 |

# Report of the directors

Continued

(c) Remuneration

The remuneration of the directors who held office during the year ended 31st May 2007 is set out below:

| | Salary £ | Profit share £ | Health insurance £ | Total 2007 £ | Total 2006 £ | Pension 2007 £ | Pension 2006 £ |
|---|---|---|---|---|---|---|---|
| Non-executive | | | | | | | |
| A J Davison | 30,000 | – | – | 30,000 | 25,764 | – | – |
| G A Robb | 20,000 | – | – | 20,000 | 15,764 | – | – |
| O I Ashur | 20,000 | – | – | 20,000 | 15,764 | – | – |
| D M Cardale | 20,000 | – | – | 20,000 | 4,483 | – | – |
| | 90,000 | – | – | 90,000 | 61,775 | – | – |
| Executive | | | | | | | |
| B M Olliff | 182,200 | 676,741 | – | 858,941 | 727,182 | 22,775 | 24,632 |
| D F Allison | 135,000 | 305,250 | 1,059 | 441,309 | 340,981 | 16,875 | 15,626 |
| T W Griffith | 104,114 | 165,411 | – | 269,525 | 212,535 | 13,014 | 10,732 |
| C M Yuste | 104,114 | 165,411 | – | 269,525 | 212,535 | 13,014 | 10,732 |
| | 525,428 | 1,312,813 | 1,059 | 1,839,300 | 1,493,233 | 65,678 | 61,722 |

## Substantial shareholdings

At 25th August 2007, the Company had been notified of the following interests of 3% or more in the Company's ordinary shares:

| Interested party | Number of shares | Percentage of issued shares |
|---|---|---|
| FMH Investments NV | 7,929,425 | 29.61 |
| B M Olliff | 3,763,250 | 14.05 |
| F&C Asset Management | 2,521,447 | 9.42 |
| The City of London Employee Share Option Trust | 2,303,125 | 8.60 |
| BlackRock Investment Management | 2,120,500 | 7.92 |
| Asset Management Investment Company PLC | 1,781,275 | 6.65 |
| JP Morgan Asset Management | 954,932 | 3.57 |
| Axa Framlington Investment Managers | 880,000 | 3.29 |

## Creditor payment policy

The Company's current policy concerning the payment of its trade creditors is to:

(a) settle the terms of payment with suppliers when agreeing the terms of each transaction;

(b) ensure that suppliers are made aware of the terms of payment; and

(c) abide by the terms of payment.

The payment policy applies to all payments to suppliers for revenue and capital supplies of goods and services without exception.

As at 31st May 2007, the creditor days were Nil (2006 – Nil).

## Donations

During the year the Group made charitable donations of £5,000.

## Auditors

A resolution to re-appoint Moore Stephens LLP as the Company's auditor will be put to the forthcoming Annual General Meeting.

Each of the persons who are directors at the time when this report is approved has confirmed that:

(a) so far as each director is aware, there is no relevant audit information of which the Company's auditors are unaware; and

(b) each director has taken all the steps that ought to have been taken as a director, including making appropriate enquiries of fellow directors and the Company's auditors for that purpose, in order to be aware of any information needed by the Company's auditors in connection with preparing their report and to establish that the Company's auditors are aware of that information.

Approved by the Board of directors and signed on behalf of the Board

D F Allison
Company Secretary
14th September 2007

# Statement of directors' responsibilities

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

– select suitable accounting policies and then apply them consistently;

– make judgements and estimates that are reasonable and prudent;

– state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;

– prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for the system of internal control, for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

# Independent auditors' report to the shareholders of City of London Investment Group plc

We have audited the Group and Parent Company financial statements (the "financial statements") of City of London Investment Group plc for the year ended 31st May 2007 which are set out on pages 28 to 44. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

## Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of directors' responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

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

We report to you whether in our opinion the information given in the directors' report is consistent with the financial statements. In addition, we read other information contained in the Annual Report. This other information comprises the Introduction and highlights, the Chairman's statement, the Chief Executive Officer's review and the Financial review. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

## Basis of audit opinion

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

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

## Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Group's and the Parent Company's affairs as at 31st May 2007 and of the Group's profit for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the directors' report is consistent with the financial statements.

Moore Stephens LLP
14th September 2007
Registered Auditors and Chartered Accountants
St Paul's House, Warwick Lane, London EC4M 7BP

# Consolidated profit and loss account

For the year ended 31st May 2007

| | Note | Total 2007 £ | Total 2006 (as restated) £ |
|---|---|---|---|
| Turnover | 1,2 | 18,304,881 | 14,118,639 |
| Administrative expenses | | | |
| Staff costs | 4(b) | 5,954,730 | 4,568,763 |
| Other administrative expenses | | 5,139,946 | 4,350,907 |
| AIM listing costs | | – | 482,708 |
| Depreciation | | 120,494 | 108,112 |
| | | (11,215,170) | (9,510,490) |
| Other operating income | | – | 9,520 |
| Operating profit | 6 | 7,089,711 | 4,617,669 |
| Interest receivable and similar income | 7 | 242,103 | 109,562 |
| Profit on ordinary activities before taxation | | 7,331,814 | 4,727,231 |
| Tax charge on profit on ordinary activities | 8 | (2,457,856) | (1,784,138) |
| Profit on ordinary activities after taxation | | 4,873,958 | 2,943,093 |
| Dividends | 9 | (735,864) | (2,282,675) |
| Retained profit for the financial year | 17 | 4,138,094 | 660,418 |
| Basic profit per share | 10 | 19.9p | 13.5p |
| Diluted profit per share | 10 | 17.5p | 11.7p |

# Consolidated statement of total recognised gains and losses

For the year ended 31st May 2007

| | Note | 2007 £ | 2006 (as restated) £ |
|---|---|---|---|
| Retained profit for the period | | 4,138,094 | 660,418 |
| Increase in revaluation reserve | | 511,323 | 134,506 |
| Total recognised gains and losses for the period | | 4,649,417 | 794,924 |
| Prior year adjustment | 17 | (106,325) | |
| Total gains and losses recognised since the last annual report | | 4,543,092 | |

# Consolidated balance sheet

31st May 2007

| | Note | 2007 £ | 2006 (as restated) £ |
|---|---|---|---|
| **Fixed assets** | | | |
| Tangible assets | 11 | 193,362 | 225,939 |
| Investments | 12 | 46,859 | 61,253 |
| | | 240,221 | 287,192 |
| **Current assets** | | | |
| Debtors | 13 | 2,613,212 | 2,136,312 |
| Investments | 14 | 2,299,325 | 1,359,563 |
| Cash at bank and in hand | | 6,616,824 | 2,708,915 |
| | | 11,529,361 | 6,204,790 |
| **Creditors, amounts falling due within one year** | 15 | (3,210,074) | (2,160,169) |
| **Net current assets** | | 8,319,287 | 4,044,621 |
| **Total assets less current liabilities** | | 8,559,508 | 4,331,813 |
| **Capital and reserves** | | | |
| Called up share capital | 16 | 267,777 | 267,777 |
| Share premium account | 17 | 1,357,283 | 1,357,283 |
| Investment in own shares | 17 | (1,573,525) | (1,027,283) |
| Revaluation reserve | 17 | 645,829 | 134,506 |
| Share option reserve | 17 | 230,845 | 106,325 |
| Profit and loss account | 17 | 7,631,299 | 3,493,205 |
| **Shareholders' funds** | 17 | 8,559,508 | 4,331,813 |

The Board of directors approved these financial statements on 14th September 2007.

Signed on behalf of the Board of directors

B M Olliff
Chief Executive Officer

D F Allison
Finance Director

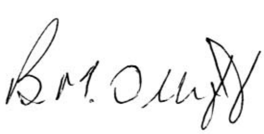
# Company balance sheet

31st May 2007

| | Note | 2007<br>£ | 2006<br>(as restated)<br>£ |
|---|---|---|---|
| **Fixed assets** | | | |
| Tangible assets | 11 | 74,748 | 63,252 |
| Investments | 12 | 621,789 | 636,187 |
| | | 696,537 | 699,439 |
| **Current assets** | | | |
| Debtors | 13 | 3,407,872 | 632,617 |
| Investments | 14 | 2,299,325 | 1,359,563 |
| Cash at bank and in hand | | 427,988 | 35,261 |
| | | 6,135,185 | 2,027,441 |
| Creditors, amounts falling due within one year | 15 | (3,318,544) | (1,093,182) |
| Net current assets | | 2,816,641 | 934,259 |
| Total assets less current liabilities | | 3,513,178 | 1,633,698 |
| **Capital and reserves** | | | |
| Called up share capital | 16 | 267,777 | 267,777 |
| Share premium account | 17 | 1,357,283 | 1,357,283 |
| Investment in own shares | 17 | (1,573,525) | (1,027,283) |
| Revaluation reserve | 17 | 645,829 | 134,506 |
| Share option reserve | 17 | 230,845 | 106,325 |
| Profit and loss account | 17 | 2,584,969 | 795,090 |
| Shareholders' funds | 17 | 3,513,178 | 1,633,698 |

The Board of directors approved these financial statements on 14th September 2007.

Signed on behalf of the Board of directors



B M Olliff
Chief Executive Officer

D F Allison
Finance Director

# Cash flow statement

For the year ended 31st May 2007

| | Note | 2007 £ | 2006 £ |
|---|---|---|---|
| **Consolidated cash flow statement** | | | |
| Net cash inflow from operating activities | 20 | 7,708,693 | 4,145,424 |
| Returns on investments and servicing of finance | 21 | 196,487 | 109,562 |
| Taxation | 21 | (2,190,642) | (1,643,687) |
| Capital expenditure and financial investment | 21 | (58,545) | (164,267) |
| Equity dividends paid | | (735,864) | (2,282,675) |
| Financing | 21 | (546,242) | 907,685 |
| Management of liquid resources | 21 | (465,978) | (761,167) |
| Increase in cash | 23 | 3,907,909 | 310,875 |

# Notes to the financial statements

For the year ended 31st May 2007

## 1 Accounting policies

The financial statements are prepared in accordance with applicable United Kingdom law and accounting standards. The principal accounting policies adopted by the directors are set out below.

(a) Consolidation

These financial statements consolidate the financial statements of the Company and all of its subsidiary undertakings. The Company's principal subsidiaries are City of London Investment Management Company Limited and City of London US Services Limited, all other subsidiaries being dormant at 31st May 2007.

Goodwill of £25,023 arising on the acquisition of the subsidiary undertakings, being the excess of cost over the fair value of the net tangible assets acquired, was written off directly to reserves in the year of acquisition for those acquisitions prior to 23rd December 1998. Any goodwill arising on subsequent acquisitions will be capitalised and amortised over its useful economic life.

(b) Turnover

Turnover arises in North America, Europe and Australia and comprises investment management fees earned. Fees are recognised in turnover as the investment management services are provided, in accordance with the underlying agreements.

(c) Foreign currency translation

Monetary assets and liabilities denominated in foreign currencies are translated into sterling at the rates of exchange ruling at the balance sheet date and any exchange differences arising are dealt with through the profit and loss account.

(d) Tangible fixed assets and depreciation

For all tangible fixed assets depreciation is calculated to write off their cost to their estimated residual values by equal annual instalments over the period of their estimated useful lives, which are considered to be:

| | | |
|---|---|---|
| Short leasehold property improvements | – | over the remaining life of the lease |
| Furniture and equipment | – | four years |
| Computer and telephone equipment | – | four years |

(e) Investments

Fixed asset investments are stated at cost less provision for any impairment in value.

Current asset investments are those investments which are considered to be liquid assets. They are stated at market value, and unrealised gains and losses are reflected in the revaluation reserve in accordance with the alternative accounting rules of the Companies Act 1985.

(f) Leases

The cost of operating leases is charged to the profit and loss account in equal periodic instalments over the periods of the leases.

(g) Pensions

The Group operates defined contribution pension schemes covering the majority of its employees. The costs of the pension schemes are charged to the profit and loss account as they accrue.

(h) Deferred taxation

Deferred tax is provided in full on timing differences which result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates that are expected to apply when they crystallise based on current tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the financial statements. Deferred tax assets are recognised to the extent that it is regarded more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

## 1 Accounting policies continued

(i) Comparatives

Comparatives have been restated in respect of "Share-based payments" in accordance with FRS 20.

(j) Change in accounting policy

In preparing the financial statements for the current period, the Group has adopted FRS 20 "share-based payments". The effect of this change in policy on the financial statements is to increase the administrative costs as detailed below. A corresponding amount is credited to a share option reserve in accordance with FRS 20.

| End of accounting period | Share-based payment | Total share option reserve |
|---|---|---|
| 31st May 2005 | 42,299 | 42,299 |
| 30th November 2005 | 27,301 | 69,600 |
| 31st May 2006 | 36,725 | 106,325 |
| 30th November 2006 | 56,657 | 162,982 |
| 31st May 2007 | 67,863 | 230,845 |

Share-based payments

The Company operates an Employee Share Option Plan. In accordance with FRS 20, the fair value of the employee services received in exchange for share options is recognised as an expense. The fair value has been calculated using the Binomial pricing model, and has then been expensed on a straight line basis over the vesting period of three years, based on the Company's estimate of the number of shares that will actually vest.

The estimated fair values of options which fall under FRS 20, and the inputs used in the Binomial pricing model to calculate those fair values, are as follows:

| Date of grant | Expiry date | Expected life (yrs) | Risk-free rate | Share price at grant (£) | Exercise price (£) | Volatility | Dividend yield | Estimated fair value (£) | Number outstanding |
|---|---|---|---|---|---|---|---|---|---|
| 14/05/2004 | 14/05/2014 | 3.00 | 5.0411% | 0.2600 | 0.2600 | 33.5589% | 4.50% | 0.0668 | 2,000,000 |
| 17/12/2004 | 17/12/2014 | 3.00 | 4.5420% | 0.4500 | 0.4500 | 30.9463% | 4.50% | 0.1061 | 536,250 |
| 31/03/2006 | 31/03/2016 | 3.00 | 4.5300% | 1.4000 | 1.4000 | 25.4798% | 4.50% | 0.2450 | 818,750 |
| 10/10/2006 | 10/10/2016 | 3.00 | 4.9865% | 1.8000 | 1.8000 | 29.3594% | 4.50% | 0.3196 | 50,000 |
| 30/01/2007 | 30/01/2017 | 3.00 | 5.4828% | 2.6100 | 2.6100 | 29.8223% | 4.50% | 0.4834 | 140,500 |
| 30/03/2007 | 31/03/2017 | 3.00 | 5.4338% | 2.7300 | 2.7300 | 29.3557% | 4.50% | 0.4948 | 143,500 |

The expected life of the options has been assumed to be three years based upon the empirical evidence available. The risk-free rate has been assumed to be represented by the yield to maturity at the date of grant of a UK Gilt strip with term to maturity equal to the expected life of the option. The volatility of the Company's share price at each date of grant has been calculated as the average of the standard deviations of daily continuously compounded returns on the stock of a group of comparable companies.

In accordance with the transitional provisions, FRS 20 has been applied only to grants of share options after 7th November 2002 that had not vested as at 1st June 2006, although, as required by FRS20, the disclosures below include grants of share options prior to 7th November 2002.

# Notes to the financial statements

Continued

## 1 Accounting policies continued

The number and weighted average exercise price of share options for each of the following groups is as follows:

| | 2007 Number | 2007 Weighted average exercise price | 2006 Number | 2006 Weighted average exercise price |
|---|---|---|---|---|
| Outstanding at the beginning of the year | 4,747,050 | 0.54 | 4,435,350 | 0.36 |
| Granted during the year | 334,000 | 2.54 | 825,000 | 1.40 |
| Forfeited during the year | 6,250 | 1.40 | – | – |
| Exercised during the year | 277,125 | 0.45 | 513,300 | 0.45 |
| Expired during the year | – | – | – | – |
| Outstanding at the end of the year | 4,797,675 | 0.68 | 4,747,050 | 0.54 |
| Exercisable at the end of the year | 3,108,675 | 0.33 | 1,385,800 | 0.45 |
| The weighted average share price at the date of exercise for share options exercised during the year was | | 214.45 | | – |

(2006: No share prices available prior to AIM listing)

## 2 Turnover

| | 2007 £ | 2006 £ |
|---|---|---|
| Management fees earned by subsidiary companies charged as a percentage of funds under management | 18,304,881 | 14,118,639 |

## 3 Analysis of turnover, operating profit and net assets

The directors consider that the Group only undertakes one class of business, and hence only analysis by geographical location is given.

| | Turnover | | Operating profit | | Net assets | |
|---|---|---|---|---|---|---|
| | 2007 £ | 2006 £ | 2007 £ | 2006 (as restated) £ | 2007 £ | 2006 (as restated) £ |
| Europe | 1,130,223 | 585,206 | 601,146 | 855,197 | 6,606,459 | 2,367,636 |
| North America | 16,780,057 | 13,185,903 | 6,301,978 | 3,538,613 | 1,923,885 | 1,921,165 |
| South America | – | 298,173 | – | 205,660 | 1,643 | 2,973 |
| Other | 394,601 | 49,357 | 186,587 | 18,199 | 27,520 | 40,039 |
| | 18,304,881 | 14,118,639 | 7,089,711 | 4,617,669 | 8,559,508 | 4,331,813 |

## 4 Employees

(a) Average number of persons employed by the Group in the year:

| | 2007 Number | 2006 Number |
|---|---|---|
| Investment management staff | 9 | 9 |
| Sales and dealing staff | 2 | 2 |
| Research staff | 10 | 7 |
| Administration accounts and settlement staff | 23 | 20 |
| | 44 | 38 |

## 4 Employees continued

(b) Staff costs incurred during the year in respect of these employees were:

| | 2007 £ | 2006 (as restated) £ |
|---|---|---|
| Wages and salaries | 2,256,950 | 1,960,784 |
| Profit sharing payments | 2,923,952 | 2,024,485 |
| Social security costs | 395,124 | 299,276 |
| Defined contribution pension costs | 254,184 | 220,192 |
| Share options charge | 124,520 | 64,026 |
| | 5,954,730 | 4,568,763 |

The Group made contributions of £254,184 (2006 – £220,192) in the period to individual defined contribution pension schemes established for directors and employees. There were no outstanding or prepaid contributions at the balance sheet date.

## 5 Directors

| Directors' emoluments comprise: | 2007 £ | 2006 £ |
|---|---|---|
| Emoluments (excluding pension contributions and awards under share option schemes) | 1,929,300 | 1,555,008 |
| Pension contributions | 65,678 | 61,722 |

| | 2007 Number | 2006 Number |
|---|---|---|
| Number of directors on whose behalf pension contributions were paid during the year | 4 | 4 |
| Number of directors who exercised share options during the period | 1 | 2 |

| Highest paid director's remuneration: | 2007 £ | 2006 £ |
|---|---|---|
| Emoluments (excluding pension contributions and awards under share option schemes and other long-term incentive schemes) | 858,941 | 727,181 |
| Pension contributions | 22,775 | 24,632 |

## 6 Operating profit

| The operating profit is arrived at after charging: | 2007 £ | 2006 (as restated) £ |
|---|---|---|
| Depreciation of owned assets | 120,494 | 108,112 |
| Auditors' remuneration: | | |
| – Statutory audit | 31,510 | 30,000 |
| – Taxation services | 12,337 | 22,810 |
| – Corporate finance services | – | 97,539 |
| – Other services | 5,575 | 34,243 |
| Operating lease rentals: | | |
| – Land and buildings | 135,418 | 136,494 |
| – Other | 6,543 | 7,022 |

# Notes to the financial statements

Continued

## 7 Interest receivable and similar income

| | 2007 £ | 2006 £ |
|---|---|---|
| Interest on bank deposit | 196,487 | 109,562 |
| Profit on sale of investments | 45,616 | – |
| | 242,103 | 109,562 |

## 8 Tax charge on profit on ordinary activities

(a) Analysis of tax charge on ordinary activities:

| | 2007 £ | 2006 £ |
|---|---|---|
| Tax at 30% (2006 – 30%) based on the profit for the year | 2,260,228 | 1,538,223 |
| Double taxation relief | (542,228) | (415,360) |
| Adjustments in respect of prior years | (11,518) | (3,148) |
| | 1,706,482 | 1,119,715 |
| Foreign tax for the current period | 778,144 | 652,983 |
| Adjustments in respect of prior years | (26,770) | 11,440 |
| | 751,374 | 664,423 |
| | 2,457,856 | 1,784,138 |

(b) Factors affecting tax charge for the current period:

The tax assessed for the period is different to that resulting from applying the standard rate of corporation tax in the UK: 30% (prior year: 30%). The differences are explained below:

| | 2007 £ | 2006 (as restated) £ |
|---|---|---|
| Profit on ordinary activities before tax | 7,331,814 | 4,727,231 |
| Tax at 30% thereon | (2,199,544) | (1,418,169) |
| Effects of: | | |
| Expenses not deductible for tax purposes | (41,353) | (119,208) |
| Capital allowances less than depreciation | (16,733) | – |
| Unrelieved overseas tax | (235,916) | (237,623) |
| Prior period adjustments | 38,288 | (8,292) |
| Other | (2,598) | (846) |
| | (2,457,856) | (1,784,138) |

The Company has revalued its current asset investments to market value. Deferred tax has not been recognised on this revaluation, but the estimated tax payable if the investments were sold at the values shown is £193,749 (2006 – £40,352).

## 9 Dividend

| | 2007 £ | 2006 £ |
|---|---|---|
| Dividends paid: | | |
| Interim dividend of £0.03 per share (2006 – £0.09) | 735,864 | 1,982,662 |
| Final dividend in respect of year ended: | | |
| 31st May 2005 of £0.36 per share | – | 300,013 |
| | 735,864 | 2,282,675 |

## 10 Earnings per share

The calculation of earnings per share is based on the profit for the period of £4,873,958 (2006 restated – £2,943,093) divided by the weighted average number of ordinary shares in issue for the year ended 31st May 2007 of 24,432,528 (2006 – 21,855,212).

As set out in Note 17 the Employee Benefit Trust held 2,303,125 ordinary shares in the Company as at 31st May 2007. The Trustees of the Trust have waived all rights to dividends associated with these shares. In accordance with FRS 22 the ordinary shares held by the Employee Benefit Trust have been excluded from the calculation of the weighted average of ordinary shares in issue.

The calculation of diluted earnings per share is based on the profit for the year of £4,873,958 (2006 restated – £2,943,093) divided by the diluted weighted average of ordinary shares for the year ended 31st May 2007 of 27,823,144 (2006 – 25,272,459).

Reconciliation of the figures used in calculating basic and diluted earnings per share:

| | 2007 Number of shares | 2006 Number of shares |
|---|---|---|
| Weighted average number of shares – basic earnings per share | 24,432,528 | 21,855,212 |
| Effect of dilutive potential shares – share options | 3,390,616 | 3,417,247 |
| Weighted average number of shares – diluted earnings per share | 27,823,144 | 25,272,459 |

## 11 Tangible fixed assets

| Group | Furniture and equipment £ | Computer and telephone equipment £ | Short leasehold improvements £ | Total £ |
|---|---|---|---|---|
| Cost | | | | |
| At 1st June 2006 | 94,697 | 587,580 | 159,163 | 841,440 |
| Additions | 7,531 | 80,386 | – | 87,917 |
| Disposals | (10,801) | – | – | (10,801) |
| At 31st May 2007 | 91,427 | 667,966 | 159,163 | 918,556 |
| Accumulated depreciation | | | | |
| At 1st June 2006 | 81,893 | 386,394 | 147,214 | 615,501 |
| Charge for the year | 6,710 | 106,781 | 7,003 | 120,494 |
| Disposals | (10,801) | – | – | (10,801) |
| At 31st May 2007 | 77,802 | 493,175 | 154,217 | 725,194 |
| Net book value | | | | |
| At 31st May 2007 | 13,625 | 174,791 | 4,946 | 193,362 |
| At 31st May 2006 | 12,804 | 201,186 | 11,949 | 225,939 |

# Notes to the financial statements

Continued

## 11 Tangible fixed assets continued

| Company | Furniture and equipment £ | Computer and telephone equipment £ | Short leasehold improvements £ | Total £ |
|---|---|---|---|---|
| **Cost** | | | | |
| At 1st June 2006 | 46,678 | 207,978 | 132,419 | 387,075 |
| Additions | 2,751 | 52,131 | – | 54,882 |
| Disposals | (8,551) | – | – | (8,551) |
| At 31st May 2007 | 40,878 | 260,109 | 132,419 | 433,406 |
| **Accumulated depreciation** | | | | |
| At 1st June 2006 | 43,459 | 155,787 | 124,577 | 323,823 |
| Charge for the year | 1,961 | 36,121 | 5,304 | 43,386 |
| Disposals | (8,551) | – | – | (8,551) |
| At 31st May 2007 | 36,869 | 191,908 | 129,881 | 358,658 |
| **Net book value** | | | | |
| At 31st May 2007 | 4,009 | 68,201 | 2,538 | 74,748 |
| At 31st May 2006 | 3,219 | 52,191 | 7,842 | 63,252 |

## 12 Investments held as fixed assets

| Group | Unlisted investments £ |
|---|---|
| **Cost** | |
| At 1st June 2006 | 61,253 |
| Additions | 255 |
| Disposals | (14,649) |
| At 31st May 2007 | 46,859 |

| Company | Unlisted investments £ | Shares in subsidiary undertakings £ | Total £ |
|---|---|---|---|
| **Cost** | | | |
| At 1st June 2006 | 60,183 | 576,004 | 636,187 |
| Additions | 255 | – | 255 |
| Disposals | (14,649) | (4) | (14,653) |
| At 31st May 2007 | 45,789 | 576,000 | 621,789 |

## 12 Investments held as fixed assets continued

| Subsidiary undertakings | Activity | Holding of ordinary shares |
|---|---|---|
| City of London Investment Management Company Limited | Management of funds | 100% |
| City of London Unit Trust Managers Limited | Dormant company | 100% |
| City of London US Investments Limited | Holding company for US companies | 100% |

City of London US Investments Limited holds 100% of the ordinary shares in the following:

| | |
|---|---|
| City of London US Services Limited | Service company |
| City of London Quantitative Management Limited | Dormant company |
| City of London Latin America Limited | Dormant company |

The above companies are incorporated in Great Britain and registered in England and Wales. They are included in the consolidated financial statements of the Group. In the opinion of the directors, the value of the subsidiaries is at least equal to their cost.

## 13 Debtors

| | Group | | Company | |
|---|---|---|---|---|
| | 2007 £ | 2006 £ | 2007 £ | 2006 £ |
| Trade debtors | 2,352,826 | 1,762,550 | – | – |
| Amounts owed by Group undertakings | – | – | 2,456,417 | 35,110 |
| Other debtors | 111,631 | 180,282 | 53,292 | 98,779 |
| Prepayments and accrued income | 148,755 | 193,480 | 107,152 | 157,725 |
| Corporation tax recoverable | – | – | 791,011 | 341,003 |
| | 2,613,212 | 2,136,312 | 3,407,872 | 632,617 |

## 14 Current asset investments

Group and Company

| | 31st May 2007 £ | 31st May 2006 £ |
|---|---|---|
| Unlisted investments at market value | 2,231,989 | 1,359,563 |
| Listed investments at market value | 67,336 | – |
| Total at market value | 2,299,325 | 1,359,563 |
| Unlisted investments at cost | 1,578,458 | 1,225,057 |
| Listed investments at cost | 75,038 | – |
| Total at cost | 1,653,496 | 1,225,057 |

# Notes to the financial statements

Continued

## 15 Creditors: amounts falling due within one year

| | Group | | Company | |
|---|---|---|---|---|
| | 2007 £ | 2006 £ | 2007 £ | 2006 £ |
| Trade creditors | 369,140 | 252,893 | – | – |
| Sundry creditors | 37,604 | 57,279 | 37,604 | 85,357 |
| Amounts owed to Group undertakings | – | – | 2,445,607 | 541,520 |
| Other creditors including taxation and social security | 1,047,906 | 780,692 | – | – |
| Accruals and deferred income | 1,755,424 | 1,069,305 | 835,333 | 466,305 |
| | 3,210,074 | 2,160,169 | 3,318,544 | 1,093,182 |

## 16 Share capital

| Group and Company | 31st May 2007 Number of shares | 31st May 2006 Number of shares |
|---|---|---|
| Authorised | | |
| Ordinary shares of 1p each (2006 – 1p each) | 90,000,000 | 90,000,000 |
| | £ | £ |
| Ordinary shares of 1p each (2006 – 1p each) | 900,000 | 900,000 |

| Group and Company | 31st May 2007 Number of shares | 31st May 2006 Number of shares |
|---|---|---|
| Allotted, called up and fully paid | | |
| Ordinary shares of 1p each (2006 – 1p each) | 26,777,800 | 26,777,800 |
| | £ | £ |
| Ordinary shares of 1p each (2006 – 1p each) | 267,777 | 267,777 |

## 17 Combined statement of movement in reserves and reconciliation of shareholders' funds

| Group | Share capital £ | Share premium account £ | Investment in own shares £ | Revaluation reserve £ | Share option reserve £ | Profit and loss account £ | Total £ | Year ended 31st May 2006 (as restated) Total £ |
|---|---|---|---|---|---|---|---|---|
| At 1st June 2006 – as previously stated | 267,777 | 1,357,283 | (1,027,283) | 134,506 | – | 3,599,530 | 4,331,813 | 2,565,178 |
| Prior year adjustment FRS 20 | – | – | – | – | 106,325 | (106,325) | – | – |
| At 1st June 2006 – as restated | 267,777 | 1,357,283 | (1,027,283) | 134,506 | 106,325 | 3,493,205 | 4,331,813 | 2,565,178 |
| Purchase of own shares | – | – | (670,948) | – | – | – | (670,948) | – |
| Share allotment | – | – | 124,706 | – | – | – | 124,706 | 907,685 |
| Revaluation reserve | – | – | – | 511,323 | – | – | 511,323 | 134,506 |
| Share option reserve | – | – | – | – | 124,520 | – | 124,520 | 64,026 |
| Profit retained for the period | – | – | – | – | – | 4,138,094 | 4,138,094 | 660,418 |
| At 31st May 2007 | 267,777 | 1,357,283 | (1,573,525) | 645,829 | 230,845 | 7,631,299 | 8,559,508 | 4,331,813 |

| Company | Share capital £ | Share premium account £ | Investment in own shares £ | Revaluation reserve £ | Share option reserve £ | Profit and loss account £ | Total £ | Year ended 31st May 2006 (as restated) Total £ |
|---|---|---|---|---|---|---|---|---|
| At 1st June 2006 – as previously restated | 267,777 | 1,357,283 | (1,027,283) | 134,506 | – | 901,415 | 1,633,698 | 845,521 |
| Prior year adjustment FRS 20 | – | – | – | – | 106,325 | (106,325) | – | – |
| At 1st June 2006 – as restated | 267,777 | 1,357,283 | (1,027,283) | 134,506 | 106,325 | 795,090 | 1,633,698 | 845,521 |
| Purchase of own shares | – | – | (670,948) | – | – | – | (670,948) | – |
| Share allotment | – | – | 124,706 | – | – | – | 124,706 | 907,685 |
| Revaluation reserve | – | – | – | 511,323 | – | – | 511,323 | 134,506 |
| Share option reserve | – | – | – | – | 124,520 | – | 124,520 | 64,026 |
| Profit/(loss) retained for the period | – | – | – | – | – | 1,789,879 | 1,789,879 | (318,040) |
| At 31st May 2007 | 267,777 | 1,357,283 | (1,573,525) | 645,829 | 230,845 | 2,584,969 | 3,513,178 | 1,633,698 |

Investment in own shares relates to City of London Investment Group Plc shares held by an Employee Benefit Trust on behalf of City of London Investment Group Plc.

At 31st May 2007 the Trust held 2,303,125 ordinary 1p shares (2006 – 2,262,750), of which 2,297,675 ordinary 1p shares (2006 – 2,247,050) were subject to options in issue.

In total, the Company has granted options over 4,797,675 ordinary shares at exercise prices from £0.26 to £2.73. These options have a range of exercise dates from September 2000 to March 2017.

## 18 Profit of the Parent Company

As permitted by section 230 of the Companies Act 1985, the profit and loss account of the Parent Company is not presented as part of these financial statements. The Parent Company's profit for the financial period before dividends paid, amounted to £2,525,743 (2006 restated – £1,964,635).

## 19 Operating lease commitments

At 31st May 2007 the Group was committed to making the following payments during the next year in respect of operating leases:

| | Motor vehicle 2007 £ | Land and buildings 2007 £ | Motor vehicle 2006 £ | Land and buildings 2006 £ |
|---|---|---|---|---|
| Leases which expire: | | | | |
| Within one year | 3,886 | – | – | 34,755 |
| In the second to fifth years inclusive | – | 131,150 | 6,826 | 99,496 |
| | 3,886 | 131,150 | 6,826 | 134,251 |

The Group is also committed to paying a minimum of £165,169 per annum in respect of a service agreement which expires in 2009.

## 20 Reconciliation of operating profit to net cash inflow from operating activities

| | 2007 £ | 2006 (as restated) £ |
|---|---|---|
| Operating profit | 7,089,711 | 4,617,669 |
| Profit on sale of fixed assets | – | (9,519) |
| Depreciation charges | 120,494 | 108,112 |
| Increase in debtors | (476,900) | (1,043,783) |
| Increase in creditors | 782,691 | 408,417 |
| Translation adjustments on investments | 68,177 | 502 |
| Share-based payment charge | 124,520 | 64,026 |
| Net cash inflow from operating activities | 7,708,693 | 4,145,424 |

## 21 Gross cash flows

| | 2007 £ | 2006 £ |
|---|---|---|
| **Returns on investments and servicing of finance** | | |
| Interest received | 196,487 | 109,562 |
| **Taxation** | | |
| Corporation tax paid | (2,190,642) | (1,643,687) |
| **Capital expenditure and financial investment** | | |
| Payments to acquire investments | (255) | (41,727) |
| Receipts from sale of investments | 29,627 | – |
| Payments to acquire tangible fixed assets | (87,917) | (133,268) |
| Receipts from sale of tangible fixed assets | – | 10,728 |
| | (58,545) | (164,267) |
| **Financing** | | |
| (Increase)/repayment of ESOP loan | (546,242) | 230,985 |
| Issue of ordinary share capital | – | 676,700 |
| | (546,242) | 907,685 |
| **Management of liquid resources** | | |
| Payment to acquire current asset investments | (580,139) | (761,167) |
| Receipts from sale of current asset investments | 114,161 | – |
| | (465,978) | (761,167) |

## 22 Reconciliation of net cash flow to movement in net funds

| | 2007 £ | 2006 £ |
|---|---|---|
| Increase in cash in the year | 3,907,909 | 310,875 |
| Increase in liquid assets | 465,978 | 761,167 |
| Other non cash changes | 30,816 | – |
| Changes in market value and exchange rate movements | 442,968 | 134,506 |
| Change in net funds | 4,847,671 | 1,206,548 |
| Net funds at 1st June | 4,068,478 | 2,861,930 |
| Net funds at 31st May | 8,916,149 | 4,068,478 |

# Notes to the financial statements

Continued

## 23 Analysis of changes in net funds

| | At 1st June 2006 £ | Cash flows £ | Changes in market value and exchange rates £ | Other non-cash changes £ | At 31st May 2007 £ |
|---|---|---|---|---|---|
| Cash at bank and in hand | 2,708,915 | 3,907,909 | – | – | 6,616,824 |
| Current asset investments | 1,359,563 | 465,978 | 442,968 | 30,816 | 2,299,325 |
| | 4,068,478 | 4,373,887 | 442,968 | 30,816 | 8,916,149 |

## 24 Related party transactions

Advantage has been taken of the exemption under Financial Reporting Standard No. 8 not to disclose transactions between entities, 90% or more of whose voting rights are controlled within the Group.

## 25 Financial instruments

Most of the Group's revenues, and a significant part of its expenses, are denominated in currencies other than sterling, principally United States' and Canadian Dollars. These revenues are derived from fee income which is based upon the net asset value of accounts managed, and have the benefit of a natural hedge by reference to the underlying currencies in which investments are held. Inevitably, debtor and creditor balances arise which in turn give rise to currency exposure. Each of the Group's subsidiaries eliminates its currency exposure by transfer to the holding company. All hedging activity is therefore assessed at the group level. Forward foreign exchange transactions are executed so as to substantially reduce the Group's exposure to currency market movements. The level of forward currency hedging is such as is judged by the directors to be consistent with market conditions.

As at 31st May 2007, the Group had net asset balances of US $8,242,038 (2006 – US $7,507,086), offset by forward sales totalling US $4,500,000 (2006 – US $3,600,000), and net asset balances of C $574,804 (2006 – C $501,335).

The Group has no borrowings, and therefore has no exposure to interest rate risk other than that which attaches to its interest earning cash balances. The Group's strategy is to maximise the amount of cash which is maintained in interest bearing accounts, and to ensure that those accounts attract a competitive interest rate. At 31st May 2007 the Group held £6,616,824 (2006 – £2,708,915) in cash balances, of which £6,581,480 (2006 – £2,552,656) was held in bank accounts which attract variable interest rates.

The fair value of the Group's financial assets and liabilities is materially the same as the book value.

# Notice of Annual General Meeting

Notice is hereby given that the Annual General Meeting of City of London Investment Group Plc will be held at 10 Eastcheap, London EC3M 1LX on Monday 29th October 2007 at 11.30 am for the following purposes:

## Ordinary business

1. To receive and adopt the financial statements for the year ended 31st May 2007 together with the reports of the directors and auditors thereon.

2. Having retired by rotation, to re-elect David Michael Cardale as a director of the Company in accordance with article 132 of the Company's articles of association.

3. Having retired by rotation, to re-elect George Alan Robb as a director of the Company in accordance with article 132 of the Company's articles of association.

4. Having retired by rotation, to re-elect Carlos Manuel Yuste as a director of the Company in accordance with article 132 of the Company's articles of association.

5. Having been appointed by the board over three years ago, to re-elect Thomas Wayne Griffith as a director of the Company in accordance with article 136 of the Company's articles of association.

6. To re-appoint Moore Stephens LLP as auditors of the Company to hold office from the conclusion of the meeting until the conclusion of the next general meeting of the Company at which accounts are laid before the Company and authorise the directors to determine the auditors' remuneration.

## Special business

To consider and, if thought fit, pass the following resolution as a special resolution:

7. THAT the Company be generally and unconditionally authorised to make market purchases (within the meaning of section 163(3) of the Companies Act 1985) of any of its ordinary shares of £0.01 (1p) provided that:

   (a) the maximum number of ordinary shares which may be purchased is 4,000,000 (representing 14.94% of the Company's issued ordinary share capital at the time of this resolution);

   (b) the minimum price which may be paid for each ordinary share is £0.01 (1p) which amount shall be exclusive of expenses, if any;

# Notice of meeting

Continued

(c) the maximum price, exclusive of any expenses, which may be paid for any ordinary share is an amount equal to 105% of the average of the middle market quotations for the ordinary shares of the Company as derived from the Daily Official List of the London Stock Exchange plc for the five business days immediately preceding the date on which such share is contracted to be purchased;

(d) unless previously renewed, revoked or varied, this authority shall expire at the conclusion of the annual general meeting in 2008 or 15 months after the passing of this resolution (whichever is the earlier); and

under this authority the Company may make a contract to purchase ordinary shares which would or might be executed wholly or partly after the expiry of this authority and may make purchases of ordinary shares pursuant to it as if this authority had not expired.

By order of the Board

D F Allison
Company Secretary
14th September 2007

Registered office
10 Eastcheap
London EC3M 1LX

Registered in England and Wales No 2685257

# Notes to the Notice of Annual General Meeting

1. A member entitled to receive notice, attend and vote at the annual general meeting ("AGM") is entitled to appoint a proxy or proxies to attend and, on a poll, vote instead of him. Such proxy need not be a member of the Company. Completion of a form of proxy does not preclude the member attending the meeting and voting in person if they so wish. To be valid, the instrument appointing a proxy, together, if appropriate, with a power of attorney or other authority (if any) under which it is signed, or a notarially certified copy of such authority, must be deposited at the offices of the Company's registrars, Capita Registrars, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4TU no later than 11.30 am on 27th October 2007. A form of proxy accompanies this notice.

2. Pursuant to regulation 41 of the Uncertificated Securities Regulations 2001, the time by which a person must be entered on the register of members of the Company in order to have the right to attend and vote at the annual general meeting (and for the purposes of the determination by the Company of the numbers of votes they may cast) is *11.30 am on 27th October 2007*. The rights of members to attend and vote at the meeting will be determined by reference to entries on the register of members at *11.30 am on 27th October 2007*. Changes to entries on the register of members of the Company after that time will be disregarded in determining the rights of any person to attend or vote at the meeting.

3. In the case of joint holders, the signature of only one of the joint holders is required on the form of proxy, but the vote of the first named on the register of members will be accepted to the exclusion of the other joint holders.

4. The following documents are available for inspection between 10.00 am and 12.00 noon at the registered office of the Company on any weekday and will also be available for inspection at the place of the AGM from the commencement of the meeting until the conclusion thereof:

   a) The register of interests of the directors (and their families) in the share capital of the Company.

   b) Copies of the directors' contracts of service and letters of appointment of the non-executive directors.

   c) Terms of reference of the Audit, Remuneration and Nominations Committees.

# Explanation of the business of the Annual General Meeting

### Report and accounts (Resolution 1)

The first item on the agenda requires that the directors must present the accounts of the Company for the year ended 31st May 2007 together with the directors' report and the independent auditors' report thereon.

### Re-appointment of directors (Resolutions 2-5)

The Company's articles of association require that at every annual general meeting, one-third of the directors or, if their number is not three or a multiple of three, the number nearest to one-third shall retire from office. In addition, the articles of association require that all directors who have been in office for more than three years or have been appointed by the directors since the last annual general meeting of the Company will stand for re-appointment.

Article 137 of the Company's articles of association requires that a resolution for the appointment or re-appointment of two or more persons as directors by a single motion may not be moved unless a resolution that it shall be so moved has first been agreed to by the meeting without any vote being given against it. Consequently separate resolutions will be put to the meeting.

### Re-appointment of Auditors (Resolution 6)

The Company is required at each general meeting at which accounts are laid before the shareholders to appoint auditors to hold office from the conclusion of the annual general meeting until the conclusion of the next annual general meeting. Moore Stephens LLP are the current auditors and have indicated their willingness to continue in office. If Resolution 6 is passed, Moore Stephens LLP will be re-appointed as auditors to the Company, at a fee to be agreed by the board of directors.

### Purchase by the Company of its own shares (Resolution 7)

Under section 166 of the Companies Act 1985, the directors of a company may make market purchases of that company's shares if authorised to do so. The Company's articles of association give a general authority to the directors to purchase shares on the market but that authority is subject to the approval of shareholders. Your directors believe that granting such approval would be in the best interests of shareholders in allowing directors the flexibility to react promptly to circumstances requiring market purchases.

Accordingly, Resolution 7, which will be proposed as a special resolution, will give the directors the authority to purchase issued shares of the Company under section 166 of the Companies Act 1985. The authority contained in this Resolution will be limited to an aggregate nominal value of £40,000 which represents 14.94% of the issued ordinary share capital of the Company as at 14th September 2007. The price which may be paid for those shares is also restricted as set out in the Resolution. This authority will expire at the conclusion of the Company's annual general meeting in 2008 or 15 months after the passing of this resolution (whichever is the earlier).

The board has no present intention of exercising this authority. However, this will be kept under review, and the board will use this power only if and when, taking account of market conditions prevailing at the time, other investment opportunities, appropriate gearing levels and the overall financial position of the Group, they believe that the effect of such purchases will be in the best interests of shareholders generally and that they will result in an increase in earnings per share.

Shares purchased under this authority may be held as treasury shares. The Company may purchase and hold shares as treasury shares up to a maximum amount equal to 10% of the nominal value of the issued ordinary share capital at that time, rather than cancelling them. Shares held in treasury do not carry voting rights and no dividends will be paid on any such shares. Shares held in treasury in this way can be sold for cash or cancelled. This would allow the Company to manage its capital base more effectively and to replenish its distributable reserves.

If and when the board resolves to exercise its authority to make market purchases, it will at that time decide whether shares purchased are to be cancelled or held in treasury.

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