Transforming to communications and information

Annual Report and Accounts 2000

Marconi

Cover photo: The 8 workstations in our advanced Network Operations Centre in Pittsburgh, US can manage remotely up to 32 communications networks for customers around the world

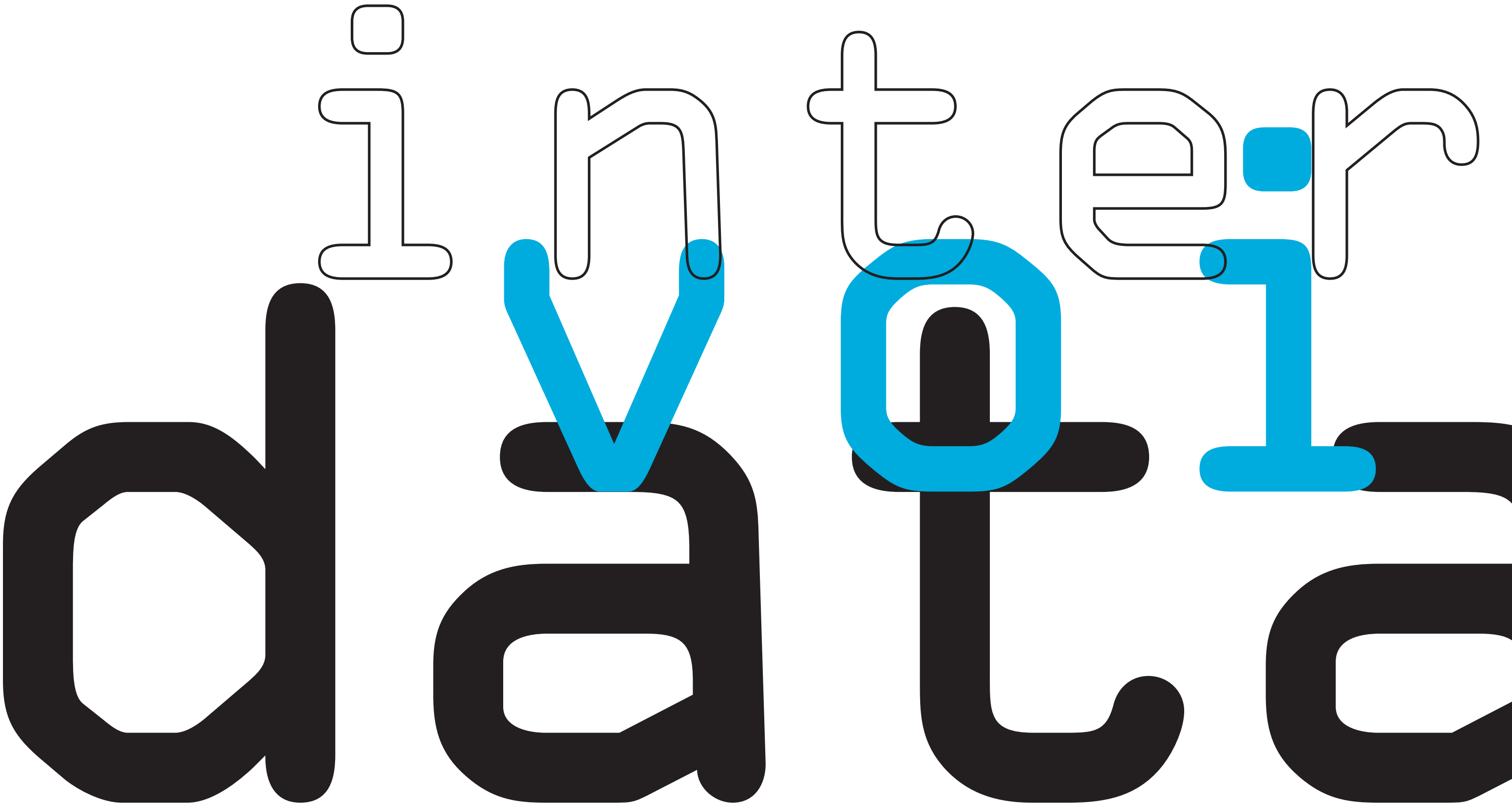
For more information on Marconi, please visit our website: www.marconi.com

Optical networks delivering vast, flexible communications capacity… medical scans captured and transmitted around the globe… digital codes to tag and track millions of products… communications and applications services to take our customers into the future.

Bandwidth, data and knowledge services that allow people to communicate better… faster… to any business… anywhere… at any time. Solutions and products that capture information and make it valuable.

Here's what we see ahead…

Seizing the Opportunity



Marconi is pursuing a once-in-a-lifetime opportunity to transform communications and knowledge management. The moment is unique because right now, the landscape of communications and information is being transformed beyond recognition.

Change is being driven by four overwhelming trends

- The Internet keeps booming. It's doubling and redoubling in almost every measure – traffic, subscribers, applications and enthusiasm.
- Applications that were previously web-independent are being irreversibly pulled into the Internet. Voice and video are joining data and graphics.
- Internet convergence is bringing together information and communication in new and powerful ways. The most mundane business routines are now being transformed. Even the time-honoured practices of medicine are changing as Healthcare Information Systems improve diagnosis and treatment.
- Mobile communication continues to expand with more subscribers, more devices, more applications and more services every day. Third Generation – the mobile Internet – will drive this even faster with voice, video and data available to handsets.

Picks, shovels and maps

The Internet boom is a high-tech gold rush, a latter day Klondike of bits and bandwidth. In that earlier gold rush, some prospectors struck it rich. Some went broke. But the people who consistently profited were the ones who supplied the prospectors with the picks, shovels and maps. That is Marconi's starting position. We supply the picks, shovels and maps to harness the power of bandwidth and information.

The new demands of carriers

As the Internet accelerates, carriers everywhere are simultaneously adjusting to the intense pressures of deregulation. We've seen traditional operators privatised, making the incumbents far more aggressive. And we've seen fierce new competitors appear and thrive.

These vast changes have put traditional business models under threat. In the old model, carriers designed, built, owned and operated their infrastructure end-to-end. The infrastructure was the business.
In the new era, the engineering resources of carriers and service providers are stretched thin. Yet spurred by competition and user appetites for data, the demand for new services is growing exponentially. So carriers are beginning to embrace what was nearly unthinkable just a decade ago. They are procuring fully converged, end-to-end networks and network management from outside partners. Marconi has already proved it can be the ideal partner to exploit this new opportunity. With newly acquired and expanded capabilities, we're prepared to design, plan, build and operate carrier and service provider networks that transform the communications landscape.

The new opportunity in data

As the full implications of exploding bandwidth become clear, data anywhere will become data everywhere, and data managers will soon realise that knowledge will have much greater value-added than data, per se. Marconi combines the connectivity of next generation communications networks with industry-specific domain knowledge, expertise and applications. We're transforming communication and information for our customers. Our Systems business delivers Internet-enabled applications in e-commerce, e-distribution, e-logistics and e-medicine. We're developing Internet applications everywhere, from the Radiology lab to the petrol pump to the soft drink vending machine.

The Marconi vision

Marconi intends to drive the transformation and convergence of communications and information. We will add relevant information and knowledge management to our customers' businesses. We will meet the needs of carriers by defining the New Public Network. In this way, we will profit and grow, supplying the picks, shovels and maps of the Internet gold rush.

Connecting with Customers

Every enterprise aspires to understand its customers. At Marconi, we aspire to more. We aim to transform communications and information. And that means we give our customers the communication networks, connectivity and services they need to transform their businesses. To do this, we get to know our customers and their businesses intimately, rolling up our sleeves and digging into the details. Pursuing this strategy has led to substantial victories. Some represent huge sales. Some represent world firsts or bests. All of them represent a significant transformation of communication and information for our customers, as these examples illustrate.

Our Customer's Aim…
Staying ahead of insatiable customer demand for bandwidth-intensive applications and new services.
Marconi Solution…
In a $1 billion agreement with BellSouth, Marconi is supplying the world's largest Fibre in the Loop deployment. Using the Marconi Deep Fiber™ access platform, the build-out will bring fibre optic distribution to within 500 feet of residential and business subscribers. The resulting network will support high-speed data, voice and video applications, at up to 200 times faster than today's dial-up access. The partnership with BellSouth was forged, from the beginning of our consulting process, as we re-assigned a team of 50 European R&D engineers, accelerating our time-to-market by six months and giving BellSouth a significant advantage in the markets they serve.

Our Customer's Aim…
Revolutionising soft drink vending, creating new retailing opportunities and deepening customer relationships.
Marconi Solution…
The Coca-Cola Company chose Marconi data technology to link more than a half-million vending machines worldwide.
The result? A new, intelligent online vending machine that will engage customers as never before. Potential applications include cashless vending via credit cards and debit cards; audio, video and touch screen interactivity; couponing and Internet browsing. This new Internet-age application is just the latest development in our long-standing relationship with Coca-Cola and its bottlers. Already they have nearly 60,000 vending machines online, thanks to Marconi technology.

Our Customer's Aim…
Managing the exploding demand for voice and data services by creating an advanced, multi-service switching architecture for a global communications company.
Marconi Solution…
When Sprint needed to expand the capacity of their network, they turned to the Marconi ASX™-4000 Asynchronous Transfer Mode (ATM) switches, connecting Points of Presence across North America. With the ASX-4000, Sprint will be able to offer customer services at up to 622 megabits per second – equal to the bandwidth of over 9,000 simultaneous voice conversations. Marconi also offers Sprint an easy migration path to even higher bandwidth – and an expanding range of services for its customers – in the future.

Our Customer's Aim…
Enabling more rapid, reliable and cost-effective information transmission for the leading Electronic Funds Transfer retail transaction processors in the US.
Marconi Solution…
Thrucomm brought us in to plan, build and operate a wireless Virtual Private Network that will reshape the Electronic Funds Transfer industry. For Marconi to succeed it is critical to enable Thrucomm to deploy the network quickly to bring a nationwide service to market.
The Marconi wireless solution includes products and services valued at more than $650 million. And it's only the first cross-selling synergy to be realised from our agreed acquisition of the global wireless consultancy, MSI.

Our Customer's Aim…
Enabling a new telecom operator to leapfrog into the fast-growing market for broadband Internet access.
Marconi Solution…
Marconi helped to make Atlantic Telecom one of the UK's first – and fastest – broadband Internet service providers. Marconi integrated and built the system, including Marconi Wireless Internet Protocol Local Loop (WipLL) access and Marconi ATM switching, along with servers and software from other vendors. The new 'always on' atlantic-e.com service delivers access speeds up to 25 times faster than ISDN, making possible full-frame video over the Internet.

Our Customer's Aim…
Connecting global airports, offices and reservations call centres with data, voice and video.
Marconi Solution…
Delta Air Lines turned to Marconi for an ATM network, including ATM core switches and Ethernet edge switches. The network provides a single infrastructure for data, voice and video and paves the way for new applications in customer service, operations and revenue management. Delta imposed an aggressive rollout schedule and had a host of legacy equipment with which the new network components needed to work – constraints that might have made other vendors think twice. Marconi is already well on the way to meeting these requirements.

Telling our story

Marconi is firmly established with the customers we serve around the world. While our brand is only six months in the making, now is an opportune time to make our global brand meaningful, credible and relevant to current and prospective customers. The Marconi brand promises our customers nothing short of the transformation of communications and information. Our global brand campaign has started to make this connection with our customers, to the solutions, products and services to achieve their Finest Hour.

The Marconi Brand promises customers nothing short of the transformation of communications and information. We get to know our customers and their businesses intimately. We roll up our sleeves and dig into the details to give our customers the communications networks, connectivity and services to transform their businesses and enable them to achieve their Finest Hour.

Developing the Future

r&d

Developing the future

Marconi is innovating by combining technologies from wherever they are developed. This is our key to accelerating value creation from our Research and Development activities. Our vision is to access important new technologies from the best sources and be the leader at integrating them into exciting new product solutions. These solutions will sustain the development of our existing products but also spin-out radical opportunities for creating new businesses.

Strategic thinking

Marconi is doing this by creating a Virtual Technology Centre consisting of a worldwide, entrepreneurial network of strategic alliances with key companies, research partnerships with premier universities and our own centres of technological excellence.

As an example, the new Marconi laboratory being sited at Cambridge in the UK is part of a long term venture with Cambridge University. We have committed funding for advanced communications research and related development within the University, as well as locating our own product development teams there to leverage the advances into market beating solutions.

We are also optimising our growing investment in in-house capabilities. The Caswell laboratory, for instance, with its international reputation in high performance photonics and gallium arsenide semi-conductor research, is focusing to meet the soaring demand for advanced photonic components, such as lasers and modulators, for Marconi's core network products and to supply customers in fast growing external markets.

All this effort is co-ordinated and focused into a number of critical technology themes. These themes include implications of future internet traffic profiles, service management, transparent photonic routing and modelling. In addition we are active players in key industry bodies which are developing the next generation communications standards, such as the Multi-Protocol Label Switching (MPLS) forum.

Near term results

In the Internet age, the market waits for no one. Customer requirements and business opportunities demand unprecedented speed and agility. Here again, Marconi R&D has shone, as some recent developments demonstrate.

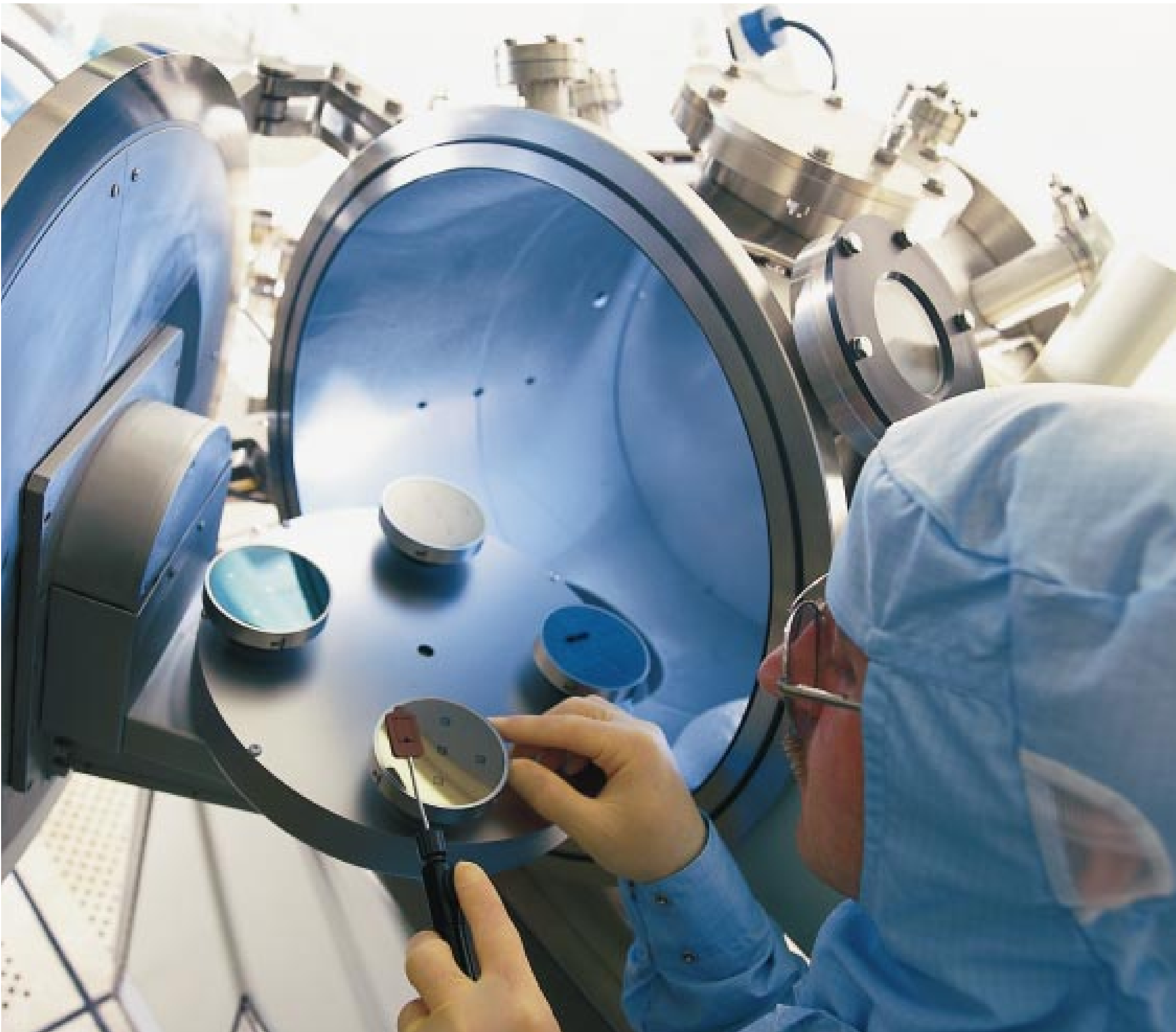
- We're accelerating the launch of Fibre in the Loop combined with ADSL technology for Internet access and service delivery to residences and business.
- We were first to market with ring-based metropolitan Dense Wave Division Multiplexing, based on another Marconi world first: an All-Optical remotely reconfigurable Add/Drop Multiplexer. This allows carriers to provision remotely wavelengths in a flexible and dynamic way. This system is in live network trials with operators around the world.
- Our 32-wavelength SmartPhotonix system is based on yet another Marconi world first, the tuneable laser. It produces 32 optical wavelengths from a single product, rather than requiring 32 separate lasers.
- We created the world's first commercial broadband ATM switch and introduced the first 40 Gigabits per second carrier class ATM switch.
- We expect to be first in the market with the 'Big Fast Switch,' starting at 240 Gigabits per second.
- We were first to demonstrate live Multi-Media over Packet services, with the Quality of Service (QoS) that carriers need to deliver higher service levels – and earn higher service fees.

Deep domain expertise

Beyond infrastructure, Marconi is also developing some of the most promising domain specific applications that the New Public Network will support. Our intimate knowledge of customer requirements in retailing, in healthcare and in logistics management have led to breakthroughs of vast commercial significance. This knowledge enables us to understand the new applications which will drive the future communications infrastructure. Simple, everyday transactions will soon be transformed by Marconi's synthesis of communications and information.

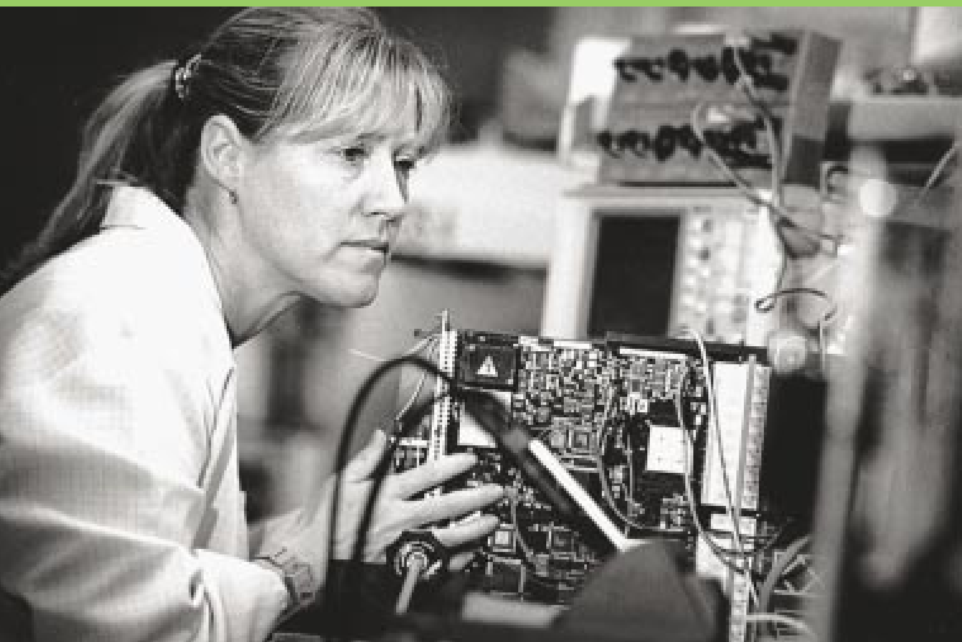
Pictured right: Part of the unique semiconductor wafer processing technology at Caswell used in optical communications components.

In the Internet age, customer requirements and business opportunities demand unprecedented speed and agility. Marconi can point to an ever growing list of major innovations including: the world's first commercial broadband ATM switch, the first ring-based metropolitan Dense Wave Division Multiplexing and live Multi-Media over Packet services. We combine this agility with a long term view that positions us strategically for the converged world of voice, video and data networking.



Creating a Culture of Innovation

We are a talent business. Our assets are our people and the skills they possess and which they can develop. Recognising this, we have been building a new company culture, in keeping with our fast-moving industry and the astonishing worldwide pace of change. This culture is designed to embrace the many new people who have joined our Company as a result of recent acquisitions, and to blend the mixture of cultures, backgrounds, history and experience that individuals bring to the Company into something we call The Marconi Way.



The Marconi Way

This has grown out of an extensive Company-wide programme, with one thousand of our people already taking part from around the world. It's a practical programme, designed to ensure our organisation reaches its ambitious objective – to be one of the world's leading communications and information solutions companies.

Our people have created The Marconi Way – a set of shared beliefs that binds us together, gives pace to the organisation and drives us forward. It's about real people with passion and pride in their work. It's about people working at high velocity, having a radical outlook, learning fast and working together to deliver long term success for our customers around the world. It's also about taking responsibility for delivering each time and every time: making every commitment special whether for customers, colleagues, shareholders or the communities in which we operate. But it's not just about making people believe in what they're doing, it's also about giving them the power to make a difference.

Communicating with our people

One of the ways in which we can help bind everyone together is by making sure that information is available and flows smoothly throughout the organisation. We have addressed this by launching *momentum*, a Company-wide Intranet which carries daily and breaking news, the Company's share price, internal job opportunities, a Company-wide contact directory and a special page called 'Tell George', which invites people to share their thoughts about the business with the Chief Executive.

Because not all employees have regular access to a PC, we intend to provide everyone with a Palm Pilot, which will enable them to access both *momentum* and our corporate Internet site. Using a software package called Connect, each individual will be able to create their own web page on *momentum*, providing details about their experience and interests. This will be a powerful way of networking within the organisation, acting as a catalyst for sharing knowledge.

Sharing in the future

We will also make our people feel part of the Company in a practical way – by making them shareholders. In this way, we are enabling everyone to participate in the success that they're helping to create. It also means that the whole Company will be focused on maximising shareholder value.

The Marconi Launch Share Plan was introduced in November 1999, at which time all our employees were granted 1,000 share options. When the share price reaches £16.03 – double the price at the launch of the Plan – we will have created more than £20 billion of additional value for our shareholders. At the same time, the options will vest and all our employees will become Marconi shareholders.

Promoting a learning culture

Leading edge technologies are at the heart of Marconi's future success and it is vital that we attract the right young people into the business. Graduate and post-graduate recruits are the lifeblood of our technological development and we take on between 800 and 900 every year around the globe. We are also constantly forging new links with higher education to attract young people to the industry and to provide opportunities for all our employees to further their knowledge and skills.

Part of this approach is the Marconi Academy initiative. We are sponsoring an undergraduate programme to attract young people to undertake three-year courses leading to a Bachelor of Science degree from Warwick and Nottingham universities in the UK. The courses are designed by Marconi and the universities and combine two-thirds work based experience and training with one-third academic work at university. Twenty young people will take part in this programme this year at both our Coventry and Beeston sites.

We are also designing with Loughborough University a Master of Engineering degree in ASIC design and Telecom Systems engineering. Again, we plan to have 20 young people studying on this programme this year, providing us with future recruits educated and trained in exactly the technologies we need for tomorrow.

For our existing employees, we are also sponsoring a Marconi Masters programme – a three-year Master of Science course in International Technology Management – which is intended to provide our people with a combination of technical knowledge and business skills. The Masters programme has been developed jointly by Marconi and Warwick University in the UK and Carnegie Mellon University in the US working with a consortium of some of the world's leading universities.

The technical and managerial challenges of the fast moving, high technology markets in which Marconi has chosen to operate demand talented, committed and decisive people. Marconi is dedicated to investing in the future of its employees, their development, professionalism and capabilities. The culture Marconi is creating will ensure all of our employees share a vision and beliefs which encourage entrepreneurialism and radically new ways of working and learning, and which prepare us for the challenges to come.

Financial Highlights

	2000 £ million	1999 £ million
Turnover	5,724	4,090
Group and joint venture operating profit before goodwill amortisation and exceptional items	750	508
Return on sales (per cent)	13.1	12.4
Research and development expenditure	471	287
Earnings per share excluding goodwill amortisation and exceptional items	16.9p	14.4p

Chairman's Statement

This is the first annual report since Marconi plc was created from the former GEC in November last year. I am very pleased to report an excellent start for the Company in its new form. Marconi is transformed, growing and doing well.

I am particularly gratified that the management team, led by Chief Executive Lord Simpson, have achieved so much in delivering on the promises that were made last year following the separation of the defence business.

The last twelve months have seen a radical reshaping of our Company, and a concurrent commitment to the successful integration of the new acquisitions. Our business strategy now is to drive for organic growth, while continuing a well considered acquisitions and disposals programme.

By focusing on sales growth we have achieved some very significant large contract wins, particularly in the vital US market. Many of these were the result of pulling together skills and technologies from all the various branches of our Communications and Systems businesses.

Strong financial performance

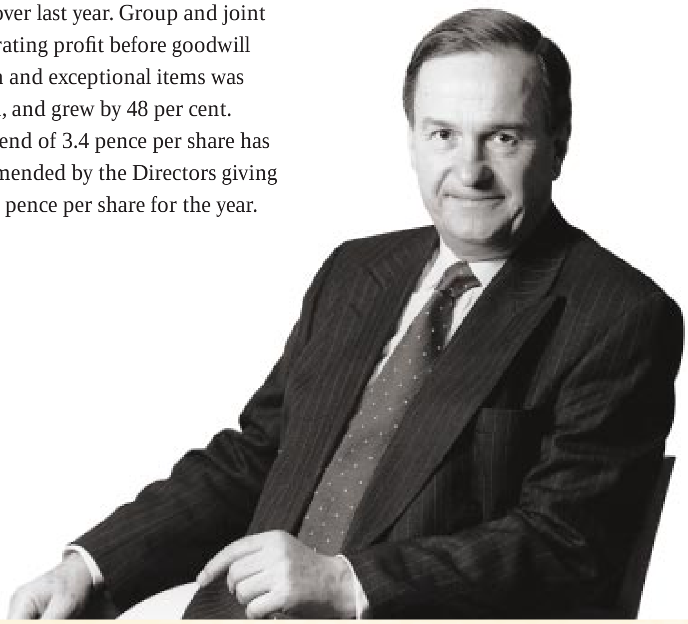
In looking back over this year's results, I am pleased to say the Company has continued its excellent progress. Turnover was £5,724 million, an increase of 40 per cent over last year. Group and joint venture operating profit before goodwill amortisation and exceptional items was £750 million, and grew by 48 per cent. A final dividend of 3.4 pence per share has been recommended by the Directors giving a total of 5.2 pence per share for the year.

The Marconi Way

Marconi continues to exploit all the possibilities inherent in transforming the communications and information markets in which we participate. We are the Company that supplies the technology and infrastructure that make the Internet and e-business possible. While individual dot.coms may come and go, the continuing strong demand for bandwidth throughout the world means solutions suppliers like Marconi have a very promising future. In all this, we continue to operate with a firm commitment to delivering shareholder value.

Key to this strategy are the men and women who make Marconi work. Our employees continue to give the dedicated and energetic commitment that has long been a hallmark of the way we work.

I wish to pay tribute to their efforts and to praise their response to our recently introduced programme of values, known as The Marconi Way. The Marconi Way puts a premium on the need for fast, accurate and innovative working practices in a market that is defined by the need for creative thinking and quick responses. While Marconi is a substantial global company, I have been impressed by the atmosphere of enthusiasm and entrepreneurial energy that permeates everything we do.



The Board

I am sorry to report the death last December of Sir Christopher Harding. Christopher served as a non-executive Director for seven years. I personally found his unflappable, courteous presence a constant source of inspiration in everything we did.

During the course of the year we welcomed two new executive Directors to the Board. They are Mike Parton, the Chief Executive of Marconi Communications Networks, and Mike Donovan, Chief Executive of Marconi Systems and Marconi Capital.

The last year has seen dramatic changes in Marconi that have placed unusually heavy demands on the non-executive members of the Board. I would like to express my gratitude to them for all their efforts and their unfailing patience and dedication to the cause of our Company.

Marconi's future

As I look to the future, I have confidence that the management of Marconi will continue to deliver impressive results from the restructured Company. Further details of the reorganisation that has taken place within Marconi and the plans for its future can be found in the Chief Executive's Review on page 12. For my own part, I would like to leave you with a continuing feeling of excitement about the business sectors in which Marconi now operates and about the prospects for our future. I firmly believe the Company is on the right track, in the right markets and on course for continuing success.

Sir Roger Hurn
Chairman

The last twelve months have seen a radical reshaping of our Company. Our business strategy now is to drive for organic growth while continuing a well considered acquisitions and disposals programme.

Chief Executive's Review

The Marconi management team is committed to drive and maximise shareholder value. A major milestone in this journey was completed during the year, with the rationalisation and refocusing of our core business. This transformation has enabled Marconi to become a leading communications and information technology solutions company, and to build on this momentum to deliver another year of strong sales growth and improving margins.

Strategic developments

Over the course of 1999/2000, we completed the separation of the defence business and merged it with British Aerospace. On 30 November 1999, Marconi was listed on the London Stock Exchange, marking the completion of our Company's transformation.

Between the time of announcing and completing this watershed transaction, the Company built a strong global position in the fast growing market for communications and networking equipment. We also continued to serve our leading global enterprise customers by building software applications businesses in our Systems portfolio.

With the acquisition of RELTEC Corporation for $1.7 billion (£1.0 billion) completed in April 1999, we gained entry into the US communications equipment market for the first time, as well as a world leading position in broadband access solutions.

Our networking equipment portfolio was further strengthened with the acquisition for $4.5 billion (£2.9 billion) in June 1999 of FORE Systems of the United States. This business allows Marconi to serve the world's largest carriers and Internet Service Providers, through a range of leading high performance Internet switching equipment used in the backbone of these networks.

Marconi's capabilities as a leading supplier of communications and networking equipment were further enhanced during the year by the acquisitions of RDC, the transmission business of Nokia, the Bosch Public Networks division and Australian Communications Solutions.

After the year end, we also announced an agreement to acquire MSI, a global consultancy to the wireless communications industry and a provider of planning services and business software to deliver wireless infrastructure.

These acquisitions have effectively re-invented Marconi as a leading player in communications and information knowledge management around the world. More information on the acquisitions and our communications businesses is included on page 18 of this report.

The acquired businesses were rapidly and successfully integrated, and the Group was redefined into five customer facing divisions under the global Marconi brand.

The Group has already won landmark orders totalling more than $2 billion in cross-selling synergies.

The strong underlying growth trends in communications and the overall margin improvement across the Group confirm our ability to improve the operation of existing businesses and to effectively integrate these acquisitions and quickly reap the benefits of effective synergy.

Group performance

Communications Networks

The integration of RELTEC Corporation and FORE Systems was successfully completed in the third quarter, with the creation of the Marconi Communications Networks business, headquartered in Pittsburgh, PA, in the United States. The business demonstrated strong growth, particularly in the fourth quarter, as it started to realise some of the cross-selling synergies created by the expanded global presence and product portfolio as a result of the acquisitions.

The first major sale coming from the acquisition and integration of RELTEC Corporation was realised in December when BellSouth committed to a $1 billion contract for the world's largest broadband Fibre in the Loop deployment using Marconi's Deep Fiber™ solution.

A further indication of our success in the acquisition and integration of FORE Systems came in March 2000, with a $100 million initial contract win from Sprint. They chose Marconi to deploy our ASX-4000 switch – the most robust and highest capacity switch available today – in their network.

The Communications Networks business substantially increased its sales. This strong growth was driven by strong performances from the Optical Networks & Transmission and Broadband Switching divisions, which increased like-for-like sales by 30 per cent and 31 per cent respectively.

Mobile Communications

Mobile Communications was formed in November 1999 to focus and capitalise on the emerging opportunities developing within the rapidly growing third generation mobile market.

With our acquisition of MSI, coupled with the significant worldwide capability of our Services business, we are well placed to design, plan, build and operate third generation mobile communication networks.

The greater market insight that MSI brings to Marconi, combined with the expertise of our Mobile Communications business in Italy gives us a further opportunity to participate in this exciting market. The Mobile Communications division has been tasked with assessing opportunities to win a slice of the market for third generation networks. This development will be based on an innovative business model, involving partnering arrangements to create a competitive product and service offering.

Communications Services

In November 1999, we combined the Services businesses of Marconi Communications, RELTEC Corporation and FORE Systems. This reflects the growing demand from customers for higher value-added services in planning, building and operating their networks.

Marconi completed the task of rationalising and refocusing its core businesses during the year to become a leading communications and IT systems Company. We built on this momentum to deliver another year of strong sales growth and improving margins.

Chief Executive's Review

The results of this restructuring began to be realised in May 2000, when Communications Services was awarded a contract valued at more than $650 million by Thrucomm of the US, to become sole supplier to plan, build and operate their wireless network. The contract is a clear demonstration of the cross-selling synergies of the acquisition, drawing on expertise from MSI, Communications Networks, Communications Services and Systems.

Marconi Systems

Marconi Systems is structured into three businesses: Commerce Systems, Data Systems and Medical Systems. Operational improvements at all three businesses were reflected in operating profit growth of 29 per cent in the second half of the financial year, compared with 13 per cent in the first half.

Systems also accelerated the development of new applications-based businesses built on our strong existing market positions and a blue-chip customer base. Marconi Online was launched in May 2000 to strengthen our competitive position in retail automation products. Through this new business we secured a $100 million contract with Coca-Cola as the exclusive provider of intelligent vending technology that will initially interconnect more than 500,000 soft drink vending machines using Marconi networking and knowledge management technology.

Through Marconi Medical Systems, a wide range of next generation multi-slice Computed Tomography scanners was launched in the third quarter of the financial year. In tandem with strengthening conditions for Magnetic Resonance imaging equipment our consultative selling model underpinned our sales. We decided to exit the low-margin x-ray market which suppressed sales but improved our earnings.

Sales at Marconi Commerce Systems were restrained by the slowing demand resulting from unprecedented consolidation among oil companies. In addition, sales growth in the year was flat in comparison with the strong sales performance in the previous year. This condition was a direct result of US environmental legislation which stimulated our customers' investment. Marconi Commerce Systems successfully introduced new products through field trials during the year. These new products include an Internet-enabled fuel dispensing 'data pump' that will enter the US market this summer.

Marconi Data Systems' performance reflected increasing sales momentum after the launch of new laser coding and information management products at the beginning of the second half. A new generation of products for the secondary coding and information management market is also due for launch in the current year.

Marconi Capital

Marconi Capital is increasingly focused on the development of emerging technology businesses. Through Marconi Ventures, our newly launched $100 million venture capital fund, we will invest in early stage businesses with high growth potential or technology synergies with our core businesses.

Marconi Capital will continue to manage the disposal of our non-core businesses.

In March 2000, the sale of Avery Berkel was agreed, and the sale of the facilities management activities of EASAMS was completed. Negotiations are continuing for the sale of Woods Air Movement.

Research and development

Our R&D investment for the year increased by 64 per cent to £471 million. It is focused on delivering next-generation broadband communications and emerging knowledge management software applications and a number of important new products in these areas will be launched this year.

Outlook

This year has seen Marconi emerge from its restructuring phase to become a global leader in communications and information technology. At the same time, we have kept to our commitment to shareholders and continue to deliver profitable growth.

A combination of corporate developments the Company has undertaken and the dynamics of our selected high growth markets strongly positions Marconi to continue this positive trend.

The complementary nature of our major acquisitions means that we will reap significant benefits in terms of sales growth by developing broader and deeper relationships with our existing customers and new prospects, evidenced by cross-selling.

In addition to being focused on the fastest growing segments of the communications industry, the current boom in demand for optical products which vastly increase network capacity and enhance the deployment of third generation mobile communications infrastructure are particularly attractive opportunities to further accelerate the growth of Marconi.

Marconi is committed to transforming the Communications and IT industry. With our domain knowledge and expertise, we are well positioned to service and capitalise on the broad customer base of Marconi Systems, and to develop the Company as a provider of converged solutions. Our recent orders from Coca-Cola and Thrucomm are good demonstrations of this convergence of Marconi's networking communications and knowledge management capabilities.

We also see opportunities to develop our Services business as we seek to provide fully outsourced communication network services for our customers.

As you have already read, our R&D expenditure continues to grow in absolute terms and as a percentage of sales and we expect it to continue to increase as we move towards providing applications, software and solutions to address the evolving needs of our customers. Increased R&D expenditure will bring new, leading edge products, services and solutions to market more quickly.

Against the background of these developments, momentum is building at Marconi.

Buoyant conditions in the global market for communications equipment and services, and our cross-selling successes across the Group, provide a springboard for Marconi to continue accelerating top line growth while maintaining margins.

Lord Simpson
Chief Executive

Buoyant conditions in the global market for communications equipment and services, and our cross-selling successes across the Group, provide a springboard for Marconi to continue accelerating top line growth while maintaining margins.

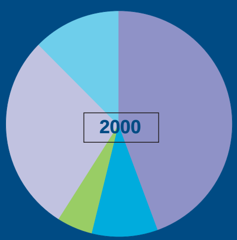
Group at a Glance

Marconi is a major international company focused on high growth communications markets and selected high technology markets. We have a workforce of 49,000 people serving customers in more than 100 countries.

Group turnover

Group operating profit*

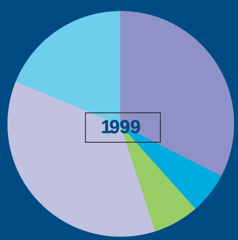
Turnover by division



Communications:
- Networks £2,535m
- Services £543m
- Mobile £295m

- Systems £1,633m
- Capital £711m

Other activities, including intra-activity sales £7m

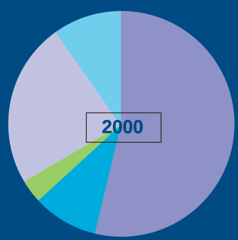


Communications:
- Networks £1,343m
- Services £244m
- Mobile £271m

- Systems £1,501m
- Capital £772m

Other activities, including intra-activity sales (£41m)

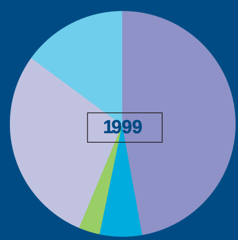
Operating profit by division*



Communications:
- Networks £416m
- Services £73m
- Mobile £26m

- Systems £184m
- Capital £75m

Other activities (£24m)



Communications:
- Networks £247m
- Services £32m
- Mobile £16m

- Systems £151m
- Capital £78m

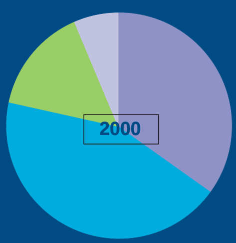
Other activities (£16m)

** Operating profit/margin is stated before goodwill amortisation and exceptional items.*

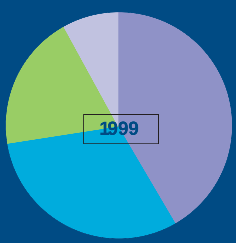
Group R&D expenditure

Group operating margins*

Turnover by region

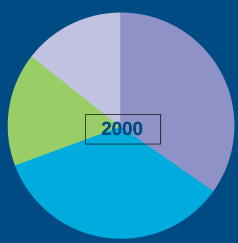


- United Kingdom £1,993m
- The Americas £2,499m
- Rest of Europe £870m
- Africa, Asia and Australasia £362m

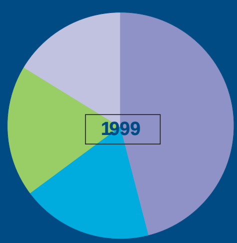


- United Kingdom £1,699m
- The Americas £1,268m
- Rest of Europe £797m
- Africa, Asia and Australasia £326m

Employees by region



- United Kingdom 17,000
- The Americas 17,000
- Rest of Europe 8,000
- Africa, Asia and Australasia 7,000



- United Kingdom 17,000
- The Americas 7,000
- Rest of Europe 7,000
- Africa, Asia and Australasia 6,000

Review: Communications Networks

Our global Communications business was created in November 1999, and is headquartered in Pittsburgh, PA, in the US. This represented the successful completion of our integration of FORE Systems and RELTEC Corporation. The business showed strong growth, particularly in the fourth quarter, as it started to realise some of the cross-selling synergies created by the expanded global presence, access to a broader customer base and the increased services and products portfolio resulting from the acquisitions.

Operating performance

Sales for this business increased by 89 per cent, or 19 per cent on a like-for-like basis, to £2,535 million. Growth was driven by strong performances from the Optical Networks and Broadband Switching divisions in particular, which increased like-for-like sales by 30 per cent and 31 per cent respectively.

Operating profit before goodwill amortisation and exceptional items grew by 68 per cent, or 36 per cent like-for-like. Return on Sales before goodwill amortisation and exceptional items increased from 14.4 per cent to 16.4 per cent on a like-for-like basis.

A leader in communications networking

Our Communications business designs and integrates communications network solutions for public operators, service providers and enterprises with private networks. Our blue chip customer base includes more than 80 of the world's largest 100 telecommunications companies and three of the top five Internet Service

Market overview

Telecommunications is undergoing the biggest revolution since the invention of the telephone 124 years ago. Today's public telecommunications network is a direct descendant of the 19th Century system – it is more automated, more reliable and works faster – but it is still optimised to carry the original dominant service – voice telephone calls.

Networks are being revolutionised because of the phenomenal growth in data traffic over the last few years, caused by the expansion of Internet use, as well as corporate intranets and bandwidth-hungry services like videoconferencing. Demand for these services is growing so rapidly that the total volume of data traffic carried over public networks has overtaken the total volume of voice traffic and is accelerating away.

Growth in the worldwide personal wireless communications market is also increasing at a rapid rate as users increasingly demand mobile data transmission and Internet access. Existing second generation (2G) technology for wireless communications networks is incapable of meeting these demands as it can transmit data only at very slow speeds. Wireless network operators have upgraded existing 2G technology to 2.5G with hardware and software changes to increase data transmission speed and bandwidth. These upgrades, however, do not have the speed or bandwidth to keep pace with the growth in the number of users and their increasing demand for new mobile Internet and data applications. Substantially improved data transmission rates which will be available in third generation (3G) systems are required to meet users' increased voice, data and multimedia needs in the long term.

The existing public network is struggling to cope with these demands. What is needed is a new generation of broadband networks that are optimised for data, but that also carry voice calls and any emerging services such as video-on-demand. What is needed is the New Public Network.

The forces that are shaping the New Public Network are also impacting enterprise networks – the privately owned networks which businesses use to carry their own internal voice and data communications. Traditionally voice and data networks have been separate, but interest is growing in converged networks carrying voice, data and video applications. This will require a new generation of enterprise network equipment that can efficiently carry data but also handle the real-time demands of voice and video.

The equipment which will power the next generation networks will be a fusion of data networking technology originating from enterprise networks, and public telecommunications technology which brings the scaleability, reliability and quality of service that large scale public networks and enterprise networks demand.

The step change to public and enterprise networks has created an exciting opportunity for Marconi to focus our activities on products and solutions to meet the demand for next generation broadband networks.

We have developed and are continuing to develop a range of solutions in broadband switching, optical transmission and next-generation access markets, by focusing on developing products and services with high growth potential. These technologies are explained in more detail on the following pages. Further information is also available on our website: www.marconi.com

These strong market conditions are sustainable and are based on the industry growth in demand for data multimedia and converged network solutions. Market growth is also supported by the worldwide trend towards deregulation of telecommunications services, which is generating competitive investment in broadband networks. Presently, the growth in data traffic is primarily generated by the growth in Internet use. This will increase with the adoption of e-business techniques as companies seek to realise the substantial efficiency gains in terms of speed and cost which net-based business processes can bring.

Providers. Some of these customer partnerships include AT&T, BellSouth, British Telecom, Cable & Wireless, Colt, Energis, GTE, KPN, MCI WorldCom, NTL, Sprint, Telecom Italia, Telecom South Africa, Telstra and US West. Our enterprise network customers include Access Graphics, Ameritech, Cable & Wireless, Delta Air Lines, FDC Technologies, K-Net, Microsoft, UUNET Technologies and the US Government.

Our range of solutions and products addresses a number of layers of communications networking equipment – network services, broadband switching, optical transport and broadband access.

Network services

This is the software that allows operators to package competitive communications services for their customers. It includes the software that enables services from a simple dial tone to enhanced services such as multi-party conferencing. We have more than 15,000 man years of experience in writing this Intelligent Networking and call control software.

Broadband switching

Broadband switching is the ability to direct the traffic in the network core and the access layer. We acquired FORE Systems for their leadership in enterprise and core Asynchronous Transfer Mode (ATM) switching. Our switches provide carrier-grade reliability and scaleability – key requirements for success in large public networks and enterprise applications.

Optical transport

Optical transport acts as the highway system that carries the traffic through the communications network.

Marconi has a leading position in optical transport. We are the world number one in Synchronous Digital Hierarchy (SDH), the transport standard used outside of North America and Japan. We were first to offer fully remotely reconfigureable products for Dense Wave Division Multiplexing (DWDM) technology that vastly expands the capacity of metropolitan and regional networks. This is an exciting emerging market segment that is estimated to grow at around 50 per cent per annum from 2000 to 2005.

Broadband access

The access layer of the network is the last mile of optical fibre and copper cable connecting residential and commercial users to the network.

Marconi acquired RELTEC Corporation in April 1999 to become the market leader in Deep Fiber solutions that extend optical fibre closer to the subscriber, thus expanding the range of services they can receive such as high-speed Internet and video on-demand services. We have more than 10 million lines of this Deep Fiber technology already deployed in the US and Europe.

We also offer, through technologies we acquired with RDC and Bosch Public Networks Division, leading broadband wireless access technologies. These products currently offer residential and business customers data and Internet access at speeds in excess of 4Mbps – 70 times faster than a 56Kbps modem.

CEO Mike Parton talks about the future:

Market conditions are strong. Over the past twelve months we have vastly increased our technical capabilities, our service capabilities and our distribution capabilities. Our restructuring and rapid integration of the businesses acquired has led to each of those businesses having their best quarter ever in the last quarter of the financial year. We are now seeing opportunities that did not exist for us before. We are building up a tremendous momentum. The future looks very exciting.

Review: Communications Networks

Marconi has built a global business platform

Over the last 18 months Marconi has built a strong technology base and a global market presence for its Communications business.

We purchased the 40 per cent minority share in one of our UK companies, GPT, in 1998 and integrated it with Marconi SpA in Italy to create Marconi Communications. In doing so, we created a leading position in the transmission market in Europe.

We moved into the US telecoms market – which represents more than 50 per cent of the world communications networking market – by buying RELTEC. This provided us with a base of US blue chip carrier customers and a leading position in Deep Fiber access technology.

The acquisition of FORE Systems in June 1999 dramatically expanded our communications business with the addition of a portfolio of leading edge broadband switches and a wide range of Internet Service Provider and enterprise customers.

In addition, Marconi acquired a number of small companies that added technology or market presence to strengthen our competitive position. RDC was a technology in-fill acquisition which gives us a broadband wireless IP local loop system. With Marconi Communications South Africa we now have a strong market position in that country. Our distribution arrangements with Ericsson and our acquisition of Nokia's SDH and DWDM manufacturing business brought us deeper technology access and a set of new international customers. The acquisition of Bosch Public Networks division in January 2000 added a major footprint in Germany, which is the largest communications market in Europe, and some additional access technologies.

The result of this corporate activity has been to create enormous cross-selling synergies for Marconi. We already serve most of the world's largest operators. Our communications equipment sales are spread across some of the fastest growing product areas in the telecoms equipment market. They also provide a strong geographic balance across North America, Europe, the UK, and the Asia Pacific region. Our goal is to broaden our relationships with these important customers by offering them the entire Marconi solutions and products portfolio. Already we have begun to realise some of the cross-selling synergies that have been created, with major contracts with Sprint and BellSouth.

Realising cross-selling opportunities

A landmark contract with BellSouth

In December 1999, BellSouth committed to the world's largest broadband fibre in the loop deployment using Marconi's Deep Fiber solution. This is the largest commitment to date from any major global carrier to drive high-speed fibre optics deep into its network. It will bring fibre optic distribution to within 500 feet of individual subscribers and allow BellSouth enough bandwidth to offer the rapid deployment of highly competitive voice, video and data services today, with plenty of capacity for future services as they emerge. By helping BellSouth to strengthen their competitive position using our market leading Deep Fiber solution, Marconi will generate more than $1 billion in sales revenue over the next three years.

We are extremely proud to have earned this business. BellSouth will continue to be an important customer for many years and they remain at the forefront of fibre optic distribution – a position they have held since 1995.

High performance solution for Sprint

A clear demonstration that the acquisition and integration of FORE Systems will lead to major business gains for Marconi came from a contract with Sprint to deploy our ASX-4000 switch – the most robust and highest capacity switch available today – into their network. The switch will provide the advanced, multiservice switching architecture for Sprint's broadband services network, connecting a series of Internet Points of Presence around North America.

Sprint is a global communications company at the forefront of integrating long distance, local and wireless communications services and is one of the world's largest carriers of Internet traffic. The Company developed and operates the United States' only nationwide, all digital, fibre optic network and is the leader in advanced data communications services.

When evaluating solutions for its broadband network services, Sprint demanded a switching solution that would provide the maximum speed, capacity, reliability and scalability for carrying voice, video and data services. With the Marconi solution Sprint achieves all those objectives and has outstanding software functionality that will allow them to quickly offer more advanced services to their customers in the future.

Review: Mobile Communications

Mobile Communications was formed in November 1999 to exploit Marconi's expertise in wireless communication systems, and to focus on opportunities within the large and rapidly emerging third generation (3G) mobile market.

Operating performance

Mobile Communications turnover rose by 9 per cent or 13 per cent like-for-like, increasing to £295 million from £271 million. This was underpinned by strong growth in sales of private mobile radio products.

Operating profit before goodwill amortisation and exceptional items rose to £26 million from £16 million, representing growth of 63 per cent or 69 per cent like-for-like. Return on Sales before goodwill amortisation and exceptional items increased from 5.9 per cent to 8.8 per cent.

Our Mobile Communications business designs, develops and integrates leading-edge communications and information technologies into wireless communications systems for personal, professional and secure uses.

The Mobile Communications business competes in two principal market segments: private mobile radio and secure communications.

In addition, we are evaluating the market for third generation mobile telephony to determine ways to use our existing expertise in mobile communications to extract value from this market which is projected to experience rapid growth. We expect demand for 3G networks will increase dramatically as operators begin to deploy new infrastructure to provide Internet and data services to their customers over mobile handsets.

Private mobile radio systems

Marconi provides private mobile radio (PMR) systems for public safety and emergency services organisations like fire departments, ambulance services, utilities, air traffic control authorities and security services. These customers require a communications system with a high level of call privacy and security, fast call connection speed, guaranteed connections even when the system is busy, direct operations mode for communications in remote areas, and rugged and highly reliable service in time-critical situations.

The standard for this technology throughout Europe and much of Asia is TETRA (Terrestrial Trunked Radio). As other nations adopt this standard, demand for TETRA is expected to increase. Market estimates forecast that the TETRA market will grow at an annual rate of 100 per cent and represent a £2.6 billion opportunity over the next five years.

Secure communications

Marconi provides secure communications systems for organisations such as armed forces, police and emergency services that require particularly secure fault-tolerant communications. The market for secure communications is growing, driven by rising demand for increasingly sophisticated communications technologies and services.

Mobile Communications strategy

Our Mobile Communications strategy is to continue to develop our existing PMR and secure communications businesses, and to focus on the 3G mobile communications market using our experience in 2G technology. We intend to implement our strategy by:

Broadening our TETRA product offering

We are broadening the range of special services offered by our TETRA products, targeting increasing market share in Europe and the Asia Pacific region where the TETRA standard has been adopted.

Widening our geographic presence for PMR and secure communications

We are increasing our direct sales efforts in China, Germany, Scandinavia and South Africa, and indirect sales efforts around the world using global distributors.

Marketing 2G and 2.5G products

We also are developing technology that upgrades 2G to increase its capabilities for providing data transmission and Internet access. This 2.5G technology is already in an advanced stage of development and is due to be released to the market in the third quarter of 2000. Our aim is to provide 2G and 2.5G products that will help operators migrate to 3G networks.

Developing complete solutions for 3G networks

Our primary strategy is to develop a complete portfolio of solutions and products for 3G networks, with technical advantages developed based on our experience with current generation technology and the expertise of MSI, for the first commercial launch of 3G networks in Europe in 2002.

By not having a legacy of wireless communications systems in place, Marconi Mobile is in a position to offer 'scalable' solutions without prior systems constraints. Solutions which are upgradable and expandable in order to fit a particular operator's needs yet flexible enough to continue to fit these changing needs over time in response to market demands and evolving technology.

Aldo Olivari, Chief Executive (left) and Sandro Gualano, Chairman talk about the future:

Demand for third generation mobile communications is growing exponentially. We have the right expertise to enter this market with a competitive product that clearly differentiates us from other vendors – and to create a huge amount of value for Marconi's shareholders. We are very excited about the opportunity to take part in the 3G revolution.

Review: Communications Services

Dramatic change in the requirements of communications carriers and service providers is at the heart of changes in the way Marconi adds value for customers. In response to these market demands we have formed a global communications services organisation, Marconi Services, which provides higher value-added services, planning, building and operating networks for our customers.

In April 2000, Marconi's overall services offering was strengthened by the agreement to acquire MSI, a global provider of consulting, design and planning, and business and Operational Support Services software used by the wireless telecommunications industry.

Operating performance

Services' turnover more than doubled during the reporting period, increasing to £543 million from £244 million. This represented like-for-like growth of 32 per cent.

Operating profit before goodwill amortisation and exceptional items increased by 128 per cent, or 46 per cent like-for-like. Return on Sales before goodwill amortisation and exceptional items rose to 13.4 per cent from 12.1 per cent like-for-like.

The criteria for success in the rapidly growing market for communications network services are global presence, breadth of service portfolio and the ability to create tailor-made solutions for customers.

During the past year we have made very significant progress on all three fronts, both organically and through acquisition. The integration of FORE, RELTEC, Bosch Public Networks division and Australian Communications Solutions has increased our reach and capability beyond our traditional domestic markets. The acquisition of MSI will bring a world class consultancy and solutions capability in the mobile and broadband wireless markets.

Marconi Services now provides a broad range of support services to the communication and service provider industry worldwide. It helps to enable both established telecommunications operators and new competitors – as well as enterprise customers – to optimise their business returns from their network investments. Marconi Services is committed to plan, build and operate networks for our customers which reduces the burden of managing infrastructure and frees more of their resources to focus on serving their customers. In addition, we are leveraging our established systems integration capabilities to deliver innovative e-business applications in the converging IT and communications marketplace. We are transforming the use of communications technology and information management to provide imaginative solutions that will bring real value and new benefits into our customers' businesses to better reflect how their customers can harness the convergence of communication and information.

Our customers include many of the leading service providers and major organisations worldwide. Our main carrier and service provider customers include

Market overview

The explosion in demand for Internet and mobile services is presenting our customers with several significant challenges. They need to meet unprecedented growth rates in network traffic. They need to upgrade technologies to support new data and mobile services. They also need to compete in an increasingly liberated and competitive environment.

In order to focus on these challenges and remain competitive, network operators have begun to outsource many phases of the network lifecycle – from network design and planning, through building and deployment, to operation and maintenance. This enables them to focus on the business of developing, marketing and selling communications services to their customers. For instance, established operators such as BT, Telecom Italia and Telstra are looking for third parties like Marconi to maintain their network infrastructure, so that they can focus on upgrading their network technologies and deploying new services to customers. On the other hand, new operators in the carrier network market like Atlantic Telecom and NTL are looking for complete, turnkey solutions from Marconi, so that they can enter markets as quickly as possible, without the need for a large internal workforce.

Increasingly, customers require a service-based solution, including consultancy, network design and build, project management and operations support. This market dynamic is driving the significant growth rates in our Communications Services business, and is the reason why Marconi places service at the core of its customer relationships and management strategy.

A growing market

The global communications support services market is estimated at $82.5 billion worldwide, with an annual growth rate of 15 per cent. We believe that this growth rate will increase as operators continue to outsource the design, planning, building and operation of their networks. This outsourcing trend is accelerating as the explosion of new operators and service providers leads to the consolidation of network infrastructure. In turn, services such as telehousing, server farms and network operation centres are emerging to allow the networks of many operators to be located and operated together. This trend is creating a new market niche for our Communications Services business and we are very well placed in terms of capabilities and worldwide presence to take advantage of it.

Atlantic Telecom, BellSouth, British Telecom, Cable & Wireless, Colt, Deutsche Telekom, NTL, Omnitel, Sprint, Telecom Italia, Telstra and Viag.

Our business customers include Adelphia Business Solutions, Delta Air Lines, Hong Kong Mass Transit Railway Corporation, Italian Railways, London Underground, Railtrack, Shell and Thrucomm.

Our achievements

- A $650 million contract with Thrucomm in the United States. This is the first cross-selling synergy to be realised from Marconi's acquisition of MSI. It demonstrates Marconi's enhanced ability to win and implement wireless network plan, build and operate service contracts. Thrucomm will draw on expertise from Marconi's Communications Networks, Communications Services and Systems divisions, as well as MSI.
- A $40 million contract with Atlantic Telecom to provide network services that have enabled Atlantic to become one of the UK's first – and fastest – broadband Internet Service Providers (ISP) – giving them a head start in what will be an increasingly crowded market.
- A $120 million turnkey contract for planning and building the communications infrastructure for the prestigious West Coast Main Line modernisation programme for Railtrack in the UK. This will enable Railtrack to focus on its core business of running an efficient rail system.

Future growth

Future growth of our Communications Services business will come from five sources:

Increased volume of standard services
The volume of standard services including installation and commissioning, technical support, repair support and customer training, will increase due to the growth of Marconi Communications.

Increased demand for high value services
Significant growth in high value added services, including consultancy, network design, network planning and optimisation, turnkey network build, systems integration along with operation and maintenance will continue because of the market trend towards outsourcing.

Increased global reach
During the past 18 months we have continued to increase our presence in new territories with new acquisitions. Marconi is now well established on all continents, our global support backbone operates 24 hours a day, seven days a week with major hubs in the UK, the US and Australia. We now have more than 6,000 service personnel employed in more than 60 countries and a strong presence in key markets worldwide, notably the US, Germany, Italy, the UK, Australia and the Middle East.

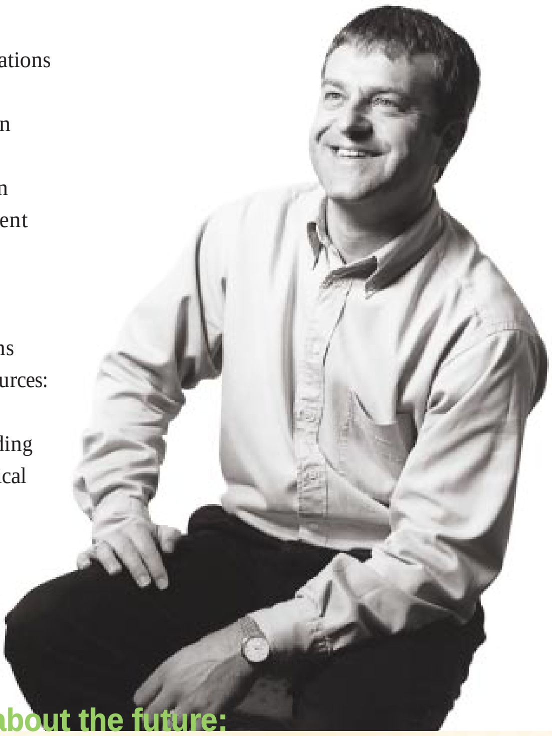
Coupled with the capabilities of MSI, Communications Services can now provide high value-adding network services such as design, planning and optimising wireless networks for our customers and offering third generation mobile and broadband wireless services.

As the global reach of our communications equipment business increases, it brings prospects for further growth in the Services business.

Realising Group synergies
The convergence of IT and communications, along with fixed and wireless networks, is presenting Communications Services with major systems integration opportunities. For instance, as our Systems business develops from being a supplier of infrastructure to being a supplier of applications, it will drive significant revenue opportunities to deliver our services to a broader market.

Entering new market sectors
Future market and revenue opportunities present Communications Services with new areas for potential growth. These are two examples:

- Enabling Applications Service Providers. We expect an explosion in the number of service providers delivering software applications services over their network. Through our recent acquisitions, we will be launching a new suite of services including facilities management, data centres and web hosting to support our customers' rapid entry into this fast-growth sector.
- Network infrastructure consolidation. As liberalisation continues to attract new entrants into the communications services market, operators will want to buy managed services, rather than build their own networks. During the year we have opened four state-of-the-art, multi-million dollar Network Operation Centres in the US, Europe and Australia to offer our customers new levels of services and solutions.



CEO Neil Sutcliffe talks about the future:

This has been a tremendous year for Marconi Services. We have formed a global services business focused on our global customers, increased our presence through a number of strategic acquisitions, strengthened our capability in terms of consultancy services and solutions, and launched several new global service offerings. At the same time the business has more than doubled its sales.

The pace of change in the markets we serve continues to accelerate and new opportunities are constantly emerging. The momentum we have created and the enormous progress we have made stand us in very good stead for the year ahead and beyond.

Review: Systems

Our Washington D.C. based Systems division consists of three global US-based businesses; Commerce Systems, Data Systems and Medical Systems. Each of them has a strong market position, based on leading technology and an established core of prominent, global customers. Just some of the leading brand names we count among our customers are Anheuser Busch, Boeing, Coca-Cola, ExxonMobil, FedEx, Ford, Glaxo-Wellcome, Nestlé, Shell, The Mayo Clinic and VW.

Market overview

The pattern of business of Marconi Systems continues to develop, with a large and growing proportion of revenues coming from the sale of software applications and information technology. Each business is building on its strongly competitive market position and is developing higher value-added software applications and Internet-based businesses. The impetus for growth in the market is technology that is enabling e-commerce, which puts value in our customers' hands by enabling them to run their businesses more efficiently. Due to the dramatic shift to doing business in the e-world, the markets within which the customers of each of our Systems businesses compete are undergoing huge secular shifts that are creating dramatic business opportunities for Marconi.

Strong demand exists in these and adjacent markets for applications, solutions and services which will enable our customers to reposition their business models to capitalise on the developing e-commerce opportunities and to create value by running their business more efficiently. Marconi Systems develops and applies these solutions for customers across a range of industries. The proportion of revenues attributed to the sale of software and information technology is significant today and is rapidly growing.

The Systems businesses will continue to develop in two ways. They are extracting maximum value from the traditional markets that they serve and are simultaneously developing new applications and services focusing on these huge e-commerce opportunities. Strong relationships with leading brand name customers and deep domain knowledge provide an excellent platform to introduce increasing levels of software and solution applications-based products and services.

Additionally, there are in excess of two million pieces of Marconi equipment in front of consumers every day. These are points of direct customer contact and, as the technology platform evolves, each represents an opportunity for Marconi to extract value through content, right down to the consumer level.

Resources for the development of applications and solutions will come not only from within each of the Systems businesses, but also from recent acquisitions and from our equity investments in early stage companies through Marconi Ventures. Examples of this are given within the individual Systems business descriptions and within the Capital section.

Operating performance

Systems' turnover increased 9 per cent, supported by businesses acquired in 1998 and 1999, such as Elscint and Logitron.

Operating profit before goodwill amortisation and exceptional items increased to £184 million from £151 million – growth of 22 per cent or 10 per cent like-for-like. Reflecting ongoing operational improvements, operating margins rose from 10.1 per cent to 11.3 per cent.

Medical Systems increased sales by 12 per cent. Marconi launched a range of next generation multi-slice Computed Tomography scanners in the third quarter of the financial year, underpinning sales growth in combination with strengthening conditions in the market for Magnetic Resonance imaging equipment.

Sales at Commerce Systems rose one per cent on a reported basis but fell by 13 per cent like-for-like, restrained by slowing customer demand compared to the prior year as a result of unprecedented consolidation among oil companies.

Data Systems' performance, with turnover rising 8 per cent, or 6 per cent like-for-like, reflected increasing sales momentum after the launch of new products at the beginning of the second half. A new generation of products for the secondary coding market is also due for launch in the current year.

Commerce Systems

This business is the world's most successful provider of retail automation and dispensing equipment to the petroleum retailing sector. Through its Marconi Online subsidiary it is establishing a growing presence in convenience stores and unattended intelligent vending. The Coca-Cola contract with Marconi Online will connect more than half a million vending machines to the Internet, and create new services and new marketing opportunities for our customer. In future, intelligent vending machines may interact with individual customers and allow cashless purchases. This is one example of how Marconi's intelligent vending solutions will revolutionise inventory and revenue management in the retail vending process.

In forecourt automation solutions, there are major innovations such as Internet-enabled dispensers, in-pump credit card readers and even pumps that instantly recognise individual customers. In the US, these retail automation products have achieved strong market acceptance and when they become available around the world demand is likely to accelerate, as major oil companies and retail fuel operators use them as marketing tools to drive incremental revenues. Supermarkets and hypermarkets are also strong players in the fuel retailing market, and this again offers significant opportunities for growth to Marconi. We believe that Commerce Systems is well positioned in these markets due to several factors including advanced technology, strong relationships with key customers, a worldwide distribution network and a broad solutions and products range. Looking to the future, key success factors will be our market coverage, retail automation products and interactive online applications.

CEO Mike Donovan talks about the future:

The Systems businesses are transforming themselves in two ways. They are getting better and better at extracting value from the traditional markets they've served, and are simultaneously developing new applications for their products and services. These are fast becoming knowledge management businesses.

To achieve the transformation, one of the great assets we start with is an extremely strong customer base. Basically, any major global blue chip brand you've heard of is likely to be a customer of Marconi Systems. That gives us a tremendously strong platform from which to develop the business…

Review: Systems

Data Systems

This business has an excellent blue chip client base and is the world leader in coding systems. Its growth opportunities lie in continuing to lead the market with new technology developments and exploiting an emerging business model based on providing customers with real-time information-based solutions, particularly in the e-logistics world.

The coding, marking and addressing industries continue to be driven by the need to incorporate more and more variable information such as production statistics, date codes and addresses or other personalised information onto products. In addition, the significant new growth driver in this market is the emergence of business-to-business and business-to-consumer e-commerce models.

We provide systems that enable customers to capture, track and manage information – systems that provide information linkages between the product and the producer throughout the e-commerce supply chain. Using our systems, customers will soon be able to track the location of their product in real time, anywhere, from the point of origination to the ultimate destination. The further movement towards total solutions for Supply Chain Management has created a number of new business opportunities in the information systems market. These opportunities include enabling Application Service Providers (ASPs) that offer Enterprise Resource Planning, Manufacturing Resource Planning and Customer Relationship Management applications for our customers.

Medical Systems

This business is a leading global provider of medical imaging equipment for both diagnostic and therapeutic uses. It is the world's largest distributor of radiological consumables and accessories and has a growing presence in the important and emerging business of Healthcare Information Systems.

The main diagnostic imaging technologies which we supply are Computed Tomography, Magnetic Resonance Imaging and Nuclear Medicine. Demand is increasing, fuelled by rising standards of living, increased life expectancies and by new, less invasive medical and surgical techniques. These are life saving technologies.

The ongoing digital revolution in computer and communication technology is the most important driver of change in the medical imaging industry today. To capitalise on the growth opportunities, we are focusing our research and development on the computer hardware and software applications which analyse sensing data from a variety of source technologies. Data needs to be transformed into information that can add value for the medical decision-maker, by improving either the accuracy or the timeliness of a diagnosis or therapy, and where appropriate, enable real time global image transfer to aid in diagnosis consultation.

Medical Systems' future development will harness our knowledge of Radiology and accelerate growth in Health Care Information Systems, including the electronic storage and transfer of medical images enabled by the Internet. We shall continue to develop this high-growth systems business as well as continuing to strengthen our competitive position in the image capture business.

CEO Mike Donovan talks about the future:

…There's another asset, in that we have more than two million pieces of equipment in front of consumers every day. These are points of direct customer contact and, as the technology platform evolves, every single one of them is an opportunity for Marconi to extract value.

All of the Systems businesses are Internet-literate, Internet-enabled businesses, so it's really about trying to be ahead of the curve in the way that business-to-business e-commerce will develop. It's also about trying to find that place in the business-to-…

Review: Capital

The strategic focus of Capital is increasingly on the development of emerging technology and applications businesses.

To accelerate the identification of these businesses, the Group has established a $100 million venture capital fund, Marconi Ventures, which will invest in early stage technology businesses with high growth potential or synergies with the core businesses.

We hold, with a view to development or disposal, other businesses with attractive returns on capital that may not fit our high growth, high technology models. We have also progressed with the programme of non-core disposals during the year.

We have divided the Marconi Capital companies into three groups: emergent technologies, development businesses and non-core businesses.

Operating performance

Turnover for the division decreased 8 per cent, or 4 per cent like-for-like, to £711 million. Operating profit before goodwill amortisation and exceptional items fell by 4 per cent, or 17 per cent like-for-like to £75 million. Operating margins rose to 10.5 per cent from 10.1 per cent, underpinned by operational improvements within the new technology businesses.

Emergent technologies

These are businesses which we believe have the potential to support the strategic plans of our core businesses by widening their range of technologies and applications, accelerating the development cycles of new products and services, or otherwise generating attractive financial returns.

We will develop these 'next wave' high technology activities by investing in external companies through Marconi Ventures, and by identifying internal projects that could be developed as stand-alone businesses. Marconi Ventures will invest alongside other Marconi businesses to jointly develop these new activities to ultimately combine them with one of our core business divisions, refuelling Marconi's growth in the future.

Early stage businesses in which we have invested to date include:

Xcert International: Marconi owns 25 per cent of Xcert International, which is a leader in web-based security, provides digital certificate software products and services for the Internet and private networks.

Ten Square: This business redefines the concept of the 'Digital Neighbourhood' by delivering digital media promotions, entertainment and community service messages at point-of-sale devices worldwide, securely over the Internet. Marconi Ventures invested in Ten Square jointly with our Commerce Systems business.

We are targeting further investment opportunities, including businesses that are developing products to facilitate business-to-business trading over the Internet, and businesses with emerging communications hardware products and software applications.

Development businesses

We are continually reviewing our development businesses in order to maximise value from emergent technologies opportunities. We currently identify as development businesses:

Fibreway has an installed fibre optic communications backbone in the UK which it leases to telecommunications operators and large corporations to provide high-speed, broadband communications capability.

The strong growth in the telecommunications market has created an attractive opportunity for Fibreway to develop its capability as an operator. Developing this capability within Marconi may bring us into conflict with some of our major customers. Consequently, we are currently considering alternative strategic options for the separation of Fibreway.

Payphones supplies a range of modular payphones for outdoor and indoor applications and has an installed base exceeding 800,000 units. The business is focusing on developing a new range of payphones with Internet access capability.

Marconi Software Solutions provides systems integration and application development capabilities using Oracle, Java, C++ and other software language support.

Marconi Applied Technologies designs, manufactures and supplies electronic components and systems for a range of sectors, including communications, industrial, medical and science, military, safety and security.

Non-core businesses

Our non-core businesses include General Domestic Appliances (GDA), a 50 per cent owned joint venture with US company General Electric. This business manufactures domestic appliances with UK leading brand names such as Hotpoint, Creda, Cannon, Redring and Xpelair. Other businesses are Woods, an air movement systems company; Alstom, in which we hold a 24 per cent stake; and Marconi Property which manages our property assets.

These businesses are being managed for value rather than growth, as they provide an attractive return on capital but do not fit the high growth, high technology direction of Marconi.

…consumer trade where we can extract value in supporting our customers, as they in turn serve their customers.

We have excellent products and a really strong customer base. We have great opportunities to grow value in the core equipment businesses in Systems. In parallel, we are accelerating the growth of our customers' e-businesses and our applications businesses.

Finance Director's Review

Group financial performance

The Group has undergone fundamental restructuring and refocusing during the year. It has also integrated a number of substantial and strategically important acquisitions. This means that there has been significant growth in 'headline' numbers. However, there has also been strong growth in the Group's underlying 'like-for-like' results which compare the performance to the prior year as if the current group was constructed in the same way during both years. Group management regards the like-for-like figures as a more relevant measure of performance in most circumstances and these are therefore described in this review where relevant.

Sales

Group turnover rose 40 per cent to £5,724 million from £4,090 million the previous year. On a like-for-like basis this represents growth of 11 per cent.

Operating profit

Group operating profit before goodwill amortisation and exceptional items rose to £750 million from £508 million, an increase of 48 per cent or 22 per cent like-for-like. The Communications businesses increased operating profit to £515 million from £295 million, representing growth of 75 per cent or 38 per cent like-for-like.

The Group's operating margins, before goodwill amortisation and exceptional items, rose to 13.1 per cent from 12.4 per cent or 11.9 per cent like-for-like in the previous year.

Earnings per share for Marconi, before goodwill amortisation and exceptional items, increased by 17.4 per cent to 16.9 pence.

Research and development

In keeping with the Group's focus on transforming communications and information, Research and Development investment increased by 64 per cent or 21 per cent like-for-like, to £471 million.

Distribution policy

A final dividend of 3.4 pence per share has been recommended, payable on 11 August 2000. Together with the interim dividend of 1.8 pence, this gives a total dividend for 1999/2000 of 5.2 pence. This is in line with the Group's distribution strategy of covering the dividend broadly 3.25 times by earnings per share before goodwill amortisation and exceptional items.

Goodwill amortisation

The Group adopted US GAAP treatment of goodwill, which is becoming the industry standard for technology companies. Therefore, the average useful life of the goodwill relating to the Group's acquisitions has been reduced from 20 years to approximately 10 years. In addition, in-process R&D of the acquired businesses has been written off in the first year of the Group's ownership. As a result of these changes, the Group's goodwill charge (including share of joint ventures) was £765 million. The full year goodwill charge in the current year is expected to be approximately £500 million.

The Group has undergone fundamental restructuring and refocusing during the year. It has also integrated a number of substantial and strategically important acquisitions. Careful management and financial control has been maintained throughout the period and the Group's like-for-like performance has also significantly improved.

Exceptional items

Exceptional items (including share of joint ventures) charged to operating profit totalled £107 million (1999: £53 million) including Y2K costs (£43 million), restructuring of existing businesses (£44 million) and restructuring of acquisitions (£20 million).

Other exceptional items totalled a profit of £737 million. This total comprised dividends and other cash received by Marconi from the defence business that was separated from GEC (at the time Marconi merged with the non-defence businesses), minus the cost of establishing the Marconi share option plans that were approved by shareholders on 3 November 1999 and other related costs of effecting the separation and launching the new Company.

Interest

The Group's interest costs in the year were £103 million, compared with interest receivable last year of £59 million. The increase results primarily from the cost of acquisitions, partly offset by the interest on the cash received on the separation of the defence business, which occurred later in the year.

Taxation

Taxation on profit on ordinary activities, before goodwill amortisation and exceptional items, was £196 million, resulting in an effective tax rate of 30 per cent. Taxation on exceptional items, including those related to the separation, was a net credit of £198 million, producing a total tax credit for the year of £2 million.

Cash flow

Operating cash flow over the reporting period was an inflow of £610 million, compared with an inflow of £434 million in the corresponding period last year.

Non-operating cash flow, including net debt acquired, was largely driven by the US and other acquisitions, which cost £4.2 billion, less the £1.4 billion of cash received by the Group from the separation of the defence business.

Capital expenditure

Net capital expenditure for the period was £265 million, compared with £167 million last year. This figure represents 171 per cent of depreciation charged against profit.

Post balance sheet event

On 20 April 2000, Marconi announced an agreement to acquire MSI, a global provider of consulting and planning services and operational support software used by the wireless communications industry, for an initial consideration of $618 million (£391 million).

Group financial management

Treasury policies

The Group's Treasury activities are co-ordinated by the Director of Treasury and Risk Management. In addition to the treasury, project and export finance functions, the department is responsible for insurance risk management, and monitors the exposures arising from the various Marconi employee share plans. The department does not operate as a profit centre. Treasury advises operational management on treasury matters and undertakes all derivative transactions except certain standard forward exchange contracts relating to the hedging of foreign currency transaction exposures arising in the operating businesses.

Financial instruments

The Group uses financial instruments, including derivatives (principally interest rate swaps, cancellable options, currency swaps and forward foreign currency contracts) to manage interest rate and currency risk exposures. More information on financial instruments is provided in Note 25 to the Accounts.

It is the Group's policy that there is no trading in financial instruments.

The main risks faced by the Group in the financial markets are interest rate risk, liquidity risk, foreign currency risk, counterparty risk and share price risk. The Board reviews and agrees policies for managing each of these, which are summarised below:

Interest Rate Risk: Marconi's net debt was £2,145 million at 31 March 2000, and changed from a net cash position of £624 million at 31 March 1999. This was primarily due to the purchases of RELTEC Corporation and FORE Systems and other acquisitions for a combined $6.6 billion (£4.2 billion), including net debt acquired.

The Group's policy is to maintain at least 50 per cent of debt at fixed rates of interest. At 31 March 2000, 79 per cent of the Group's interest-bearing borrowings were at fixed rates after taking account of interest rate swaps. Of this total, 55 per cent were at fixed dollar rates of interest and 24 per cent were at fixed euro rates of interest.

Finance Director's Review

The term structure of interest rates is managed in observance of this policy using derivative financial instruments such as interest rate swaps and cancellable interest rate swaps. A total of $1.9 billion of swaps and cancellable interest rate swaps were taken out to fix the cost of the borrowings drawn to pay for the acquisition of RELTEC and to fix the cost of the debt acquired. The average fixed rate payable on these swaps is 5.69 per cent per annum. A further €1.0 billion of swaps and cancellable interest rate swaps were taken out as a pre-hedge for Marconi's Eurobonds, as described below. The average fixed rate payable on these swaps is 5.08 per cent per annum.

Due to the high proportion of fixed rate debt and the small net exposure on its floating rate debt and cash and investments, the Group's interest charge has limited exposure to interest rate movements. The average amount of cash and investments exceeded the average amount of floating rate debt for the year. Consequently, a one percentage point increase in market interest rates would have increased profit before taxation in the fiscal year 2000 by approximately £3 million, or less than one per cent of reported profits.

Liquidity Risk: At 31 March 2000, the Group's cash and investments totalled £624 million, of which £205 million was denominated in sterling, £206 million in US dollars and £149 million in euro and the balance of £64 million in other currencies.

Deposits are generally in short term investments with low price risk. In the year ended 31 March 2000, the average interest rate received on cash and liquid investments was approximately 4.3 per cent per annum. The largest proportion of investments was in sterling deposits – the Group held an average of £415 million in sterling deposits, earning an average interest rate of 5.4 per cent per annum.

The Group funds its activities through retained profits and, where appropriate, by bank borrowings and the debt capital markets. Marconi has obtained credit ratings for two eurobond issues from Moody's and Standard & Poor's of A3/BBB+, respectively. These bond issues were completed on 30 March 2000 and are comprised of €500 million of bonds due 30 March 2005, and €1,000 million of bonds due 30 March 2010. The net proceeds of these issues were used to reduce borrowings denominated in euros drawn under Marconi's syndicated bank facilities.

Marconi has two committed multi-currency revolving credit facilities syndicated with its main relationship banks, amounting in total to €8.3 billion. The Group drew $1.9 billion in April 1999 under these facilities to pay for the acquisition of RELTEC Corporation, and $4.3 billion in June 1999 forming the majority of the consideration for the acquisition of FORE Systems. At 31 March 2000 drawings under these facilities amounted to £1,612 million, with a weighted average maturity of 1.3 years, resulting in unused commitments of £3,495 million. These formed the majority of the total undrawn Group commitments of £3,514 million.

Foreign Exchange Risk: The Group is exposed to movements in foreign exchange rates against sterling for both trading transactions and the translation of net assets and the profit and loss accounts of overseas subsidiaries.

Exchange rate sensitivity

10 per cent reduction in value of:	Percentage reduction in Group reported sterling operating profit before goodwill amortisation and exceptional items
US$	(4.1)
Euro-traded currencies	(0.4)
Other	(0.5)
Total	(5.0)

The foreign currency management policy of the Group seeks to minimise the impact of fluctuations in exchange rates on future cash flows and requires subsidiaries to hedge firm transaction exposures against their local currency at the time the exposure is identified. These exposures are hedged by the use of spot and forward foreign exchange contracts. The Group uses derivative instruments to hedge certain commercial contracts, denominated in foreign currencies, in order to protect the period from tender to contract effectiveness and certain contingent exposures. These transactions are carried out by specialist Treasury personnel.

The Group's foreign exchange exposure has been affected by the large US acquisitions completed in the year and the separation of the defence businesses in November 1999. The main trading currency of the Group is the US dollar, followed by sterling and then the euro.

The Group has overseas subsidiaries that earn profits in their local currencies. It is not the Group's policy to hedge the exposures arising from the translation of these overseas profits into sterling.

Gross borrowings at year end were £2,769 million, and 100 per cent of these were denominated in foreign currencies in order to form a hedge for the Group's investments in currencies other than sterling. Of these, 56 per cent denominated in US dollars formed a hedge for the Group's investment in the US, and 43 per cent denominated in euros formed a hedge for the Group's investments in the eurozone.

Under UK tax regulations, Marconi is exposed to tax on changes in the translations into sterling of its foreign currency borrowings. Marconi has entered into derivative contracts with certain of its banks to eliminate the cash flow exposure resulting from these tax payments.

Marconi has subsidiaries in most of the European countries which are converting to the euro, and the major subsidiaries are located in Italy and Germany. To ensure that all eurozone subsidiaries convert in a timely and efficient manner, Marconi has established a Euro Programme Management Office to actively support and co-ordinate a euro programme throughout the Group. The programme's objectives are for all Marconi's eurozone subsidiaries to be compliant well before 1 January 2002 (the earliest date for the introduction of euro denominated notes and coins); and for the Group to be capable of conducting commercial and financial transactions, and account and report in euros, as and when required.

Counterparty Risk: All deposits are made with creditworthy and authorised counterparties. All forward contracts, swaps and other derivative contracts, as described above, are similarly managed to ensure that the benefits of such financial hedging are subject to controlled counterparty risk.

The Group uses export credit agencies to manage political and credit risks on major contracts and makes extensive use of export credit insurance in respect of small to medium-sized contracts.

Marconi, like its competitors, is facing demand to provide finance to its customers. We have responded by developing financing arrangements that are attractive to our customers whilst limiting the risk to Marconi. Only modest

Finance Director's Review

sums of vendor finance have been committed to customers to date, and the terms facilitate the early syndication to financial institutions and investors.

Exposure to customer credit risk through the provision of vendor finance is strictly controlled by a Credit Committee, comprising senior financial management at the corporate head office.

Risks are laid off to third parties wherever possible, and it is Marconi's intention to transfer outstanding loans and commitments to financial institutions and investors at the earliest practicable time.

Insurance Risk Management: Marconi maintains insurance to protect the Group from catastrophic loss in respect of public and product liability, material damage, business interruption and other major insurable risks. With effect from 31 March 2000, global insurance policies were implemented providing higher overall limits and broader coverage at lower cost. The Group is working with its insurers and advisers to improve its loss prevention and mitigation processes, and to integrate acquired entities into its risk management and insurance programmes.

Marconi Share Price Risk: Marconi has issued share options to employees under a number of different option plans. Options may be satisfied by a transfer of existing Marconi ordinary shares acquired on the market by the Marconi Employee Trust or other vehicle, or by an issue of new Marconi shares. It is intended to use existing shares to satisfy options under some of the plans. In order to hedge some of the potential cost of acquiring existing shares, the Marconi Employee Trust has entered into contracts to purchase shares in the future at prices based on the price at the date of contract. If the share price were to fall by 10 per cent, the fair value of these contracts would fall by £19 million. Marconi may use new shares, where appropriate, to satisfy options under the plans.

Internal Controls: Internal controls are maintained in order to give the Board reasonable assurance as to the Group's control over its assets, liabilities, contractual commitments and business conduct. The outsourced internal audit function reports to management and the Audit Committee on these internal controls. The Group expects to report next year in full compliance with the Turnbull Committee's guidance on internal controls. The key financial controls are outlined in detail in the Directors' Statement on Internal Financial Control on page 46.

John Mayo

John Mayo
Finance Director

Financial Contents

Directors

Each of the Directors was appointed to the Board of Marconi plc on 4 October 1999, with the exception of Mr M J Donovan and Mr M W J Parton who were appointed on 1 January 2000.

Sir Roger Hurn *Chairman*
Aged 61. Appointed to the GEC Board in 1998, Sir Roger was formerly Chairman of Smiths Industries PLC. He is Chairman of Prudential plc, a non-executive director of Imperial Chemical Industries PLC, Deputy Chairman of Glaxo Wellcome PLC and Chairman of the Court of Governors at the Henley Management College.

Lord Simpson *Chief Executive*
Aged 57. Appointed to the GEC Board in 1996, Lord Simpson is a non-executive director of Imperial Chemical Industries PLC and Nestlé S.A. He was Chairman and Chief Executive of Rover Group and subsequently Deputy Chief Executive of British Aerospace Plc and Chief Executive of Lucas Industries Plc.

W M Castell *Non-executive Director*
Aged 53. Appointed to the GEC Board in 1997, Mr Castell has been Chief Executive of Nycomed Amersham plc (formerly Amersham International plc) since 1990, having previously been Commercial Director on the board of Wellcome plc.

The Rt Hon The Baroness Dunn DBE *Non-executive Director*
Aged 60. Appointed to the GEC Board in 1997, Baroness Dunn is an Executive Director of John Swire & Sons Ltd, a non-executive Deputy Chairman of HSBC Holdings plc and a non-executive director of Christie's Fine Art Ltd; she was formerly Senior Member of the Hong Kong Executive Council and Legislative Council.

M J Donovan *Chief Executive Officer, Marconi Systems and Marconi Capital*
Aged 47. Appointed to the Board in January 2000, Mr Donovan has held a number of senior management positions in the Rover Group (1976 to 1991), Vickers plc (1991 to 1994) and British Aerospace Plc (1994 to 1998). Mr Donovan became Chief Executive of GEC's Industrial Electronics Group in 1998 and is based in the US.

J C Mayo CBE *Finance Director*
Aged 44. Appointed to the GEC Board in 1997, Mr Mayo was formerly Finance Director of Zeneca Group PLC and a Director of S.G. Warburg & Co Ltd prior to that.

R I Meakin *Personnel Director*
Aged 50. Appointed to the GEC Board in 1998, Mr Meakin has responsibility for the Group's personnel activities. He is on the board of Young Enterprise and is a member of the Steering Board at the Radiocommunications Agency and is Chairman of the DTI and D*f*EE's Education and Training Export Group. Mr Meakin was formerly Personnel Director of British Aerospace Plc.

M W J Parton *Chief Executive Officer, Marconi Communications Networks*
Aged 45. Appointed to the Board in January 2000, Mr Parton has held a number of finance appointments in ICL plc (1977 to 1980), GEC-Marconi Ltd (1980 to 1986) and STC Telecommunications Ltd (1986 to 1991). He joined GEC in 1991 as Finance Director of GPT and was appointed Managing Director of GPT's Public Networks Group in 1995, Managing Director of GEC's Industrial Group in 1997, and Chief Executive Officer of Marconi Communications Ltd at the time of its formation in July 1998.

Sir Alan Rudge CBE *Non-executive Director*
Aged 62. Appointed to the GEC Board in 1997, Sir Alan is Chairman of the Remuneration Committee and the senior independent non-executive Director. Sir Alan was formerly Deputy Chief Executive of British Telecommunications plc. He is currently Chairman of WS Atkins plc, ERA Technology Ltd and non-executive Chairman of Metapath Software International, Inc., a Fellow of the Royal Academy of Engineering and the Royal Society and a Past President of the Institution of Electrical Engineers. Sir Alan is also a non-executive director of Great Universal Stores Plc and MSI Cellular Investment Holdings BV.

Hon Raymond G H Seitz *Non-executive Director*
Aged 59. Mr Seitz, who was Ambassador of the United States to the Court of St James's from 1991 to 1994 and is Vice Chairman of Lehman Brothers International (Europe), was appointed to the GEC Board in 1994. He is also a non-executive director of British Airways plc, Cable and Wireless plc, Rio Tinto plc, Telegraph Group plc, Chairman of Authoriszor, Inc. and a Trustee of the National Gallery and the Royal Academy.

N J Stapleton *Non-executive Director*
Aged 53. Appointed to the GEC Board in 1997, Mr Stapleton is Chairman of the Audit Committee. He is Chairman of Veronis, Suhler International Ltd and a non-executive director of Sun Life & Provincial Holdings plc. He was previously Co-Chief Executive of Reed International plc and Chairman of Reed Elsevier (UK) Ltd. Mr Stapleton is a Director of The Royal Opera House Trust and a member of the Financial Reporting Review Panel.

Secretary
N C Porter

Registered Office
One Bruton Street, London W1X 8AQ
Telephone: 020 7493 8484

The Directors have considered the Committee on Corporate Governance's Combined Code issued by the London Stock Exchange in June 1998. The Combined Code consolidates the principles of good governance and code provisions of the earlier Cadbury, Greenbury and Hampel Committees. A summary of the Company's system of applying the principles, and the extent to which the provisions in Section 1 of the Combined Code have been complied with, are set out below. Section 1 of the Combined Code establishes 14 Principles of Good Governance, which are split into four areas:

1 The Board

The Company is controlled through the Board of Directors which comprises the Chairman, five executive Directors and five non-executive Directors who, with their different backgrounds, bring with them a wide range of expertise and experience to the Company's affairs. The Board considers all of the non-executive Directors to be independent as they are independent of the Company's executive management and free from any business or other relationship which could materially interfere with the exercise of their independent judgement. There is a clear division of responsibility between the Chairman and Chief Executive with no single individual having unfettered powers of decision. The Chairman is responsible for running the Board and ensures that all Directors receive sufficient relevant information on financial, business and corporate matters to enable them to participate effectively in Board decisions. The Chief Executive's primary role is the co-ordination of the Company's businesses and the development and implementation of strategy. On 1 February 2000 the Board appointed Sir Alan Rudge as the senior independent non-executive Director as recommended by the Combined Code.

The Board ordinarily meets six times a year but holds additional meetings when circumstances require. During the period 30 November 1999 (the date of listing of the Company) to 31 March 2000, the Board met on two occasions. There is frequent contact between meetings to progress the affairs of the Company. Broadly, attendance at Board and Committee meetings was in excess of 95 per cent. The non-executive Directors meet with the Chairman and Chief Executive at least twice a year to discuss a wide range of matters affecting the Company and have the opportunity to arrange additional meetings to consider and discuss with executive Directors the Company's business strategy.

Directors receive appropriate training on appointment and then as necessary. They attend an induction programme which aims to provide an understanding of the Company, its strategy, structure, geographical spread of operations, financial position, the industries in which it operates, its products and technologies, its people and, where appropriate, legal responsibilities as a director. The Directors have access to the advice and services of the Secretary and there is an approved procedure by which all Directors can obtain independent professional advice in furtherance of their duties, if required; this procedure is reviewed periodically.

The Board, which has reserved certain specific matters to itself, is responsible for overall Group strategy, acquisition and divestment policy, approval of major capital expenditure projects, consideration of significant financial matters and it reviews the financial performance and strategic direction of the operating businesses.

In accordance with the provisions of the Company's Articles of Association, at this year's Annual General Meeting all Directors are required to retire from office and seek re-election. The names and biographical details of all the Directors are set out on page 35.

The Board has established a number of committees with defined terms of reference, which are reviewed periodically, and receives reports of their proceedings. The principal committees, their membership and a brief description of their terms of reference, as of 18 May 2000, are as follows:

Audit Committee

N J Stapleton *Chairman*
W M Castell
The Rt Hon The Baroness Dunn
Sir Alan Rudge
Hon Raymond G H Seitz

The Committee reviews the Company's financial statements and reports, its financial and corporate controls and accounting policies. All the members of the Committee are independent non-executive Directors. The Company's internal and external auditors attend meetings and have the opportunity to raise matters or concerns in the absence of executive Directors.

Nomination Committee

Sir Roger Hurn *Chairman*
W M Castell
The Rt Hon The Baroness Dunn
Sir Alan Rudge
Hon Raymond G H Seitz
N J Stapleton

The Committee makes recommendations to the Board on all proposed new appointments of Directors. The Chairman and the non-executive Directors who are members of this Committee are independent.

Remuneration Committee

Sir Alan Rudge *Chairman*
W M Castell
The Rt Hon The Baroness Dunn
Hon Raymond G H Seitz
N J Stapleton

The Committee determines, on behalf of the Board, the broad framework for executive remuneration including the remuneration of executive Directors. All members of the Committee are independent non-executive Directors.

Executive Committee

Lord Simpson *Chairman*
J S Brooks
M J Donovan
J R Fryer
J I Gordon
S Gualano
J C Mayo
R I Meakin
M W J Parton
N D Sutcliffe
J N Viljoen

The Committee, which normally meets monthly, is appointed by the Board and its membership comprises the executive Directors and senior executives. A quorum requires the presence of at least two executive Directors. The Committee's main functions include approval of the Group's business plan and budget, the review of performance against plan, the Group's strategies in areas including technology, people, information technology, corporate communications and change programmes, prior to submission to the Board for its approval. This Committee also deals with day-to-day matters of a routine nature.

The Secretary of the Company is Secretary to all Board Committees.

2 Directors' Remuneration

In accordance with the requirements of the Combined Code, the Board has approved the terms of reference of the Remuneration Committee, as with all Board committees. The Report to Shareholders by the Board on Directors' Remuneration, which can be found on pages 41 to 45, sets out the Company's remuneration policy, procedures and the remuneration of individual Directors.

3 Relations with Shareholders

The Company gives communication with shareholders a high priority. The announcement of interim and final results provides opportunities for the Company to answer questions from institutional investors covering a broad range of issues and, in addition, there is regular dialogue with institutional shareholders to ensure a mutual understanding of objectives. The Company's website (www.marconi.com) provides shareholders with information about the Company including the annual and interim report, details of recent announcements, investor presentations and share price information.

The Company aims to deal expeditiously with all enquiries from individual shareholders on a wide range of matters. Individual shareholders also have the opportunity of attending the Annual General Meeting to put questions to the Chairman and the chairmen of Board committees; Directors also meet informally with shareholders before and after the meeting. The Company keeps under review ways in which it can communicate more effectively with its shareholders throughout the year as well as at the Annual General Meeting. An exhibition will be mounted at the Annual General Meeting covering a wide range of the Company's products and technology. It is the Company's practice to send the Notice of the Annual General Meeting and related papers to shareholders at least 20 working days before the meeting and to propose separate resolutions on each substantially separate issue. The Company indicates the level of proxy votes lodged in respect of each resolution proposed at its Annual General Meeting following each vote on a show of hands. In the event of a poll being called the result is announced to the London Stock Exchange.

4 Accountability and Audit

Financial Reporting

The Board includes a detailed review of the performance and financial position of each division on pages 18 to 27. Reading these alongside the Chairman's Statement on page 11, the Chief Executive's Review on page 12, the Finance Director's Review on page 28 and the Directors' Report on page 38, the Board seeks to present a balanced and understandable assessment of the Group's position and progress.

Internal Control

The Directors' Statement of Internal Financial Control can be found on page 46.

Audit Committee and Auditors

The Audit Committee meets at least three times a year with Mr J C Mayo, Finance Director and other executive Directors, attending by invitation. The Committee overviews the monitoring of the adequacy of the Company's internal controls, accounting policies and financial reporting and provides a forum through which the Company's external audit and finance functions report to the non-executive Directors. The duties of the Audit Committee also include keeping under review the scope and results of the audit and its cost effectiveness. The Committee also receives reports from the external and internal auditors on a regular basis.

Compliance Statement

The Listing Rules of the Financial Services Authority require the Board to report on compliance with the provisions contained in Section 1 of the Combined Code throughout the accounting period. As permitted by the London Stock Exchange, the Company has complied with the transitional approach of Combined Code provision D.2.1. on internal control by only reporting on internal financial control in accordance with the guidance for directors on internal control and financial reporting that was issued in December 1994. On 1 February 2000, the Board appointed Sir Alan Rudge as senior independent non-executive Director in accordance with provision A.2.1. of the Combined Code.

Save for the nomination of a senior independent non-executive Director for the period from the date of listing to 31 January 2000, the Directors consider that the Company has complied with the provisions of Section 1 of the Combined Code throughout the period from the date of listing to 31 March 2000.

Internal control: the Turnbull Committee

The Combined Code has extended the existing requirement in respect of the Directors' review of the effectiveness of the Group's system of internal financial control to include all internal controls, including financial controls, operational controls, compliance and risk management.

Internal Control: Guidance for Directors on the Combined Code (the Turnbull guidance) was published in September 1999 to provide guidance in applying these extended requirements.

The Directors have established procedures necessary to implement the guidance by formalising their Marconi Business Risk Management Process which has been implemented across the Group. The Directors therefore consider they will be in a position to report to shareholders on internal controls in full compliance with the guidance next year.

Directors' Report

Incorporation
The Company was incorporated in England and Wales on 17 September 1999.

Share Capital
On incorporation, the Company had an authorised share capital of £300,000,000 divided into 6,000,000,000 ordinary shares of 5 pence each of which two shares were issued. On 1 October 1999, 999,998 ordinary shares of 5 pence each were allotted at par but not issued against an undertaking to pay up the shares in cash, in order to enable the Company to obtain its certificate to do business under Section 117 of the Companies Act 1985. In accordance with the terms of the reconstruction of The General Electric Company, p.l.c. (GEC), 2,723,486,794 ordinary shares of 5 pence each were issued by the Company, credited as fully paid, to the former holders of GEC ordinary shares of 5 pence each on the register at the close of business on 26 November 1999, on the basis of one ordinary share of 5 pence each in the Company for one ordinary share of 5 pence each in GEC.

Reconstruction of GEC
In November 1999, following sanction by the High Court of a Scheme of Arrangement pursuant to Section 425 of the Companies Act 1985, GEC undertook an internal reorganisation and reconstruction under Section 110 of the Insolvency Act 1986 (the transaction). As a result of those steps, the former businesses of GEC became owned directly or indirectly by two new companies – MES Holdco (which held GEC's defence business – MES) and Marconi plc (which held GEC's remaining businesses). British Aerospace Plc (now named BAE Systems Plc) (BAe) acquired MES Holdco in consideration for the issue to former GEC shareholders of approximately 0.428 new BAe ordinary shares plus 13.54 pence of BAe Capital Amortising Loan Stock for each GEC share held. GEC shareholders also received one share in Marconi plc for each GEC share held prior to the reorganisation and reconstruction.

The transaction was completed on 29 November 1999; shares in the Company were admitted to the Official List of the London Stock Exchange on 30 November 1999 and dealings in the Company's shares commenced on that day.

Directors
The present members of the Board are set out on page 35, together with their biographical details.

Upon incorporation on 17 September 1999, Mr N C Porter and Mr D H Reid were appointed Directors.

On 4 October 1999, Mr W M Castell, The Rt Hon The Baroness Dunn, Sir Christopher Harding, Sir Roger Hurn, Mr J C Mayo, Mr R I Meakin, Sir Alan Rudge, Hon Raymond G H Seitz, Lord Simpson and Mr N J Stapleton were appointed Directors; Sir Roger Hurn was appointed Chairman and Lord Simpson was appointed Chief Executive. On the same date, Mr N C Porter and Mr D H Reid resigned as Directors.

Sir Christopher Harding died on 13 December 1999.

Mr M J Donovan and Mr M W J Parton were appointed to the Board on 1 January 2000.

In accordance with the recommendation of the Hampel Committee's Combined Code, Sir Alan Rudge was appointed senior independent non-executive Director on 1 February 2000.

In accordance with the provisions of the Company's Articles of Association, having been appointed during the period since incorporation, all of the present Directors, being eligible, offer themselves for re-election at the forthcoming Annual General Meeting.

The Directors' interests in the shares of the Company are shown in the Report to Shareholders by the Board on Directors' Remuneration on page 44.

Profits and Dividends
The profit for the year to 31 March 2000 on ordinary activities after taxation and minority interests amounted to £522 million.

The Directors recommend a final dividend of 3.4 pence per ordinary share which, together with the interim dividend of 1.8 pence already paid, makes a total of 5.2 pence per ordinary share at a cost of £142 million. Subject to the approval of the Annual General Meeting, the final dividend will be paid on 11 August 2000 to the shareholders registered at the close of business on 23 June 2000.

Review of the Group
An analysis of turnover and profit for the Company, its subsidiaries and its share of joint ventures and associates is shown on pages 54 and 55. A commentary on the activities of the Group including research and development activities and likely future prospects is contained in the Chief Executive's Review on pages 12 to 15.

The Company acts as a holding company; its subsidiaries and associated companies are principally engaged in the provision of communications equipment and services together with associated support applications. Further details of the principal subsidiaries and associated companies are shown on pages 76 and 77.

Structure of the Group
In addition to the reconstruction of GEC (now known as Marconi Corporation plc) mentioned above, the following acquisitions and disposals, other than those of a minor nature, were made by the Group during the year to 31 March 2000:

a RELTEC Corporation was acquired in April 1999;
b the card technology manufacturing business of Marconi Communications was sold to ID Data Systems Ltd in May 1999;
c FORE Systems, Inc. was acquired in June 1999;
d the business and assets of RDC Communications Ltd were acquired in August 1999;
e the High Field Whole Body MRI Business of SMIS Ltd was acquired in September 1999;
f a 27 per cent interest in Atlantic Telecom Group PLC was acquired in December 1999;
g the SDH and DWDM manufacturing business of Nokia was acquired in December 1999;
h the Bosch Public Networks division was acquired in January 2000;
i the Australian Communications Solutions business of SCITEC Ltd was acquired in March 2000;
j the Facilities Management and Processing Services businesses of EASAMS Ltd was sold to ITNET plc, in March 2000;
k Marconi Communications, Network Components & Services – Europe Ltd and Shanghai RELTEC Communications Technology Co. Ltd were sold to Viasystems Inc. in March 2000;
l certain business and assets of the Harvest Electronics Group were acquired in March 2000; and

m a 25 per cent interest in Xcert International, Inc. was acquired; 15 per cent was acquired in August 1999 and a further 10 per cent in March 2000.

Since 31 March 2000, the following acquisitions and disposal have been made by the Group:

n the assets of The Software Works! were acquired in April 2000;

o the remaining 30 per cent interest not already owned by the Group in Marconi Commerce Systems Latin America s.a. was acquired in April 2000;

p Intervest s.a. was acquired in April 2000;

q an agreement to acquire Metapath Software International, Inc. was signed in April 2000; and

r a conditional agreement to dispose of the Avery Berkel group was signed in March 2000. The disposal is expected to be completed at the end of May 2000.

Dividend Re-Investment Plan

The Company introduced a Dividend Re-Investment Plan to coincide with the payment of the interim dividend in February 2000. It is the Board's intention to offer shareholders the opportunity to purchase shares in the Company through the Plan in respect of future dividends. In addition, the Company operates a share purchase scheme to provide individual shareholders with the opportunity to acquire Marconi shares through a low cost facility at any time during the year (see page 80 for details).

Substantial Holders of Share Capital

Prudential plc has notified the Company that it is the holder of 91,860,227 ordinary shares of 5 pence each in the Company, being approximately 3.36 per cent of the issued share capital as at 18 May 2000. So far as the Directors are aware, no other person holds a substantial part of the issued share capital of the Company.

Payment of Creditors

It is the policy of the Group that operating subsidiaries agree with suppliers the best available terms taking account of quality, delivery, price and period of settlement and to abide by those terms.

Marconi plc is a holding company and, as distinct from the Marconi Group, has no revenue and no trade creditors. It is therefore not possible to provide statistics for the Company as required by the Companies Act.

Employees

Employees play a critical role in the success of the Marconi Group. A report of our personnel initiatives during the year can be found on pages 8 and 9.

Full and fair consideration is given to applications for employment from people with disabilities having regard to their aptitudes and abilities; special arrangements are made to support the continued employment of those who become disabled. Wherever practical, access, facilities and training programmes are made available allowing people with disabilities to participate at work to the best of their ability.

Individual employees and their representatives are kept informed of current business issues through briefing groups, newspapers, training seminars and professional networks as well as through more formal consultative procedures.

During the period when the transaction with BAe was pending, no share options were granted to employees by GEC. In order to attract and retain employees during this period, phantom options were granted to 311 employees in respect of 4,310,228 GEC ordinary shares at subscription prices of between £4.78 and £5.385 per share. Following the reconstruction of GEC and listing of Marconi (mentioned above) these phantom options were converted into options over Marconi shares. Phantom options were also granted to employees of companies acquired during the same period in exchange for the options granted to them by their employing company; for example, employees of RELTEC Corporation and FORE Systems. Outstanding GEC phantom options were exchanged for Marconi phantom options on 30 November 1999. As at 31 March 2000, 70,392,525 Marconi phantom options were outstanding.

In connection with the reconstruction of GEC and the listing of Marconi, employees remaining in the Marconi Group were given the opportunity to exchange their existing GEC options for options over Marconi shares on a value-for-value basis and, of such options, a total of 31,882,007 Marconi shares were outstanding at 31 March 2000. On 30 November 1999, options over 20,025,493 Marconi shares were granted at a subscription price of £8.015 per share under the Marconi 1999 Stock Option Plan to those employees electing to exchange certain of their options.

Since 30 November 1999 (the date of listing of Marconi plc) the following options have been granted:

a to 37,630 employees in respect of 37,626,863 ordinary shares of 5 pence each at nil cost under the Marconi Launch Share Plan. The options are exercisable provided that two conditions are met; firstly, the market value of a Marconi share doubles to £16.03 during the period 30 November 1999 to the fifth anniversary date, and secondly, that a participant normally remains in employment with the Marconi Group until the third anniversary date or, if later, at the time that the first condition is met;

b to 5,204 employees in respect of 4,824,492 ordinary shares of 5 pence each at a subscription price of £7.035 per share under five year savings contracts and to 3,267 employees in respect of 1,631,768 ordinary shares of 5 pence each at a subscription price of £7.475 per share under three year savings contracts under the Marconi UK Sharesave Plan; and

c to 110 employees in respect of 1,554,603 ordinary shares of 5 pence each at subscription prices ranging from £8.07 to £10.085 per share under the Marconi 1999 Stock Option Plan.

Details of the options outstanding at 31 March 2000, and details of shares allotted pursuant to the exercise of options during the period ended 31 March 2000, are given in Notes 9 and 19 to the Accounts.

Energy, Environment and Health & Safety

Marconi is a world class business and expects to maintain high standards in its energy, environment and health and safety policies and practices throughout its global operations. The Group aims to minimise the impact of its operations and products on the environment and to provide a safe and healthy workplace for all its employees and visitors.

Marconi seeks to comply with all relevant laws and regulations and to anticipate future legislation by embracing best practice today. Management systems are being implemented which are appropriate for a high technology company with a number of separate distinct businesses operating in many different countries. For energy and the environment, each business is working towards achieving ISO 14001 globally.

Directors' Report

continued

Marconi's energy procurement continues to optimise the benefits available from UK deregulated markets, where significant cost saving have been achieved without compromising environmental performance.

A key objective is to design and manufacture products to high environmental standards thereby minimising the depletion of natural resources and energy and enabling those products to be recycled at the end of their useful life. Whilst actively supporting material recycling, ensuring continuous reductions in waste sent to landfill, Marconi is a pioneer in the use of new materials – such as lead free solders.

Charitable Donations

Charitable donations in the United Kingdom amounted to £269,000 excluding operating units' support for charitable purposes and for educational establishments.

Year 2000

The Group completed its preparations for the potential impacts of the Year 2000 date change on software and computing systems as expected. During the date change period a central co-ordination centre monitored Year 2000 related incidents across the world to provide early warning of potential problems, to provide executive management with reports on operational status across the Group and to resolve any problems.

In the event there were only a very small number of minor incidents that were dealt with using the operating and contingency plans developed during the Year 2000 programme. There was no material disruption to Marconi's business.

Business at the Annual General Meeting

The Annual General Meeting will take place on 25 July 2000. Details relating to the business to be put to shareholders at the Annual General Meeting can be found in the letter from the Chairman, to shareholders which incorporates the Notice of Meeting, which accompanies this Annual Report and Accounts.

By Order of the Board
Marconi plc

N C Porter
Secretary
One Bruton Street, London W1X 8AQ
18 May 2000

Report to Shareholders by the Board on Directors' Remuneration

Membership and Framework

The Remuneration Committee consists of wholly independent non-executive Directors. During the period 4 October 1999 (the date on which Directors were first appointed to the Committee prior to the listing of the Company on 30 November 1999) to 31 March 2000, the members of the Committee were:

Sir Christopher Harding *Chairman, until 13 December 1999*
Sir Alan Rudge *Chairman, from 1 February 2000*
W M Castell
The Rt Hon The Baroness Dunn
Hon Raymond G H Seitz
N J Stapleton

The Committee meets at least twice a year and makes decisions on behalf of the Board on the contracts of service and the remuneration packages of the Chairman and executive Directors. The Committee also determines the framework within which executive remuneration is more generally determined and in its review of executive Directors' pay takes account of the remuneration of the other members of the Executive Committee. The Committee has access to and takes professional advice from inside and outside Marconi. The Committee also takes the advice of the Chairman and Chief Executive, as appropriate, on the performance of the executive Directors. The fees of non-executive Directors are reviewed and determined by the Board.

Remuneration Policy

As a result of the significant changes to the Group over the past year, the Committee has reviewed employment and remuneration policies and their relevance to a global, high technology business. With fewer than one-third of the Company's employees now based in the UK, the Committee is conscious of the need to be familiar with market practice in those countries in which it operates.
The Committee's principles, however, remain the same, namely:

- To ensure that executive remuneration policy and practices support business strategy, are competitive but also cost effective
- Remuneration packages must be tailored to attract, motivate and retain senior executives with the right skills and in accordance with their contribution and performance
- To align executives' interests with those of shareholders through the establishment of competitive short and long term incentive plans
- To ensure that remuneration packages are transparent and clearly explained

Elements of Remuneration

Basic salary

Basic salaries for executive Directors are reviewed by the Remuneration Committee usually annually taking into account individual performance, skills and market competitiveness. Basic salary is the only element of remuneration which is pensionable. The Committee reviews data from both internal and external advisers and includes among its comparators large, global FTSE companies. It also assesses data derived from US high technology companies when looking at other senior roles particularly in relation to the other members of the Executive Committee. Account is also taken of pay decisions across the Marconi Group. Performance assessment of executive Directors includes the performance of the Group and the achievement of individual objectives. Basic salaries for executive Directors were increased by 4 per cent during the year under review, except in the case of those executives promoted to the Board.

Short term incentive bonus

Executive Directors are eligible to participate in a short term incentive plan. The plan pays bonuses only when an economic value added target (based on profitable growth) is met. The payment for 'on-target' performance is 25 per cent of basic salary for executive Directors and is subject to a maximum payment in any single year of 50 per cent. Any incentive earned beyond this level, capped at 100 per cent of basic salary, is carried forward and paid in two equal instalments but only to the extent that the economic value added target is achieved in future years.
In considering the payment of short term incentive bonuses, the Committee also takes account of personal performance. During the year, bonuses were paid at the rate of 50 per cent; no amounts were carried forward.

Longer term incentives

At a meeting held on 3 November 1999, shareholders approved the introduction of a number of share plans following the reconstruction of GEC and the listing of Marconi on 30 November 1999. Two main discretionary plans were approved – the Marconi 1999 Stock Option Plan and the Marconi Long Term Incentive Plan – and the executive Directors participate in both plans. In addition, shareholders approved the introduction of the Marconi UK Sharesave Plan and the Marconi Launch Share Plan in which the executive Directors and all eligible employees may participate. Full details of options granted to executive Directors under these plans are set out below.

In summary, options may be granted under the Marconi 1999 Stock Option Plan for a period of up to ten years from 30 November 1999. Options granted under the plan will become exercisable three years from the date of grant, provided the performance condition has been met, that is the percentage increase in Marconi's earnings per share must be equal to or greater than the percentage increase in the Retail Prices Index plus 3 per cent per annum. Thus, the shortest period over which the performance target can be satisfied is three financial years from the date of grant; if the target is not satisfied after this period, it can be retested over the four financial years from the date of grant, and so on.

Under the Long Term Incentive Plan, each year executive Directors can receive an award of up to a maximum of 50 per cent of basic salary, subject to satisfaction of demanding corporate performance over the three years from the date of award. After three years from the date of award, provided Marconi's total shareholder return is in the top 50 of the FTSE 100 index, participants may be granted a nil cost option to acquire Marconi shares. To the extent that the awards vest, the nil cost options will normally be exercisable in three tranches, one-third immediately upon vesting, one-third on the first anniversary and one-third on the second anniversary of the date of grant. On 30 November 1999, executive Directors participated in the plan for the first time; their nil cost options under the plan will vest in two annual tranches from July 2002; the shorter performance period and the accelerated vesting of the tranches reflect the fact that the grant of these awards was delayed by reason of the transaction with BAe. The conditional awards of notional shares made to executive Directors on 30 November 1999 were: Lord Simpson – 42,170; Mr J C Mayo – 32,439; and Mr R I Meakin – 17,841. At their date of appointment, 1 January 2000, and at 31 March 2000, Mr M J Donovan and Mr M W J Parton held conditional awards of notional shares of 55,390 and 72,208 respectively. No other awards under the plan are held by executive Directors.

Retirement Benefits

All executive Directors are members of the Group's pension scheme, the G.E.C. 1972 Plan. Members contribute at the rate of 3 per cent of salary and employer contributions made during the year ended 31 March 2000 amounted to 6.6 per cent of salary (1999 6.6 per cent).

Funded unapproved retirement benefit schemes (FURBS) are operated for the five executive Directors – Mr M J Donovan, Mr J C Mayo, Mr R I Meakin, Mr M W J Parton and Lord Simpson. Contributions to each of the FURBS are made on the advice of the actuary; such contributions are calculated to produce a capital sum targeted to provide benefits at the normal retirement age equivalent to a two-thirds pension. The targeted benefit takes into account the capital value of any relevant benefit in payment or otherwise arising from previous employments together with the capital value of benefits arising from membership of the G.E.C. 1972 Plan. Lord Simpson's normal retirement age is 60 (62 for the other four executive Directors) and his pensionable salary is restricted to £540,800 but subject to increase at the same percentage amount (if any) as the annual rate of increase in basic salary – with a maximum increase of 4 per cent per annum. In the event of cessation of employment before normal retirement age, or at retirement age, each of the Directors is entitled to the cash amount held in the FURBS established for him.

In accordance with the requirements of the Listing Rules, the disclosures required for the year ended 31 March 2000 are set out below. The figures for pension contributions shown on page 43 are the contributions paid by the Company in respect of each executive Director.

The pension benefits earned by the Directors under the G.E.C. 1972 Plan are as follows:

	Length of pensionable service (years)	Increase in accrued pension during the year £000	Cost of pension benefits accrued during the year net of member's contributions £000	Accumulated total accrued pension at 31 March 2000 £000
M J Donovan	1	1	2	2
J C Mayo	2	1	2	4
R I Meakin	3	1	11	5
M W J Parton	9	1	1	14
Lord Simpson	3	1	10	5

Notes

1 The pension entitlement shown is that which would be paid annually at normal retirement age based on service to 31 March 2000.

2 The increase in accrued pension during the year excludes any increase for inflation.

3 The cost of pension benefits accrued during the year net of member's contributions has been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11. The cost of pension benefits accrued during the year net of member's contributions is a measure of the capital cost of providing future pension payments and accordingly is a liability of the Group's pension arrangements and not a sum paid or due to the Directors of the Company.

4 Members of the scheme have the option to make contributions to the Selected Benefit Scheme (an AVC scheme); neither the contributions nor the resulting benefits are included in the above table.

5 During the year, the Company made the following payments to the Trustee of the FURBS in respect of individual Directors: Lord Simpson £308,000 (1999 £152,825), Mr J C Mayo £222,300 (1999 £183,000), and Mr R I Meakin £205,320 (1999 £150,578). Mr M J Donovan and Mr M W J Parton became Directors during the year. Contributions of £13,212 and £35,625 were paid into their FURBS respectively, in respect of the period during which they were Directors of the Company, in line with their employment contracts in force prior to becoming Directors. The contributions are determined each year based on actuarial advice to be sufficient to meet the obligations. Periodically the contributions are reviewed by the actuary.

6 In the event of death in service, a lump sum of four times pensionable salary, plus additional benefits for a surviving spouse and/or children, inclusive of any death benefits arising from the G.E.C. 1972 Plan, will be held on trust for the benefit of dependants of each of Mr M J Donovan, Mr J C Mayo, Mr R I Meakin, Mr M W J Parton and Lord Simpson.

Directors' Remuneration

The remuneration paid or payable by Group companies to the Directors of the Company were:

	Salary and Fees £000	Other benefits £000	Bonus £000	Excluding pension contributions 2000 Total £000	1999 Total £000	Pension contributions 2000 Total £000	1999 Total £000	Gains made on the exercise of share options 2000 Total £000	1999 Total £000
Sir Roger Hurn	250	16	–	**266**	89	**–**	–	**–**	–
Lord Simpson	669	221	338	**1,228**	1,085	**352**	182	**–**	–
M J Donovan	87	14	44	**145**	–	**21**	–	**–**	–
J C Mayo	515	167	260	**942**	877	**259**	212	**–**	–
R I Meakin	283	153	143	**579**	489	**226**	167	**–**	–
M W J Parton	94	28	87	**209**	–	**42**	–	**–**	–
W M Castell	25	–	–	**25**	25	**–**	–	**–**	–
The Rt Hon The Baroness Dunn	25	–	–	**25**	25	**–**	–	**–**	–
Sir Christopher Harding	22	–	–	**22**	30	**–**	–	**–**	–
Sir Alan Rudge	26	–	–	**26**	25	**–**	–	**–**	–
Hon Raymond G H Seitz	25	–	–	**25**	25	**–**	–	**–**	–
N J Stapleton	28	–	–	**28**	25	**–**	–	**–**	–
	2,049	599	872	**3,520**	2,695	**900**	561	**–**	–

Notes

1 The remuneration shown in the table above, with the exception of Mr M J Donovan and Mr M W J Parton, is for the full years 2000 and 1999. The remuneration presented for Mr Donovan and Mr Parton is from 1 January 2000, the date on which they were appointed Directors of the Company.

2 Executive Directors receive certain taxable benefits, including an allowance under the company car scheme.

3 Other benefits include the payment of a non-pensionable earnings supplement in relation to the FURBS.

4 The fees of non-executive Directors are determined by the Board; the basic fee paid during the year was £25,000 per annum with a further £5,000 per annum paid to the Chairmen of the Audit Committee and the Remuneration Committee. With effect from 1 April 2000, the basic fee was increased to £33,000 with a further £7,000 per annum paid to the Chairmen of the Audit Committee and the Remuneration Committee.

5 Non-executive Directors do not have service contracts and do not participate in any of the incentive arrangements open to executive Directors or the Group's pension scheme.

6 All Directors are reimbursed all necessary and reasonable expenses incurred in the performance of their duties.

7 No remuneration was paid to Mr D H Reid and Mr N C Porter in their capacity as initial Directors of the Company.

Report to Shareholders by the Board on Directors' Remuneration
continued

Directors' Interests

The Directors' interests as defined by the Companies Act 1985 (which include trustee holdings and family interests incorporating holdings of infant children) in shares of the Company and its subsidiaries are as follows:

Ordinary shares

	As at 31 March 2000* Beneficial	As at 1 April 1999† (or subsequently on appointment) Beneficial
W M Castell	**10,000**	10,000
The Rt Hon The Baroness Dunn	**10,000**	10,000
M J Donovan	**23,232**	23,232
Sir Roger Hurn	**11,450**	11,450
J C Mayo	**164,388**	164,340
R I Meakin	**11,050**	10,025
M W J Parton	**28,776**	28,750
Sir Alan Rudge	**10,000**	10,000
Hon Raymond G H Seitz	**11,027**	11,006
Lord Simpson	**106,606**	74,493
N J Stapleton	**13,572**	11,500

†Interests in ordinary shares of GEC
*Interests in ordinary shares of Marconi plc

Notes

1 None of the Directors held any non-beneficial interests in the shares of GEC or the Company during the year.

2 There have been no other changes in the interests of Directors between 31 March 2000 and 18 May 2000.

3 On the date of incorporation, 17 September 1999, and on 4 October 1999, the date on which certain of the Directors were appointed, none of the present Directors held any interest in the share capital of the Company.

4 In accordance with the terms of the reconstruction of GEC, ordinary shares of 5 pence each were issued by the Company, credited as fully paid to the former holders of GEC ordinary shares of 5 pence each on the register at the close of business on 26 November 1999, on the basis of one ordinary share of 5 pence each in the Company for one ordinary share of 5 pence each in GEC.

5 The following table shows the interests of Directors in options over ordinary shares of 5 pence each in GEC under the GEC Share Option Schemes for the period 1 April 1999 to 28 November 1999, and, subsequently, over ordinary shares of 5 pence each in the Company under the Marconi 1999 Stock Option Plan and the Marconi UK Sharesave Plan for the period 29 November 1999 to 31 March 2000:

	At 1 April 1999 and 28 November 1999		At 29 November 1999 (or subsequently on appointment)		Granted during the period		Exercised during the period		At 31 March 2000		Exercisable	
	No.	Average exercise price pence	No.	Average exercise price pence	No.	Exercise price pence	No.	Average market price pence	No.	Average exercise price pence	From	To
M J Donovan	–	–	266,271	338	–	–	–	–	266,271	338	Nov 1999	Nov 2009
	–	–	335,681	844*	–	–	–	–	335,681	844*	Nov 2002	Nov 2009
J C Mayo	1,167,960	423	1,442,791	342	1,442,791	801.5*	–	–	1,442,791	342	Dec 2000	Nov 2009
	–	–	–	–	–	–	–	–	1,442,791	801.5*	Nov 2002	Nov 2009
R I Meakin	258,255	423	319,024	343	1,295	747.5	–	–	320,319	344	Dec 2000	Nov 2009
	–	–	–	–	319,024	801.5*	–	–	530,976	853*	Nov 2002	Jan 2010
	–	–	–	–	211,952	931.5*	–	–	–	–	–	–
M W J Parton	–	–	692,857	388	–	–	–	–	692,857	388	Nov 1999	Nov 2009
	–	–	684,360	801.5*	–	–	–	–	684,360	801.5*	Nov 2002	Nov 2009
Lord Simpson	–	–	1,405,864	311	1,295	747.5	–	–	1,407,159	311	Dec 2000	Nov 2009
	–	–	–	–	1,543,408	801.5*	–	–	1,543,408	801.5*	Nov 2002	Nov 2009

*Exercise price exceeds market price as at 31 March 2000.

Notes

1 On 30 November 1999, each of the executive Directors was granted the right to receive 1,000 Marconi shares at nil cost under the Marconi Launch Share Plan.

2 The mid-market price of a Marconi share as at 31 March 2000 was 749 pence with a range for the period 30 November 1999 (the first day of dealings in the Company's shares) to 31 March 2000 of 749 pence to 1095.5 pence.

3 The executive Directors, along with those employees remaining in the Marconi Group, were given the opportunity to exchange their GEC options for Marconi options on a value-for-value basis and all of the executive Directors elected to exchange their options.

4 The terms of Lord Simpson's service contract with GEC made certain provisions for awards of shares to be made to him under the rules of the GEC Employee Share Plan and the grant of a notional option. Upon the reconstruction of GEC, the service contracts of the executive Directors were reviewed and the Committee decided, taking account of the restriction with regard to Lord Simpson's notional option,

to more closely align his incentive arrangements with those of the other executive Directors. In exchange for the GEC share award and notional option held by Lord Simpson each over 625,000 GEC shares at £3.84 per share, Lord Simpson received, subject to a limitation agreed by the Committee in respect of the notional option, options over Marconi shares, details of which are set out in the table above.

5 Although options granted by GEC became exercisable immediately prior to the listing of Marconi, no options were exercised by any of the Directors. Mr J C Mayo, Mr R I Meakin and Lord Simpson each undertook not to exercise their options within a period of one year from the date of listing. Accordingly, no options were exercised during the period and no gains made. A summary and full details of Directors' shareholdings and options are contained in the Company's Register of Directors' Interests.

Personal Shareholding Policy

The Company operates a personal shareholding policy in order to assist further in aligning the interests of executives and shareholders. The policy requires executive Directors to build up, over a period of time, a target shareholding of Marconi shares with a market value equal to three times annual basic salary.

Marconi UK Sharesave Plan

The Company operates an Inland Revenue approved share option scheme, the Marconi UK Sharesave Plan, which is open to all UK employees, including executive Directors.

Marconi Launch Share Plan

On 30 November 1999, employees, including executive Directors, were granted the right to receive up to 1,000 Marconi shares at nil cost, provided that two conditions are met. Firstly, that the market value of a Marconi share doubles to £16.03 during the period 30 November 1999 to the fifth anniversary date, and secondly, that a participant normally remains in employment with the Marconi Group until the third anniversary date or, if later, at the time that the first condition is met.

Policy on the Grant of Options

The Company's policy on the granting of options is to make phased awards to key employees, based on business and personal performance. The value of awards normally ranges from 50 per cent to 150 per cent of basic salary per annum. Long Term Incentive Plan awards may also be made to senior employees based on personal performance. The maximum value of an award is 50 per cent of basic salary per annum.

Attracting and retaining highly skilled employees is key to Marconi's success. The rapid pace of change in the industries in which Marconi operates and the fierce competition for scarce highly skilled people in a global labour market where demand exceeds supply means that the Group has to compete vigorously with its competitors for the available skilled people.

The Committee is aware that the Company's current approach to share option grants is not sufficiently competitive compared to that provided by its US competitors who currently dominate the industries in which the Group operates. The Committee has decided to undertake a detailed review of the Company's approach to the granting of share options, particularly in the US where more than 40 per cent of the Group's turnover and profit are achieved.

Service Contracts

Each of the executive Directors has a service contract with Marconi Corporation plc (formerly GEC) subject to termination by either party giving not less than one year's notice or, if not already terminated, on Lord Simpson reaching the age of 60 years and the remaining executive Directors on reaching the age of 62 years. It is intended that each of the executive Directors will, in due course, enter into service contracts with the Company in substantially the same form as their existing service contracts, which will in such circumstances be revoked. None of the Directors offering themselves for re-election at the forthcoming Annual General Meeting has a service contract with the Company or any of its subsidiaries with a notice period of more than one year.

When considering compensation payable in respect of termination of service contracts of executive Directors, the Committee would pay due regard to the need for mitigation.

Non-executive Directors serve for a period of three years, subject to renewal by agreement with the Board.

External Appointments

With the approval of the Chairman of the Company, executive Directors are permitted to hold appointments outside the Company. Any fees payable in connection with such appointments are retained by Directors unless otherwise agreed.

In preparing this report, the Remuneration Committee has given full consideration to the provisions set out in Schedule B to the Combined Code.

On behalf of the Board of
Marconi plc

Sir Alan Rudge
Chairman of the Remuneration Committee
18 May 2000

Directors' Statement on Internal Financial Control

The Directors have overall responsibility for Marconi's system of internal financial control which aims to safeguard the Group's assets and to ensure that proper accounting records have been maintained and that financial information is reliable. Any system of internal control can only provide reasonable, but not absolute, assurance against material misstatement or loss.

The framework of key financial controls is as follows:

- A management structure with clearly defined levels of delegated authority gives major decision-making responsibility to the divisional managing directors, who are accountable for the conduct and performance of their businesses within agreed business strategy.
- The divisional managing directors are responsible for completing Letters of Assurance which certify that they are not aware of any weaknesses in internal controls which have resulted in the risk of material loss.
- All controlled business groups have cascaded this risk control reporting system throughout their operations to ensure unit level responsibility and maximum transparency of any issues to the divisional managing directors and the Marconi Directors.

The Group's overall strategy is reviewed regularly by the Directors. Executive Directors agree a strategic plan, a comprehensive phased budget and a set of objectives with the management of each division on an annual basis. The Directors approve the agreed Group budget.

Actual results, using the same policies adopted in the annual accounts, are reported monthly and variances against budget and last year are prepared for executive review. Forecasts are updated monthly. Quarterly performance reviews are held with each sector management team. Group results are prepared monthly and reviewed by the Directors at their regular meetings.

Central review and approval procedures operate in major risk areas such as acquisitions and disposals, capital expenditure, contract tenders, litigation, industrial relations, treasury management, taxation and environmental issues.

The external auditors report on any weaknesses in internal financial control identified during their audit. These reports, and the management replies, giving details of remedial actions taken, are reviewed by the Audit Committee.

Marconi's out-sourced Internal Audit function reviews and monitors the Group's internal control processes. Internal Audit co-ordinates its work with external audit and reports regularly to the executive Directors and periodically to the Audit Committee.

The Group's investments in joint ventures, associated companies and major investments are safeguarded by regular attendance of Marconi representatives at meetings of Directors, regular discussions with management and consultation on material corporate transactions.

The Board has reviewed the effectiveness of the Group's internal financial control system. This review included consideration of both the reports of the external and internal auditors and the Letters of Assurance provided by the managing directors of each division and of the budgeting and monthly reporting process.

The Directors have adopted the transitional approach in reporting on internal controls by restricting their statement to internal financial controls. The statement on Corporate Governance on page 37 covers progress on the implementation of the Turnbull guidance.

Directors' Responsibilities for the Financial Statements

The Directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and of the Group as at the end of the financial year and of the profit or loss of the Group for that period.

The Directors consider that the financial statements on pages 48 to 77, have been prepared on a going concern basis, appropriate accounting policies have been used and applied consistently, reasonable and prudent judgements and estimates have been made and applicable accounting standards have been followed.

The Directors are responsible for ensuring that the Company keeps accounting records which disclose with reasonable accuracy the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 1985.

The Directors have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and the Group and to prevent and detect fraud and other irregularities.

After reviewing the Group's budget and projected cash flows and taking into account the Group's net monetary debt balances at 31 March 2000, the Directors consider that the Company and the Group have adequate resources to continue as a going concern for the foreseeable future and accordingly adopt that basis in preparing the accounts.

Auditors' Report

To the members of Marconi plc

We have audited the financial statements on pages 48 to 77 which have been prepared under the accounting policies set out on pages 48 and 49.

Respective responsibilities of Directors and auditors

The Directors are responsible for preparing the Annual Report, including as described on page 46 preparation of the financial statements, which are required to be prepared in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established by statute, the Auditing Practices Board, the UK Listing Authority and by our profession's ethical guidance.

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

We review whether the corporate governance statement on page 37 reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the UK Listing Authority and we report if it does not. We are not required to consider whether the Board's statement of internal control covers all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risks and control procedures.

We read the other information contained in the Annual Report, including the corporate governance statement, and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

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

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

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 March 2000 and of the profit of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche
Chartered Accountants and Registered Auditors
Hill House
1 Little New Street
London EC4A 3TR
18 May 2000

Accounting Policies

The financial statements have been prepared in accordance with applicable accounting standards.

The more important Marconi Group accounting policies are summarised below to facilitate the interpretation of the financial statements.

Accounting convention

The financial statements are prepared under the historical cost convention, as modified by the valuation of listed fixed asset investments.

Basis of consolidation

The financial statements consolidate the accounts of Marconi plc and all of its subsidiary undertakings (Group companies or subsidiaries). All accounts are made up to 31 March.

Basis of preparation

Marconi plc was incorporated on 17 September 1999. Its ordinary shares were listed on the London Stock Exchange on 30 November 1999 having become the new ultimate parent company of the remaining businesses of Marconi Corporation plc (formerly The General Electric Company, p.l.c. (GEC)) following the separation of the MES Business, GEC's international aerospace, naval shipbuilding, defence electronics and defence systems business, and the subsequent merger of the MES Business with British Aerospace Plc. Prior to 29 November 1999, Marconi plc had not made any profits or losses.

To provide information which is meaningful to the shareholders of Marconi plc, the Directors believe it is necessary to prepare the accounts excluding the separated business, that is on the basis that the separation of the MES Business had taken effect prior to 1 April 1998. The Directors believe that this information reflects the ongoing operations of the Marconi Group more clearly. Marconi plc's combination with the remaining businesses of GEC has been accounted for as a merger and, in the accounts, is presented as if Marconi plc had been the parent of the remaining businesses for each year presented. The accounts have been presented as if GEC's investment in the MES Business had been distributed by way of a dividend in specie prior to 1 April 1998 and reflects amounts recorded in the accounts of the companies remaining after the separation.

Where an investment was made by the GEC Group in a company in the MES Business in the prior year, on separation it is treated as a distribution in the prior year and shown as part of exceptional items, merger/demerger receipts and (costs) in the profit and loss account.

The interest, tax and management charges reflect the overall historical corporate structure of GEC and these are not necessarily indicative of those which the Marconi Group would have incurred had the MES Business been separated prior to 1 April 1998. The accounts include dividends from the MES Business, shown as part of exceptional items, merger/demerger receipts and (costs) in the profit and loss account.

As Marconi plc was incorporated on 17 September 1999, the Company balance sheet is presented at 31 March 2000 only and therefore no comparatives are presented.

The Marconi Group profit and loss account for the period from 17 September 1999 to 31 March 2000 is presented in note 27 in order to comply with Section 227 of the Companies Act 1985. This statutory information consolidates the continuing Marconi subsidiaries for this period only.

Turnover

Turnover, excluding VAT, comprises sales to outside customers, and the Group's percentage interest in sales of joint ventures. The Group records transactions as sales when the delivery of products or performance of services takes place in accordance with the terms of sale.

Currency translation

Profits and losses of overseas subsidiaries, joint ventures and associates and cash flows of overseas subsidiaries are translated at the average rates of exchange during the year. Non-sterling net assets are translated at year-end rates of exchange. Key rates used are as follows:

	Average rates		Year-end rates	
	2000	1999	**2000**	1999
US Dollar	**1.62**	1.66	**1.60**	1.61
Italian Lira	**3,015**	2,861	**3,228**	2,895
Euro	**1.56**	1.47	**1.67**	1.50

Reserves are adjusted to include the differences arising from the restatement to year-end rates of exchange of profits and losses and the translation of the net assets of overseas subsidiaries, joint ventures and associates at the beginning of the year. All other exchange gains and losses are included in profit on ordinary activities before taxation.

Financial instruments

The Group uses financial instruments, including interest rate and currency swaps, solely for the purpose of raising finance for its operations and to manage interest and currency risks associated with the Group's underlying business activities. There is no trading activity in financial instruments.

Foreign exchange transaction exposures

The Group hedges actual foreign exchange exposure as soon as there is a firm contractual commitment. Forward contracts are used to hedge the exposure. Amounts are included in the accounts at the forward exchange contract rate. If the contract ceases to be a hedge any subsequent gains or losses are recognised through the profit and loss account.

Balance sheet translation exposures

A large proportion of the Group's net assets are denominated in overseas currencies. Where appropriate, the Group hedges these balance sheet translation exposures by borrowing in relevant currencies and markets, and by the use of currency swaps. Currency swaps are used only as balance sheet hedging instruments, and the Group does not hedge the currency translation of its profit and loss account. Exchange gains or losses arising on the hedging borrowings and on the notional principal of currency swaps during their life and at termination or maturity are dealt with as a movement in reserves.

Interest rate risk exposure

The Group hedges its exposure to movements in interest rates associated with its borrowing primarily by means of interest rate swaps and forward rate agreements.

Tangible fixed assets

Property, plant, machinery, fixtures, fittings, tools and equipment are recorded at cost and depreciated on a straight line basis over their estimated useful lives. Freehold land does not bear depreciation where the original cost of purchase was separately identified.

Tangible fixed assets are depreciated using the following rates:

Freehold buildings	– 2 per cent to 4 per cent per annum
Leasehold property	– over the period of the lease or 50 years for long leases
Plant and machinery	– 10 per cent per annum on average
Fixtures, fittings, tools and equipment	– 10 per cent per annum

Leased assets

Assets held under finance leases are included in tangible fixed assets and the present values of lease commitments are included under creditors. Operating lease payments are charged to the profit and loss account as incurred.

Goodwill

Purchased goodwill is capitalised and amortised on a straight line basis over its estimated useful economic life. Each acquisition is separately evaluated for the purposes of determining the useful economic life, up to a maximum of 20 years. The useful economic lives are reviewed annually and revised if necessary.

Research and development

Expenditure incurred in the year is charged against profit unless specifically chargeable to and receivable from customers under agreed contract terms.

Stocks and contracts in progress

Stocks and contracts in progress are valued at the lower of cost, including appropriate overheads, and estimated net realisable value. Provisions are made for any losses incurred or expected to be incurred on uncompleted contracts. Profit on long term contracts in progress is taken when a sale is recorded on part-delivery of products or part-performance of services, provided that the outcome of the contract can be assessed with reasonable certainty. Advance payments received from customers are shown as creditors unless there is a right of set-off against the value of work undertaken. Progress payments received are deducted from the value of the work carried out, any excess being included with payments received in advance.

Taxation

Taxation on profit on ordinary activities is that which has been paid or becomes payable in respect of the profits for the year. Deferred taxation is provided on all timing differences which are expected to reverse in the future without replacement at the rate of tax anticipated to apply in the year of assessment.

Investments

Joint ventures comprise long term investments where control is shared under a contractual arrangement. The sector analysis of turnover, profit and net assets includes the Group's share of the results and net assets of joint ventures.

Associates consist of long term investments in which the Group holds a participating interest of not less than 20 per cent and over which it exercises significant influence. Investments in joint ventures and associates are stated at the amount of the Group's share of net assets including goodwill at 31 March derived from audited or management accounts made up to that date. Profit before taxation includes the Group's share of joint ventures and associates.

Other unlisted fixed asset investments and the Company's investment in shares in Group companies are stated at cost less provision for impairment in value. Listed fixed asset investments are stated at market value. Current asset investments are stated at the lower of cost and net realisable value except dated listed securities which are stated at market value.

Pensions and other post retirement benefits

The expected cost of providing pensions and other post retirement benefits, as calculated periodically by independent actuaries, is charged to the profit and loss account so as to spread the cost over the expected average service lives of current employees.

Share options

In accordance with UITF abstract 17, Employee share schemes, the costs of awarding shares under employee share plans are charged to the profit and loss account over the period to which the performance criteria relate.

In the year ended 31 March 2000 certain costs relating to employee share plans have been charged to exceptional items, merger/demerger receipts and (costs). For further information, refer to note 4.

Consolidated Profit and Loss Account

For the year ended 31 March

	Note	2000 Continuing Operations £ million	2000 Acquisitions £ million	2000 £ million	1999 £ million
Turnover					
Group	3	**4,183**	**1,254**	**5,437**	3,789
Share of joint ventures		**287**	**–**	**287**	301
	1	**4,470**	**1,254**	**5,724**	4,090
Operating (loss)/profit					
Group operating profit/(loss)					
Excluding goodwill amortisation and exceptional items		**592**	**133**	**725**	483
Goodwill amortisation		**(151)**	**(612)**	**(763)**	(63)
Operating exceptionals	4a	**(84)**	**(22)**	**(106)**	(51)
	3	**357**	**(501)**	**(144)**	369
Share of joint ventures					
Excluding goodwill amortisation and exceptional items				**25**	25
Goodwill amortisation				**(2)**	(1)
Operating exceptionals	4a			**(1)**	(2)
				22	22
				(122)	391
Group and joint venture operating profit before goodwill amortisation and exceptional items				**750**	508
Share of associates				**7**	57
Operating (loss)/profit	1			**(115)**	448
Exceptional items, merger/demerger receipts and (costs)	4b			**737**	(306)
Exceptional items, gains less losses on disposals of subsidiaries and other fixed assets	4c			**4**	775
Income from loans, deposits and investments, less interest payable					
Group	5			**(107)**	42
Share of joint ventures and associates	5			**4**	17
				(103)	59
Profit on ordinary activities before taxation					
Excluding goodwill amortisation and exceptional items				**654**	640
Goodwill amortisation and exceptional items				**(131)**	336
	1			**523**	976
Tax credit/(charge) on profit on ordinary activities					
Excluding tax on goodwill amortisation and exceptional items				**(196)**	(238)
Tax on goodwill amortisation and exceptional items				**198**	(119)
	6			**2**	(357)
Profit on ordinary activities after taxation				**525**	619
Equity minority interests	7			**(3)**	(12)
Profit on ordinary activities attributable to the shareholders				**522**	607
Dividends	8			**(142)**	(348)
Retained profit for the financial year				**380**	259
Basic earnings per share	2			**19.4p**	22.4p
Diluted earnings per share	2			**19.1p**	22.2p
Earnings per share excluding goodwill amortisation and exceptional items	2			**16.9p**	14.4p

Balance Sheets

As at 31 March

	Note	Group 2000 £ million	Group 1999 £ million	Company 2000 £ million
Fixed Assets				
Goodwill	10	**4,397**	1,220	**–**
Tangible assets	11	**758**	470	**–**
Investments:	12			
Joint ventures				
Share of gross assets		**246**	285	
Share of gross liabilities		**(92)**	(86)	
		154	199	
Associates		**47**	29	
Other investments		**1,425**	995	
Shares in Group companies				**136**
		1,626	1,223	**136**
		6,781	2,913	**136**
Current Assets				
Stocks and contracts in progress	13	**946**	616	**–**
Debtors	14	**2,250**	1,432	**548**
Investments	15	**80**	125	**–**
Cash at bank and in hand	15	**544**	1,403	**–**
		3,820	3,576	**548**
Creditors: amounts falling due within one year	16	**(4,007)**	(2,596)	**(93)**
Net current (liabilities)/assets		**(187)**	980	**455**
Total assets less current liabilities		**6,594**	3,893	**591**
Creditors: amounts falling due after more than one year	16	**(1,078)**	(132)	**–**
Provisions for liabilities and charges	18	**(870)**	(337)	**–**
		4,646	3,424	**591**
Capital and reserves				
Called up share capital		**136**		**136**
Shares to be issued		**247**	–	**247**
Share premium account		**1**	–	**1**
Capital reserve		**375**	351	**–**
Revaluation reserve		**1,156**	847	**–**
Profit and loss account		**2,715**	2,215	**207**
Equity shareholders' interests	19	**4,630**	3,413	**591**
Equity minority interests		**16**	11	**–**
		4,646	3,424	**591**

These accounts were approved by the Board of Directors on 18 May 2000.

Signed on behalf of the Board of Directors.

Sir Roger Hurn
Lord Simpson } Directors

Cash Flow Statement

For the year ended 31 March

	Note	2000 £ million	1999 £ million
Net cash inflow from operating activities	20	**610**	434
Dividends from joint ventures and associates		**68**	426
Returns on investments and servicing of finance			
Income from loans, deposits and investments		**114**	103
Interest paid		**(148)**	(57)
Dividends paid to minority in subsidiaries		**–**	(26)
		(34)	20
Tax paid			
UK corporation tax paid		**(111)**	(242)
Overseas tax paid		**(3)**	(59)
		(114)	(301)
Capital expenditure and financial investment			
Purchases of tangible fixed assets		**(305)**	(176)
Purchases less sales of fixed asset investments		**(129)**	–
Sales of tangible fixed assets		**40**	9
		(394)	(167)
Acquisitions and disposals			
Investments in subsidiary companies	22	**(4,111)**	(956)
Net cash acquired with subsidiary companies		**137**	4
Sales of interests in subsidiary companies and associates	22	**–**	1,050
		(3,974)	98
Exceptional cash flows related to merger/demerger	20	**1,386**	(497)
Equity dividends paid to shareholders		**(397)**	(218)
Cash outflow before use of liquid resources and financing		**(2,849)**	(205)
Net cash inflow from management of liquid resources	20	**656**	81
Net cash flow from financing			
Purchases of ordinary shares		**–**	(310)
Issues of ordinary shares		**161**	27
Other	20	**1,687**	728
(Decrease)/increase in cash and net bank balances repayable on demand		**(345)**	321

Reconciliation of Net Cash Flow to Movement in Net Monetary (Debt)/Funds

For the year ended 31 March

	Note	2000 £ million	1999 £ million
(Decrease)/increase in cash and net bank balances repayable on demand		**(345)**	321
Net cash inflow from management of liquid resources		**(656)**	(81)
Net cash inflow from increase in debt and lease financing		**(1,803)**	(658)
Change in net monetary funds resulting from cash flows		**(2,804)**	(418)
Net debt acquired with subsidiaries		**(120)**	(9)
Effect of foreign exchange rate changes		**155**	16
Movement in net monetary funds in the period		**(2,769)**	(411)
Net monetary funds at 1 April	21	**624**	1,035
Net monetary (debt)/funds at 31 March	21	**(2,145)**	624

Statement of Total Recognised Gains and Losses

For the year ended 31 March

	2000 £ million	1999 £ million
Profit on ordinary activities attributable to the shareholders		
Group	**500**	538
Share of joint ventures	**18**	32
Share of associates	**4**	37
	522	607
Listed fixed asset investments		
Surplus due to movement in share price	**419**	851
Exchange rate adjustments	**(110)**	(4)
	309	847
Offset due to gains on hedging	**76**	–
	385	847
Exchange differences on translation		
Group	**48**	30
Share of joint ventures	**–**	2
Share of associates	**(4)**	(15)
	44	17
Total recognised gains and losses	**951**	1,471

Reconciliation of Movements in Shareholders' Funds

For the year ended 31 March

	2000 £ million	1999 £ million
Total recognised gains and losses	**951**	1,471
Dividends	**(142)**	(348)
Shares to be issued	**247**	–
Purchase of ordinary shares for cash	**–**	(310)
Issues of ordinary shares for cash	**161**	27
Total movement in the period	**1,217**	840
Shareholders' funds at 1 April	**3,413**	2,573
Shareholders' funds at 31 March	**4,630**	3,413

1 Principal activities, profit contributions, markets and net assets employed

Analysis of results and net assets by class of business

	Profit		Turnover		Net assets	
	2000 £ million	1999 £ million	**2000 £ million**	1999 £ million	**2000 £ million**	1999 £ million
Communications Networks	**416**	247	**2,535**	1,343	**807**	340
Communications Services	**73**	32	**543**	244	**33**	37
Mobile Communications	**26**	16	**295**	271	**123**	126
Systems	**184**	151	**1,633**	1,501	**442**	449
Capital	**75**	78	**711**	772	**202**	192
Other (including intra-activity sales)	**(24)**	(16)	**7**	(41)	**98**	109
	750	508	**5,724**	4,090	**1,705**	1,253
Goodwill	**(765)**	(64)			**4,417**	1,242
Operating exceptionals (note 4)	**(107)**	(53)				
	(122)	391			**6,122**	2,495
Alstom – before goodwill amortisation	**–**	58			**892**	943
– goodwill amortisation	**–**	(16)				
Other associates	**7**	15			**47**	29
	7	57				
Operating (loss)/profit	**(115)**	448				
Exceptional items, merger/demerger receipts and (costs)	**737**	(306)				
Exceptional items, gains less losses on disposal of subsidiaries and other fixed assets	**4**	775				
Interest bearing assets and liabilities including joint ventures and associates	**(103)**	59			**(1,595)**	740
Unallocated net liabilities					**(820)**	(783)
	523	976			**4,646**	3,424

Comparative figures have been restated to reflect the ongoing structure of the Group.
The Marconi share of joint ventures' profit, turnover and net assets are included under Capital.
Sales made by Group companies to joint ventures and associates amounted to £65 million (1999 £54 million). Purchases from joint ventures and associates amounted to £4 million (1999 £18 million).
The results and net assets from acquisitions principally affect Communications Networks.

1 Principal activities, profit contributions, markets and net assets employed continued

Analysis of turnover by class of business

	To customers in the United Kingdom 2000 £ million	1999 £ million	To customers overseas 2000 £ million	1999 £ million
Communications Networks	**755**	597	**1,780**	746
Communications Services	**240**	175	**303**	69
Mobile Communications	**18**	23	**277**	248
Systems	**46**	49	**1,587**	1,452
Capital	**433**	495	**278**	277
Other (including intra-activity sales)	**14**	(59)	**(7)**	18
	1,506	1,280	**4,218**	2,810

Analysis of turnover by territory of destination

	Turnover 2000 £ million	1999 £ million
United Kingdom	**1,506**	1,280
The Americas	**2,359**	1,280
Rest of Europe	**1,234**	968
Africa, Asia and Australasia	**625**	562
	5,724	4,090

Analysis of operating profit before goodwill amortisation and exceptional items, turnover and net assets by territory of origin

	Profit 2000 £ million	1999 £ million	Turnover 2000 £ million	1999 £ million	Net assets 2000 £ million	1999 £ million
United Kingdom	**378**	261	**1,993**	1,699	**551**	498
The Americas	**306**	157	**2,499**	1,268	**685**	364
Rest of Europe	**29**	51	**870**	797	**391**	317
Africa, Asia and Australasia	**37**	39	**362**	326	**78**	74
	750	508	**5,724**	4,090	**1,705**	1,253

2 Earnings per share

Earnings per share are calculated by reference to a weighted average of 2,696.9 million ordinary shares (1999 2,711.6 million) in issue during the year.

An adjusted basic earnings per share has been presented in order to highlight the underlying performance of the Group, and is calculated as set out in the table below.

Reconciliation of earnings per share excluding goodwill amortisation and exceptional items

	2000 Earnings £ million	2000 Earnings per share pence	1999 Earnings £ million	1999 Earnings per share pence
Earnings and basic earnings per share	**522**	**19.4**	607	22.4
Exceptional items (note 4)				
Operating exceptionals	**107**	**3.9**	53	2.0
Merger/demerger receipts and (costs)	**(737)**	**(27.3)**	306	11.3
Gains less losses on disposals of subsidiaries and other fixed assets	**(4)**	**(0.1)**	(775)	(28.6)
Taxation arising on exceptional items (note 6)	**(198)**	**(7.3)**	119	4.4
Goodwill amortisation	**765**	**28.3**	80	2.9
	455	**16.9**	390	14.4

Diluted earnings per share are calculated by reference to a weighted average of 2,737.4 million ordinary shares in issue during the year (1999 2,738.7 million ordinary shares). The increase is due to an equivalent 40.5 million shares (1999 27.1 million) which would be issued on the exercise of all share options and is calculated on earnings of £522 million (1999 £607 million).

3 Group operating profit

	Continuing operations £ million	Acquisitions £ million	**2000 £ million**	1999 £ million
Sales to customers outside the Group	4,183	1,254	**5,437**	3,789
Own work capitalised	3	–	**3**	6
Other operating income	51	4	**55**	36
	4,237	1,258	**5,495**	3,831
Increase/(decrease) in stocks of finished goods and work in progress	53	(1)	**52**	40
Raw materials and consumables	1,649	579	**2,228**	1,643
Staff costs (note 9)	1,097	276	**1,373**	983
Depreciation and amortisation	265	653	**918**	171
Cost of hire of plant	21	3	**24**	15
Other external and operating charges	794	248	**1,042**	609
Auditors' remuneration	1	1	**2**	1
	3,880	1,759	**5,639**	3,462
Operating profit/(loss) arising in the Group	357	(501)	**(144)**	369

Included in other external and operating charges are the following amounts for research and development expenditure:

	2000 £ million	1999 £ million
Communications Networks	**308**	156
Communications Services	**–**	–
Mobile Communications	**54**	39
Systems	**73**	50
Capital	**36**	42
	471	287

4 Exceptional items

a Operating exceptionals

	2000 £ million	1999 £ million
Restructuring and reorganisation costs		
Acquisitions		
Group	**20**	32
Other businesses		
Group	**43**	(3)
Joint ventures	**1**	2
Year 2000 costs		
Group	**43**	22
	107	53
Communications Networks	**39**	20
Communications Services	**2**	–
Mobile Communications	**6**	8
Systems	**36**	7
Capital	**17**	16
Other	**7**	2
	107	53
United Kingdom	**37**	36
The Americas	**29**	8
Rest of Europe	**35**	8
Africa, Asia and Australasia	**6**	1
	107	53

4 Exceptional items continued

b Merger / demerger receipts and (costs)

	2000 £ million	1999 £ million
Dividends and other cash receipts	**1,409**	392
Separation costs:		
Share option costs	**(633)**	–
Other	**(15)**	(50)
Rebranding costs	**(24)**	–
Costs of acquisition of a separated business	**–**	(648)
	737	(306)

The merger/demerger receipts and (costs) above comprise dividends and other cash received by Marconi from the defence businesses that were separated from GEC (at the time Marconi merged with the non-defence business), minus the cost of establishing the Marconi share option plans that were approved at the EGM in November 1999 and other related costs of launching the new Company.

Share options

Marconi has developed a range of employee share plans. Marconi's normal accounting practice is that the cost of awards to employees that take the form of shares or rights to shares is recognised as an operating expense over the period to which the employees' performance relates. A cost generally arises where the exercise price paid by the option holder is less than either the market value of the shares at the date of grant or the cost of Marconi satisfying the grant with existing shares, purchased either in the open market or through hedging arrangements.

The Marconi employee share plans launched on separation fall outside the normal circumstances and have been treated as exceptional items, merger/demerger receipts and (costs). The accounting treatment adopted for these plans reflects the nature of the awards which are directly connected with the separation of the MES Business since the awards, and associated costs, would not otherwise have arisen. The estimated cost of awards to employees under all plans is £643 million. A charge of £633 million is shown above and the remaining £10 million is shown in note 9c.

The basis of the accounting treatment adopted for the relevant plans is as follows:

Establishment of plans as part of the MES Business separation

Only employees of the Marconi Group (including those in acquisitions announced prior to the completion of the MES Transactions) were eligible to participate in the Marconi Launch Share Plan. This plan was designed as a one-off gift of up to 1,000 free shares for each employee to recognise the contribution the existing workforce had made and to enable them to share some of the benefits of the value created by the separation of the MES Business and the launch of Marconi plc. The entitlement to receive the shares is deferred for at least three years and is contingent on the Marconi share price doubling to £16.03. A charge of £319 million represents the market value at the date of grant of the Marconi ordinary shares which are expected to be issued under the Marconi Launch Share Plan together with the estimated payroll tax liability. The value of shares to be issued is shown in note 19b.

The grant of additional options (the matching grant) was a one-off event designed to encourage employees to remain with the Marconi Group when existing arrangements under the GEC 1997 Executive Scheme became exercisable early as a consequence of the MES Transactions. Optionholders could roll-over existing GEC options into new Marconi options on a value-for-value basis. The matching grant doubled the number of Marconi options granted to most participants who rolled over their GEC options into Marconi options or who rolled over their GEC phantom options into Marconi phantom options. The matching grant was made in direct response to the risk of employees crystallising their gains on share options and is not part of ongoing remuneration. The exercise price of options granted under the matching grant is the market value at the date of grant. In line with the commitment given to shareholders, Marconi will satisfy a proportion of the options under the matching grant by purchasing shares in the market. A charge of £221 million represents the estimated incremental cost to Marconi (net of the exercise price paid by the optionholders) of purchasing the shares in the market expected to be needed to satisfy these grants, together with the estimated payroll tax liability.

No share options were granted in the period when the BAe transaction was pending since Marconi plc did not exist and, with GEC being the listed holding company, new GEC share options would have given inappropriate rights to substitute options for BAe shares. Marconi was therefore unable to grant options and offered phantom options to employees in lieu of new grants under existing GEC option schemes. Following the launch of Marconi plc, these phantom options were, where possible, substituted with real options to acquire Marconi shares. In line with the commitment given to shareholders, substituted options will be satisfied by purchasing shares in the market. A charge of £93 million represents the estimate of the incremental cost Marconi has incurred as a result of an increase in the cost of purchasing shares in the market from the date the phantom options were granted to the date that hedging this risk in the market could commence.

Ongoing remuneration costs

An estimate of the total cost to Marconi (net of the exercise price to be paid by the optionholders and the incremental costs incurred) of purchasing the shares in the market expected to be needed to satisfy the phantom option grants is being recognised as an operating expense spread evenly over three years – the period after which the options normally become exercisable. For the year ended 31 March 2000, a charge of £10 million has been recognised.

4 Exceptional items continued

c Gains less losses on disposals of subsidiaries and other fixed assets

	2000 £ million	1999 £ million
Flotation of Alstom	–	944
Goodwill written off on disposal	–	(199)
	–	745
Other	4	30
	4	775

5 Income from loans, deposits and investments, less interest payable

	2000 £ million	1999 £ million
Income from fixed asset investments		
Listed investments	19	1
Unlisted investments	3	1
Income receivable from current asset investments and cash		
Loans and deposits	54	88
Other	31	7
	107	97
Interest payable		
Bank loans and overdrafts	(199)	(38)
Loan capital	(3)	(3)
Other	(8)	(10)
Syndicated loan fees	(4)	(4)
	(214)	(55)
	(107)	42
Share of net income receivable of joint ventures and associates	4	17
	(103)	59

6 Tax

a Tax (credit)/charge on profit on ordinary activities

	2000 £ million	1999 £ million
United Kingdom taxation		
Corporation tax 30% (1999 31%)	**147**	429
Double taxation relief	**(82)**	(193)
Deferred taxation 30% (1999 31%)	**(25)**	(9)
Taxation on franked investment income	**–**	8
Joint ventures and associates	**8**	3
	48	238
Overseas taxation		
Current	**30**	111
Deferred taxation	**(79)**	(1)
Joint ventures and associates	**3**	24
	(46)	134
Overprovision of prior years		
United Kingdom	**1**	(4)
Overseas	**(5)**	(11)
	(2)	357

The tax provided is low as the exceptional gains in respect of the separated business are not taxable in full. Conversely, amortisation of goodwill arising on acquisitions does not attract tax relief.

Included in the tax on profit are the following amounts relating to exceptional items:

	2000 £ million	1999 £ million
Operating exceptionals	**(25)**	(24)
Merger/demerger receipts and (costs)	**(175)**	8
Gains less losses on disposals of subsidiaries and other fixed assets	**2**	135
	(198)	111

Included in the £24 million overseas taxation charge for joint ventures and associates for the year ended 31 March 1999 is £20 million in respect of Alstom. There is no equivalent amount for the year ended 31 March 2000.

b Deferred taxation assets

	Group £ million	Company £ million
At 1 April 1999	40	–
Businesses acquired	14	–
Credited to profit and loss account	98	–
Exchange rate adjustment	(2)	–
At 31 March 2000	150	–

	Group		Company
	2000 £ million	1999 £ million	2000 £ million
Tax effect of timing differences on:			
Provisions and accruals for liabilities and charges	**153**	32	**–**
Accelerated capital allowances	**(3)**	8	**–**
	150	40	**–**

Deferred tax asset balances are shown in debtors (note 14).

No provision is made for any taxation that may arise if reserves of overseas subsidiaries were distributed as such distributions are not expected to occur in the foreseeable future.

7 Equity minority interests

Equity minority interests represent the share of the profits less losses on ordinary activities attributable to the interests of equity shareholders in subsidiaries which are not wholly owned by the Group.

8 Dividends

	2000 £ million	1999 £ million
Interim 1.8p per share (1999 4.2p)	**49**	112
Final 3.4p per share (1999 8.8p)	**93**	236
	142	348

The 1999 figures in the table represent the dividends paid under the GEC distribution policy, which is not comparable as Marconi only merged with the non-defence businesses of GEC.

9 Directors and employees

a Directors' remuneration

Details of Directors' remuneration specified for audit by the UK Listing Authority are given in the Report to Shareholders by the Board on Directors' Remuneration on pages 42 to 43.

b Average monthly number of employees by sector

	Number ('000) 2000	1999
Communications Networks	**20**	11
Communications Services	**5**	3
Mobile Communications	**3**	3
Systems	**11**	10
Capital	**9**	9
Other	**1**	1
Group employees	**49**	37
Share of joint venture employees	**4**	4
Group and share of joint venture employees	**53**	41

c Staff costs

	2000 £ million	1999 £ million
Wages and salaries	**1,206**	852
Social security costs	**141**	110
Other pension costs	**26**	21
	1,373	983
United Kingdom	**527**	466
The Americas	**546**	260
Rest of Europe	**228**	201
Africa, Asia and Australasia	**72**	56
	1,373	983

Included within staff costs of £1,373 million for the year ended 31 March 2000 are £10 million of costs related to ongoing remuneration costs regarding the phantom option scheme (note 4b).

d Share options

At 31 March 2000 options were still outstanding in respect of the Company's ordinary shares of 5 pence under the Company's option plans:

	Number of shares	Amount of shares £ million	Subscription price	Date normally exercisable
The Employee 1992 Savings-Related Share Option Scheme	12,101,120	0.6	179-273p	2000-2003
The Managers' 1984 Share Option Scheme	1,880,395	0.1	147-266p	2000-2004
The 1997 Executive Share Option Scheme	17,900,492	0.9	327-385p	2000-2008
The Marconi UK Sharesave Plan	6,456,260	0.3	703-748p	2003-2005
The Marconi Launch Share Plan	37,189,925	1.9	–	2002-2006
The Marconi 1999 Stock Option Plan	21,280,713	1.1	801-1009p	2002-2010
The Phantom Option Scheme	70,392,525	3.5	17-1009p	2000-2009

The Directors' interests as defined by the Companies Act 1985 (which includes trustee holdings and family interests incorporating holdings of infant children) in shares in the Company and its subsidiaries are set out in the Report to Shareholders by the Board on Directors' Remuneration on page 44.

10 Goodwill

	Cost £ million	Amortisation £ million	Net book value £ million
At 1 April 1999	1,632	(412)	1,220
Acquisitions (note 22(a))	3,928		3,928
Charged to profit and loss account		(763)	(763)
Exchange rate adjustment	13	(1)	12
	5,573	(1,176)	4,397

11 Tangible fixed assets

Group	Freehold property £ million	Leasehold property Long £ million	Leasehold property Short £ million	Plant and machinery £ million	Fixtures fittings tools and equipment £ million	Payments on account and assets under construction £ million	Total £ million
Cost at 1 April 1999	173	14	20	422	488	46	1,163
Exchange rate adjustment	(4)	–	–	(10)	(12)	2	(24)
Additions	16	4	7	115	127	36	305
Businesses acquired	25	5	11	115	20	7	183
Disposals	(7)	(4)	(1)	(72)	(66)	–	(150)
Cost at 31 March 2000	203	19	37	570	557	91	1,477
Depreciation at 1 April 1999	49	3	7	291	343	–	693
Exchange rate adjustment	(1)	–	–	(9)	(9)	–	(19)
Charged to profit and loss account	11	–	3	71	70	–	155
Disposals	(3)	–	(1)	(60)	(46)	–	(110)
Depreciation at 31 March 2000	56	3	9	293	358	–	719
Net book value at 31 March 2000	147	16	28	277	199	91	758
Net book value at 31 March 1999	124	11	13	131	145	46	470

The net book value of tangible fixed assets of the Group includes an amount of £4 million (1999 £5 million) in respect of assets held under finance leases, on which the depreciation charge for the period was £1 million (1999 £nil).

12 Fixed asset investments

a Joint ventures, associates and other

Group	Shares Cost less amounts written off £ million	Share of post acquisition reserves £ million	Other investments Loans £ million	Cost or valuation £ million	Provisions £ million	Total £ million
At 1 April 1999	145	82	1	997	(2)	1,223
Exchange rate adjustment	–	(4)	–	(110)	–	(114)
Additions	21	–	–	124	–	145
Disposals and repayments	–	(1)	–	(3)	–	(4)
Profits less losses retained	–	(43)	–	–	–	(43)
Surplus on valuation of listed investments	–	–	–	419	–	419
At 31 March 2000	166	34	1	1,427	(2)	1,626

The investment in joint ventures and associates includes capitalised goodwill of £20 million (1999 £22 million). The principal joint ventures and associates are shown on page 77.

Market values

Listed fixed asset investments are stated at market value, as follows:

	2000 £ million	1999 £ million
Alstom – listed overseas	**892**	943
Other investments – listed in the United Kingdom	**405**	–
Other investments – listed overseas	**115**	49

No provision has been made for taxation of £178 million (1999 £95 million) which could arise if these investments were realised at the values stated.

During the year ended 31 March 2000 Marconi acquired a 27 per cent stake in Atlantic Telecom Group PLC. After careful review of the Group's involvement in Atlantic Telecom Group PLC the Group does not believe that it exercises significant influence and, accordingly, has treated Atlantic Telecom Group PLC as a listed fixed asset investment from the date of acquisition.

Subsequent to the year end, Atlantic Telecom Group PLC made an offer to acquire First Telecom for £520 million through a new share issue. The effect of this transaction will be to dilute the Group's stake to below 20 per cent.

For the period from 1 April 1998 to its flotation on 25 June 1998 the results of Alstom reflect the Group's 50 per cent shareholding. From the date of flotation to 30 September 1998 the Group's shareholding was 24 per cent, and for the six months to 30 September 1998 it was included as an associate. After careful review of the Group's actual involvement in Alstom since 30 September 1998, the Group does not believe that it exercises significant influence and, accordingly, has treated Alstom as a listed fixed asset investment from that date.

At 18 May 2000 the market value of the investments shown above was, in aggregate, £1,361 million.

b Shares in Group companies

	Cost £ million
Acquired and at 31 March 2000	136

13 Stocks and contracts in progress

	Group **2000 £ million**	1999 £ million	Company **2000 £ million**
Raw materials and bought-out components	**292**	180	**–**
Work in progress	**201**	137	**–**
Payments on account	**(1)**	(15)	**–**
Long-term contract work in progress	**129**	204	**–**
Payments on account	**(19)**	(97)	**–**
Finished goods	**344**	207	**–**
	946	616	**–**

14 Debtors

	Group 2000 £ million	1999 £ million	Company 2000 £ million
Amounts falling due within one year			
Trade debtors	**1,610**	1,130	**–**
Amounts recoverable on contracts	**102**	74	**–**
Amounts owed by joint ventures and associates	**31**	37	**–**
Other debtors	**163**	62	**–**
Prepayments and accrued income	**91**	65	**–**
Amounts owed by Group undertakings	**–**	–	**548**
	1,997	1,368	**548**
Amounts falling due after more than one year			
Trade debtors	**20**	19	**–**
Amounts recoverable on contracts	**1**	1	**–**
Other debtors	**66**	–	**–**
Prepayments and accrued income	**16**	4	**–**
Deferred taxation (note 6)	**150**	40	**–**
	2,250	1,432	**548**

15 Current asset investments and cash at bank and in hand

	Group 2000 £ million	1999 £ million	Company 2000 £ million
Dated securities at market value			
Listed securities – cost £68 million (1999 £106 million)	**69**	110	**–**
Other securities	**–**	5	**–**
Other investments at lower of cost and market value listed in the United Kingdom			
Market value £11 million (1999 £10 million)	**11**	10	**–**
Investments	**80**	125	**–**
Cash at bank and in hand	**544**	1,403	**–**
	624	1,528	**–**
Divided between			
Cash and bank deposits repayable on demand (note 25)	**221**	567	**–**
Liquid resources (note 25)	**403**	961	**–**
	624	1,528	**–**

16 Creditors

	Note	Group 2000 £ million	Group 1999 £ million	Company 2000 £ million
Amounts falling due within one year				
Bank loans and overdrafts				
Repayable on demand		**74**	75	**–**
Other		**1,747**	761	**–**
Debenture loans		**8**	15	**–**
Obligations under finance leases		**1**	–	**–**
	17	**1,830**	851	**–**
Payments received in advance		**106**	96	**–**
Trade creditors		**825**	561	**–**
Amounts owed to joint ventures and associates		**10**	82	**–**
Taxation on profit		**154**	108	**–**
Other taxation and social security		**102**	59	**–**
Other creditors		**330**	143	**–**
Accruals and deferred income		**557**	348	**–**
Proposed dividend		**93**	348	**93**
		4,007	2,596	**93**
Amounts falling due after more than one year				
Debenture loans		**37**	50	**–**
Bonds	17	**894**	–	**–**
Obligations under finance leases		**8**	3	**–**
	17	**939**	53	**–**
Payments received in advance		**60**	17	**–**
Trade creditors		**1**	2	**–**
Other creditors		**78**	60	**–**
		1,078	132	**–**

17 Borrowings

	Group 2000 £ million	Group 1999 £ million	Company 2000 £ million
Bank loans and overdrafts			
Unsecured	**1,821**	836	**–**
Debenture loans			
Secured	**30**	32	**–**
Unsecured	**15**	33	**–**
Bonds	**894**	–	**–**
Obligations under finance leases	**9**	3	**–**
	2,769	904	**–**
Less amounts falling due within one year	**(1,830)**	(851)	**–**
	939	53	**–**
Analysis of repayments of loans and debentures			
Between one and two years	**6**	8	**–**
Between two and five years	**315**	34	**–**
In more than five years	**618**	11	**–**
	939	53	**–**
Debenture loans			
Repayable at par wholly within five years (average rate 5.6 per cent)	**315**	45	**–**
Repayable at par partly or wholly after five years mainly by instalments (average rate 6.4 per cent)			
Total amount	**624**	20	**–**
Instalment due after five years	**612**	11	**–**

Bonds

On 30 March 2000, the Group issued for cash consideration two unsecured euro bonds. The first euro bond has a principal amount of €500 million with a coupon rate of 5.625 per cent per annum, maturing on 30 March 2005. The second euro bond has a principal amount of €1,000 million with a coupon rate of 6.375 per cent per annum, maturing on 30 March 2010.

Maturity

An analysis of the maturity of the Group's debt is given note 25.

Borrowing facilities

The Group has various undrawn committed drawing facilities. The undrawn facilities available at 31 March were:

	Group 2000 £ million	Group 1999 £ million
Expiring in one year or less	**2,306**	1,020
Expiring in more than two years but not more than five years	**1,208**	2,396
	3,514	3,416

18 Provisions for liabilities and charges

	Restructuring £ million	Share options £ million	Other £ million	Group Total £ million	Company £ million
At 1 April 1999	70	–	267	**337**	–
Exchange rate adjustment	(1)	–	(11)	**(12)**	–
Acquisitions	21	–	201	**222**	–
Disposals	(3)	–	(2)	**(5)**	–
Charged	25	396	112	**533**	–
Released	(13)	–	(46)	**(59)**	–
Spent against existing provisions	(31)	–	(115)	**(146)**	–
	68	396	406	**870**	–

Other provisions mainly comprise expected cost of maintenance under guarantees, other work in respect of products delivered, losses on contract work in progress and other provisions for post retirement benefits.

The associated outflows are generally expected to occur over the life of the products and contracts which are long term in nature.

19 Equity shareholders' interest

a Share capital

	Number of shares	£
Fully paid ordinary shares of 5 pence each (at date of incorporation)	2	0.10
Fully paid ordinary shares of 5 pence each (reconstruction of GEC)	2,723,486,794	136,174,339.70
	2,723,486,796	136,174,339.80
Shares allotted under The Managers' 1984 Share Option Scheme	197,955	9,897.75
Shares allotted under The 1997 Executive Share Option Scheme	142,457	7,122.85
Shares allotted under The Marconi 1999 Stock Option Plan	9,173	458.65
Shares allotted under the terms of the acquisition of RELTEC Corporation	160,069	8,003.45
Shares allotted at 31 March 2000	2,723,996,450	136,199,822.50
Unissued ordinary shares	3,276,003,550	163,800,177.50
Authorised	6,000,000,000	300,000,000.00

In accordance with the terms of the reconstruction of GEC, ordinary shares of 5 pence each were issued by the Company, credited as fully paid to the former holders of GEC ordinary shares of 5 pence each on the register at the close of business 26 November 1999. All other share issues were satisfied by cash consideration. The ordinary shares in Marconi plc were issued to former GEC shareholders in consideration for the remaining businesses of GEC following the separation of the MES Business.

Under the terms of the acquisition of RELTEC Corporation, all RELTEC options were rolled over into Marconi options. 160,069 of these options have subsequently been exercised.

b Shares to be issued

This represents the Marconi ordinary shares to be issued to employees under the Marconi Launch Share Plan (note 4).

c Group reserves

	Share premium account £ million	Capital reserve £ million	Revaluation reserve £ million	Profit and loss account £ million
At 1 April 1999	–	351	847	2,215
Issue of GEC ordinary shares	–	2	–	–
Cancellation of GEC ordinary shares	–	(136)	–	–
Added in the year	1	158	309	500
At 31 March	1	375	1,156	2,715

As at 1 April 1999, the Group reserves other than the share premium account shown represent those reserves in Marconi Corporation plc (formerly The General Electric Company, p.l.c.) adjusted to reflect the separation of the MES Business (see Basis of preparation note on page 48). The movement in capital reserves of £158 million represents those shares issued by GEC prior to the separation of the MES Business. Exchange gains of £143 million and related tax charges of £43 million on borrowings hedged against equity investments denominated in foreign currencies and gains of £33 million and related tax charges of £11 million on associated tax equalisation swaps have been taken to Group reserves.

d Parent reserves

	Profit and loss account £ million
At 17 September 1999	–
Profit for the year	207
At 31 March	207

Notes

1 £34 million (1999 £82 million) of the Group's balance on the profit and loss account is not available for distribution at 31 March 2000, being the Group's share of reserves held by joint ventures and associates.

2 Pursuant to Section 230 of the Companies Act 1985 the Company is not presenting its own profit and loss account in addition to the consolidated profit and loss account on page 50. The profit of the Company from 17 September 1999 (date of incorporation) to 31 March 2000 amounted to £349 million.

20 Cash flow

a Net cash inflow from operating activities

	2000 £ million	1999 £ million
Group operating (loss)/profit	**(144)**	369
Depreciation charge	**155**	108
Goodwill amortisation	**763**	63
Increase in stocks	**(122)**	(66)
Increase in debtors	**(374)**	(85)
Increase in creditors	**349**	83
Decrease in provisions	**(17)**	(38)
	610	434

b Exceptional cash flows related to merger/demerger

	2000 £ million	1999 £ million
Dividends and other cash receipts/(payments)	**1,409**	(497)
Other	**(23)**	–
	1,386	(497)

c Net cash inflow from management of liquid resources

Comprising term deposits generally of less than one year and other readily disposable current asset investments

	2000 £ million	1999 £ million
Deposits made with banks and similar financial institutions	**(7,041)**	(5,405)
Deposits withdrawn from banks and similar financial institutions	**7,559**	5,471
Purchases of Government and similar securities	**(2)**	(1)
Sales of Government and similar securities	**107**	14
Purchases of securities issued by banks and other corporate bodies	**(3)**	(2)
Sales of securities issued by banks and other corporate bodies	**36**	4
	656	81

d Net cash flow from financing

	2000 £ million	1999 £ million
Increases in bank loans	**1,146**	657
Increases in debenture loans	**650**	2
Capital element of finance lease repayments	**7**	(1)
	1,803	658
Loans (repaid to)/received from joint ventures	**(70)**	70
Other	**(46)**	–
	1,687	728

21 Analysis of net monetary funds

	At 1 April 1999 £ million	Cash flow £ million	Acquisitions/ disposals (excluding cash and overdrafts) £ million	Exchange rate adjustment £ million	**At 31 March 2000 £ million**
Cash at bank and in hand	567	(343)		(3)	**221**
Overdrafts	(75)	(2)		3	**(74)**
		(345)			
Liquid resources	961	(656)	108	(10)	**403**
Amounts falling due within one year					
Bank loans	(761)	(1,146)	–	160	**(1,747)**
Debenture loans	(15)	236	(228)	(1)	**(8)**
Finance leases	–	(1)	–	–	**(1)**
Amounts falling due after more than one year					
Bank loans	–	–	–	–	**–**
Debenture loans	(50)	(886)	–	5	**(931)**
Finance leases	(3)	(6)	–	1	**(8)**
		(1,803)			
	624	(2,804)	(120)	155	**(2,145)**

22 Acquisitions and disposals

	2000 £ million	1999 £ million
Purchase consideration	**4,111**	968
Fair value of net tangible assets acquired	**183**	170
Goodwill arising in the Group	**3,928**	798

Goodwill of £3,928 million comprises £2,636 million for FORE Systems, £1,166 million for RELTEC Corporation and £126 million for other acquisitions in aggregate.

a Investments in subsidiary companies

During the year acquisitions were made and accounted for using the acquisition method.
Changes in the structure of the Group are shown in the Directors' Report on page 38.

Analysis of fair value of identifiable net assets of subsidiaries acquired

	RELTEC £ million	FORE £ million	Other £ million	**2000 Total £ million**	1999 Total £ million
Tangible fixed assets	86	50	47	**183**	14
Investments	–	4	–	**4**	–
Inventory	91	43	93	**227**	28
Debtors	138	80	105	**323**	70
Cash at bank and in hand	13	113	11	**137**	11
Liquid resources	–	108	–	**108**	–
Overdrafts	–	–	–	**–**	(7)
Creditors and provisions	(261)	(118)	(180)	**(559)**	(51)
Loan capital	(226)	–	(2)	**(228)**	(9)
Taxation	12	(23)	–	**(11)**	(5)
Minority interest	(1)	–	–	**(1)**	119
	(148)	257	74	**183**	170
Satisfied by:					
Cash subscribed	1,018	2,893	200	**4,111**	956
Deferred consideration	–	–	–	**–**	12
	1,018	2,893	200	**4,111**	968

22 Acquisitions and disposals continued

RELTEC Corporation

	Book value £ million	Fair value adjustments: Revaluation adjustments £ million	Accounting policy adjustments £ million	Other adjustments £ million	Fair value £ million
Tangible fixed assets	93	(7)	–	–	86
Investments	–	–	–	–	–
Stocks and contracts in progress	94	–	–	(3)	91
Debtors	138	–	–	–	138
Cash at bank and in hand	13	–	–	–	13
Liquid resources	–	–	–	–	–
Creditors and provisions	(208)	(53)	–	–	(261)
Loan capital	(223)	–	(3)	–	(226)
Taxation	13	–	–	(1)	12
Minority interest	(1)	–	–	–	(1)
	(81)	(60)	(3)	(4)	(148)

The fair value adjustments on RELTEC Corporation relate to the revaluation of impaired plant and equipment, the settlement costs of legal claims not provided for, and other costs.

FORE Systems

	Book value £ million	Fair value adjustments: Revaluation adjustments £ million	Accounting policy adjustments £ million	Other adjustments £ million	Fair value £ million
Tangible fixed assets	51	(1)	–	–	50
Investments	3	–	–	1	4
Stocks and contracts in progress	62	(19)	–	–	43
Debtors	81	–	–	(1)	80
Cash at bank and in hand	113	–	–	–	113
Liquid resources	108	–	–	–	108
Creditors and provisions	(88)	(30)	–	–	(118)
Loan capital	–	–	–	–	–
Taxation	22	(31)	(14)	–	(23)
Minority interest	–	–	–	–	–
	352	(81)	(14)	–	257

The fair value adjustments on FORE Systems relate to the revaluation of stocks to net realisable value, provision for legal claims and for contingent consideration on prior acquisitions, deferred tax assets not recognised under UK GAAP, and other identified tax exposures.

There were no other material adjustments to book values of other subsidiaries acquired.

Net cash flow from operating activities includes £61 million in respect of RELTEC Corporation and £80 million in respect of FORE Systems since acquisition. Net cash flow from financing and net cash flow from capital expenditure and financial investment includes an outflow of £226 million and £34 million respectively in relation to RELTEC Corporation. Net cash flow from capital expenditure and financial investment and net cash flow from management of liquid resources includes £64 million and £108 million respectively in relation to FORE Systems.

The results of RELTEC Corporation and FORE Systems prepared under US GAAP for the three months from 1 January 1999 to 31 March 1999 (RELTEC) and for the period from 1 April 1999 to 16 June 1999 (FORE) were as follows:

	RELTEC $ million	FORE $ million
Net sales	**257**	104
Losses before interest, income tax and extraordinary items pre-acquisition	**(18)**	(23)
Net losses after tax	**(12)**	(16)

Net losses after tax, presented under US GAAP, for the year ended 31 December 1998 were $36 million (RELTEC) and $133 million for the year ended 31 March 1999 (FORE).

22 Acquisitions and disposals continued

b Sales of interests in subsidiaries and associates

	1999 £ million
Net assets contributed	
Tangible fixed assets	5
Investments in associates	69
Other fixed asset investments	–
Inventory	2
Debtors	2
Cash at bank and in hand	–
Overdrafts	–
Creditors and provisions	(2)
Finance leases	–
Goodwill	199
	275
Accounted for by:	
Consideration	1,050
Profit on disposal	775

23 Post retirement benefits

a Pensions

Pension plan assets are held in trustee-administered funds independent of the Group's finances. The principal pension scheme, the G.E.C. 1972 Plan (the Plan) is open to all permanent UK employees of participating companies. Retirement benefits are primarily of the 'defined benefit' type.

As a result of the separation of the MES Business, the MES employees ceased to participate in the Plan and, on 6 April 2000, were transferred to a new BAE Systems pension scheme (the BAE Systems 2000 Pension Plan – the BAE Plan) providing identical benefits to the Plan. A share of the Plan's assets will be transferred to the corresponding new BAE Plan, proportional to the share of the total Plan's liabilities as at 6 April 2000 that were attributable to the MES members. The actual transfer of the Plan's assets relating to transferring MES members will be based on actuarial calculations to be performed as at 6 April 2000.

In accordance with the Transactions Agreement relating to the separation of the MES Business, an estimate of the initial transfer value for MES members of the Plan has been made by reference to an actuarial valuation as at 6 April 1999. Based on this estimate, a transfer was made from the Plan. On finalisation of the transfer value as at 6 April 2000, the remaining amount will be transferred from the Plan.

The actuarial valuation as at 6 April 1999 was undertaken using the 'projected unit' method. At the valuation date the members transferring to the BAE Plan were included in the valuation results. The main financial assumptions for assessing the funding position of the Plan adopted for the valuation were that the discount rate for pensioner liabilities and non-pensioner liabilities was 5 per cent and 6 per cent per annum respectively, increases in pensionable earnings would average 5 per cent per annum, that present and future pensions would increase at the rate of 3 per cent per annum and State pensions by 3 per cent per annum. The discount rate assumed in assessing the long term employer contribution rate was 7.25 per cent per annum.

The accumulated assets of the Plan were sufficient to fully finance the past service liabilities including provision for future inflation. The market value of the assets was £5,048 million at the valuation date. The actuary advised that, taking into account members' contributions of 3 per cent and allowing for an average discount rate of 5.75 per cent, the Company's contribution rate could be maintained at the current level of 6.6 per cent of pensionable salaries until the next actuarial valuation due as at 6 April 2002.

The total pension cost charged to the profit and loss account, excluding MES members, for the year ended 31 March 2000 amounted to £26 million (1999 £21 million). The provision in the balance sheet which resulted from the difference between the pension cost charge and contributions amounted to £23 million (1999 £26 million) in respect of the Plan, and provision for unfunded liabilities amounted to £80 million (1999 £22 million) in respect of other plans.

b Post retirement benefits other than pensions

At 31 March 2000, 9,352 employees (1999 4,860 employees) and 2,361 retired employees (1999 1,787 retired employees) of companies in the US and Canada were entitled to health care benefits after retirement. The schemes are unfunded. The benefits cost charge and provisions for the liability included in the accounts are determined by a qualified independent actuary.

During the year, the benefits cost charge was £1 million (1999 £1 million); healthcare costs after retirement charged to the provision amounted to £4 million (1999 £4 million) and the retranslation for exchange movements increased the provision by £1 million (1999 £1 million). The liability was increased in 2000 by £9 million for businesses acquired. As a result, the provision at 31 March 2000 was £74 million (1999 £67 million).

24 Other information

a Contingent liabilities

	Group 2000 £ million	1999 £ million	Company 2000 £ million
At 31 March	**25**	25	**–**

Contingent liabilities relate mainly to the cost of legal proceedings, which in the opinion of the Directors, are not expected to have a materially adverse effect on the Group.

b Capital expenditure

	Group 2000 £ million	1999 £ million	Company 2000 £ million
Commitments contracted at 31 March	**59**	40	**–**

c Operating leases

	Group 2000 £ million	1999 £ million	Company 2000 £ million
Charges in the year			
Land and buildings	**30**	15	**–**
Other items	**15**	8	**–**
	45	23	**–**
Amounts payable under operating leases which fall due in the next financial year			
Land and buildings, leases expiring			
Within one year	**7**	5	**–**
Between two and five years	**15**	9	**–**
After five years	**9**	4	**–**
Other items, leases expiring			
Within one year	**3**	1	**–**
Between two and five years	**12**	9	**–**
After five years	**11**	2	**–**
	57	30	**–**

Non-audit fees worldwide to the Group auditors amounted to £8.1 million (1999 £7.8 million) including £2.8 million for Year 2000 Programme support and £4.0 million for professional advice on acquisitions, disposals and capital restructuring.

25 Financial Instruments

Treasury policy and the Group's use of financial instruments are dealt with in the Finance Director's Review on page 29. Short term debtors and creditors have been excluded from all disclosures below except the currency profile.

a Currency and interest rate risk profile of financial liabilities

Financial assets

After taking into account interest rate swaps and forward currency contracts, the interest rate profile of the Group's financial assets at 31 March 2000 and 31 March 1999 were:

31 March 2000

	Total £ million	Floating Rate £ million	Fixed rate £ million	Non-interest bearing £ million	Fixed rate Average interest rate %	Fixed rate Weighted period years	Non-interest bearing weighted average period years
Sterling	205	31	174	–	5.9	0.1	–
US dollars	225	42	164	19	5.8	0.2	3.4
Euro	150	121	28	1	2.2	0.1	1.8
Other	65	38	26	1	5.7	0.1	1.5
Total	645	232	392	21	5.6	0.1	3.2
Analysed between							
Cash at bank and in hand (note 15)	221	139	82	–			
Liquid resources (note 15)	403	93	310	–			
Long term debtors and amounts recoverable on contracts	21	–	–	21			
	645	232	392	21			

25 Financial Instruments continued

31 March 1999

	Total £ million	Floating Rate £ million	Fixed rate £ million	Non-interest bearing £ million	Fixed rate Average interest rate %	Fixed rate Weighted period years	Non-interest bearing weighted average period years
Sterling	1,156	478	676	2	5.8	0.3	2.5
US dollars	99	17	68	14	4.9	–	2.4
Euro	223	146	74	3	3.0	1.0	2.5
Other	70	41	28	1	5.0	0.2	2.5
Total	1,548	682	846	20	5.6	0.3	2.4
Analysed between							
Cash at bank and in hand (note 15)	567	497	70	–			
Liquid resources (note 15)	961	185	776	–			
Long term debtors and amounts recoverable on contracts	20	–	–	20			
	1,548	682	846	20			

Financial liabilities

After taking into account interest rate swaps and forward currency contracts, the interest rate profile of the Group's financial liabilities at 31 March 2000 and 31 March 1999 were:

31 March 2000

	Total £ million	Floating Rate £ million	Fixed rate £ million	Non-interest bearing £ million	Fixed rate Average interest rate %	Fixed rate Weighted period years	Non-interest bearing weighted average period years
Sterling	60	–	1	59	6.0	–	7.7
US dollars	1,560	37	1,523	–	5.9	8.6	–
Euro	1,192	526	665	1	5.5	8.8	4.0
Other	18	14	3	1	6.4	1.0	1.8
Total	2,830	577	2,192	61	5.8	8.7	7.5
Analysed between							
Borrowings (note 17)	2,769	577	2,192	–			
Long term trade creditors	61	–	–	61			
	2,830	577	2,192	61			
Maturity profile of financial liabilities							
In one year or less, or on demand	1,830						
In more than one year, but no more than two years	19						
In more than two years, but no more than five years	330						
In more than five years	651						
	2,830						

31 March 1999

	Total £ million	Floating Rate £ million	Fixed rate £ million	Non-interest bearing £ million	Fixed rate Average interest rate %	Fixed rate Weighted period years	Non-interest bearing weighted average period years
Sterling	55	46	–	9	–	–	4.5
US dollars	672	48	623	1	5.8	9.3	4.1
Euro	151	99	45	7	3.9	1.0	1.5
Other	45	34	9	2	6.7	1.0	2.3
Total	923	227	677	19	5.7	8.6	3.0
Analysed between							
Borrowings (note 17)	904	227	677	–			
Long term trade creditors	19	–	–	19			
	923	227	677	19			
Maturity profile of financial liabilities							
In one year or less, or on demand	851						
In more than one year, but no more than two years	16						
In more than two years, but no more than five years	37						
In more than five years	19						
	923						

Floating rate borrowings and assets bear interest based on relevant national LIBOR equivalents.

25 Financial Instruments continued

b Currency profile

At 31 March 2000 and 31 March 1999, after taking into account the effects of currency swaps and forward foreign exchange contracts, the Group's currency exposures, excluding borrowings treated as hedges, were:

31 March 2000

	Net foreign currency monetary assets/(liabilities)				
Functional currency of Group operation	Sterling £ million	US Dollars £ million	Euro £ million	Other £ million	Total £ million
Sterling	–	1	8	1	10
US dollars	–	–	–	(2)	(2)
Euro	52	(8)	–	2	46
Other	12	5	–	–	17
Total	64	(2)	8	1	71

31 March 1999

	Net foreign currency monetary assets/(liabilities)				
Functional currency of Group operation	Sterling £ million	US Dollars £ million	Euro £ million	Other £ million	Total £ million
Sterling	–	4	49	(25)	28
US dollars	53	–	–	–	53
Euro	53	(29)	–	(1)	23
Other	179	2	1	–	182
Total	285	(23)	50	(26)	286

The Group's net monetary funds and net assets by currency at 31 March 2000 and 31 March 1999 were:

31 March 2000

Functional currency of Group operation	Net assets before net monetary funds £ million	Net monetary funds £ million	Net assets £ million
Sterling	718	(2,361)	(1,643)
US dollars	5,347	151	5,498
Euro	423	4	427
Other	303	61	364
Total	6,791	(2,145)	4,646

31 March 1999

Functional currency of Group operation	Net assets before net monetary funds £ million	Net monetary funds £ million	Net assets £ million
Sterling	2,283	227	2,510
US dollars	(51)	113	62
Euro	476	50	526
Other	92	234	326
Total	2,800	624	3,424

Notes to the Accounts
continued

25 Financial Instruments continued

c Fair values of financial assets and liabilities

The book values and fair values of the Group's financial assets and liabilities at 31 March 2000 and 31 March 1999 were:

	Book value		Fair value	
	2000 £ million	1999 £ million	**2000 £ million**	1999 £ million
Short term financial liabilities and current portion of long term borrowings	**(1,830)**	(851)	**(1,830)**	(851)
Long term borrowings	**(1,000)**	(72)	**(977)**	(69)
Financial assets	**645**	1,548	**641**	1,546
Interest rate swaps	**–**	–	**124**	(10)
Forward foreign currency contracts	**–**	–	**6**	1
Currency swaps	**–**	–	**–**	–
Tax equalisation swaps	**(41)**	–	**(27)**	–
Equity swaps	**(33)**	–	**(33)**	–

The fair values of the interest rate swaps and tax swaps have been determined by references available from the markets on which the instruments are traded. Forward foreign currency contracts and other fair values have been calculated by discounting cash flows at prevailing interest rates.

d Gains and losses on hedges

The Group enters into forward foreign exchange contracts to eliminate the currency exposure arising on sales and purchases denominated in foreign currencies as soon as there is a firm contractual commitment. It also uses interest rate swaps to manage its interest rate profile.

An analysis of these unrecognised gains and losses is as follows:

	Gains £ million	Losses £ million	Total net gains/ (losses) £ million
Unrecognised gains and losses on hedges at 1 April 1999	2	(11)	(9)
Gains and losses arising in previous years that were recognised in the year	–	–	–
Gains and losses arising before 1 April 1999 that were not recognised in the year	2	(11)	(9)
Gains and losses arising in the year to 31 March 2000 that were not recognised in that year	141	(2)	139
Unrecognised gains and losses on hedges at 31 March 2000	143	(13)	130
Of which:			
Gains and losses expected to be recognised in the year to 31 March 2001	9	(2)	7
Gains and losses expected to be recognised in the year to 31 March 2002 or later	134	(11)	123

It was impracticable to disclose the amount of the net gains or losses not recognised at 31 March 1998 which had been dealt with in the profit and loss account for the year ended 31 March 1999.

£2 million of the gains and £1 million of the losses unrecognised at 31 March 1999 were expected to have been recognised in the profit and loss account for the year ended 31 March 2000.

The cumulative aggregate gains and losses which are carried forward in the balance sheet pending their inclusion in the profit and loss account total £41 million (1999 £nil), of which £10 million (1999 £nil) is expected to be included in the profit and loss account in the next accounting period.

26 Post Balance Sheet Events

On 20 April 2000 the Company announced an agreement to acquire Metapath Software International, Inc. (MSI), a global provider of consulting and planning services and operational support software used by the wireless telecommunications industry for an initial consideration of $618 million (£391 million).

Sir Alan Rudge, a non-executive Director of the Company and non-executive Chairman of MSI, holds a substantial number of options in MSI. At the date of completion, he will receive approximately $5.3 million from MSI in respect of the cancellation of his options, which represents the difference between the offer price in the MSI transaction ($17.50) and the exercise price of such options. Sir Alan Rudge did not participate in that part of any Marconi Board meeting which considered the proposed acquisition of MSI, nor did he receive any Board papers related thereto.

27 Statutory Consolidated Profit and Loss Account

For the period from 17 September 1999 to 31 March 2000

	£ million
Turnover	
Group	3,029
Share of joint ventures	174
	3,203
Operating profit	
Group operating profit	
Excluding goodwill amortisation and exceptional items	434
Goodwill amortisation	(248)
Operating exceptionals	(78)
	108
Share of joint ventures	
Excluding goodwill amortisation and exceptional items	17
Goodwill amortisation	(2)
Operating exceptionals	(1)
	14
	122
Group and joint venture operating profit before goodwill amortisation and exceptional items	451
Share of associates	3
Operating profit	125
Exceptional items, merger/demerger receipts and (costs)	737
Exceptional items, gains less losses on disposals of subsidiaries and other fixed assets	4
Income from loans, deposits and investments, less interest payable	
Group	(59)
Share of joint ventures and associates	6
	(53)
Profit on ordinary activities before taxation	
Excluding goodwill amortisation and exceptional items	401
Goodwill amortisation and exceptional items	412
	813
Tax credit / (charge) on profit on ordinary activities	
Excluding tax on goodwill amortisation and exceptional items	(126)
Tax on goodwill amortisation and exceptional items	198
	72
Profit on ordinary activities after taxation	885
Minority interests	(1)
Profit on ordinary activities attributable to the shareholders	884
Dividends	(142)
Profit on ordinary activities attributable to the shareholders	742
Basic earnings per share	32.5p
Diluted earnings per share	32.2p
Earnings per share before goodwill amortisation and exceptional items	10.1p

Notes to the Statutory Consolidated Profit and Loss Account

The profit and loss account above covers the first statutory accounting reference period of Marconi plc from its date of incorporation on 17 September 1999 to 31 March 2000 and is required by the Companies Act 1985.

Supporting note disclosures for this period are not given as they would not provide users of accounts with material information.

The amounts in respect of Directors' remuneration required by the Companies Act 1985 Schedule 6 are included within the amounts shown in the Report by the Board to Shareholders on Directors' Remuneration on pages 42 and 43 which covers remuneration for the 12 months to 31 March 2000. Amounts for the statutory reference period in respect of salaries and other time related costs can be derived by apportioning the annual amounts.

Principal Subsidiaries and Associated Companies

Communications	Country of Incorporation
Communications Networks	
Communications Services	
Marconi Communications Ltd	Great Britain
Marconi Communications Inc.	US
FORE Systems, Inc.	US
Mobile Communications	
Marconi Communications S.p.A.	Italy

Systems	
Marconi Commerce Systems Inc.	US
Marconi Medical Systems, Inc.	US
Marconi Data Systems, Inc.	US

Capital	
Marconi Applied Technologies Ltd	Great Britain
Marconi Software Solutions Ltd	Great Britain
Fibreway Ltd	Great Britain
General Domestic Appliances Ltd (50.0%)	Great Britain
Woods Air Movement Ltd	Great Britain

Other	
Marconi Corporation plc	Great Britain

Other Associated Companies	
Plessey Holdings Ltd (50.0%)	Great Britain

1 All wholly-owned subsidiaries and associated companies disclosed above are owned by a subsidiary or subsidiaries of the Company. Further statutory information on the principal associated companies is set out below.
2 The above list of subsidiaries includes those businesses that had a material effect on the consolidated results to 31 March 2000.

Statutory Information on Associated Companies

	Class of shares	Number	Proportion of shares held %	Marconi Group equity interest
United Kingdom				
General Domestic Appliances Holdings Ltd				50.00
	'A' shares of £1	1,140,000	–	
	'B' shares of £1	1,140,000	100.00	
	'C' shares of £10, non-voting	2,362,000	100.00	
	'D' shares of £1, non-voting	100,000	–	
Plessey Holdings Ltd				50.00
	'G' ordinary shares of £1	300,500,000	100.00	
	'S' ordinary shares of £1	300,500,000	–	
Overseas				
Xcert International, Inc.				25.00
	Series E preferred stock	5,470,001	25.00	

Statistical Information 1996/2000

	2000 £m	1999 £m	1998 £m	1997 £m	1996 £m
Sales					
– continuing operations and share of joint ventures	**5,724**	4,090	3,768	3,515	3,440
– total	**5,724**	4,090	4,162	4,554	4,479
Operating (loss)/profit					
– continuing operations, excluding goodwill amortisation and exceptional items [(1)]	**750**	508	439	369	378
– total	**(115)**	448	555	391	587
Profit before taxation					
– continuing operations, excluding goodwill amortisation and exceptional items [(1)]	**654**	576	513	430	467
– total	**523**	976	794	655	735
Earnings per share					
– continuing operations, excluding goodwill amortisation and exceptional items [(1)]	**16.9p**	13.0p	11.1p	9.0p	9.4p
– basic	**19.4p**	22.4p	17.2p	14.3p	15.2p
Ordinary dividends [(2)]	**142**	348	311	365	345
Per share	**5.20p**	13.00p	11.43p	13.15p	12.51p
Retained profit [(3)]	**380**	259	169	34	72
Goodwill	**4,397**	1,220	485	456	424
Fixed assets	**758**	470	398	578	658
Investments	**1,626**	1,223	1,024	1,037	1,069
Inventories	**946**	616	548	668	721
Debtors	**2,250**	1,432	1,253	1,196	1,418
Net monetary (debt)/funds [(4)]	**(2,145)**	624	1,035	862	547
	7,832	5,585	4,743	4,797	4,837
Liabilities	**(3,186)**	(2,161)	(2,026)	(1,912)	(1,647)
	4,646	3,424	2,717	2,885	3,190
Financed by					
Shareholders' interests	**4,630**	3,413	2,573	2,771	3,058
Minority interests	**16**	11	144	114	132
	4,646	3,424	2,717	2,885	3,190

Notes

1 Continuing operations, as used in the table above, reflects the historical track record of those businesses, both Group and share of joint ventures, which form part of the Marconi Group as at 31 March 2000. The income received by the Group from its stake in Alstom (formerly GEC Alsthom), which was equity accounted until 30 September 1998, and those businesses previously disposed have been excluded.

2 The dividends per share for the years ended 31 March 1996 to 31 March 1999 reflect the dividends paid under the GEC distribution policy, which is not comparable as Marconi only merged with the non-defence businesses of GEC.

3 The interest, tax and management charges included in the retained profit for the years ended 31 March 1996 to 31 March 1999 reflect the overall historic corporate structure of GEC. These are not necessarily indicative of those which would have been incurred had the MES business been separated prior to 1 April 1995.

4 Net monetary (debt)/funds are as described in note 21 to the accounts.

Information for Shareholders

Shareholding Analysis

Classification of shareholders*	Number of holders	Percentage of total holders	Number of shares	Percentage of issued capital
Individuals				
United Kingdom	93,893	68.01	200,933,198	7.38
Foreign	3,824	2.77	9,853,785	0.36
Institutions				
United Kingdom	39,639	28.72	2,510,714,436	92.17
Foreign	698	0.5	2,495,031	0.09
	138,054	100	2,723,996,450	100

Banks/Nominees	28,789	20.85	2,078,997,501	76.32
Other Companies	10,081	7.31	321,487,144	11.80
Insurance Companies	787	0.57	69,997,386	2.57
Investment Trusts	642	0.46	8,612,017	0.32
Pension Funds	38	0.03	34,115,419	1.25
Individuals	97,717	70.78	210,786,983	7.74
	138,054	100	2,723,996,450	100

Shareholding Range*

1 – 100	6,677	4.84	292,450	0.01
101 – 1,000	58,245	42.19	33,264,050	1.22
1,001 – 5,000	59,431	43.05	132,410,658	4.86
5,001 – 25,000	11,094	8.04	101,587,546	3.73
25,001 – 100,000	1,277	0.93	63,918,865	2.35
100,001 – 500,000	806	0.58	188,551,713	6.92
500,001 – 1,000,000	199	0.14	141,037,710	5.18
1,000,001 – 10,000,000	278	0.2	801,309,843	29.42
10,000,001 – and over	47	0.03	1,261,623,615	46.31
	138,054	100	2,723,996,450	100

*as at 31 March 2000

Financial Calendar

19 May 2000	Preliminary Statement published including recommended final dividend for the year ended 31 March 2000
16 June 2000	Annual Report and Accounts or Summary Financial Statement and letter from the Chairman posted to shareholders
19 June 2000	Ordinary shares first quoted ex-dividend
23 June 2000	Record date for the final dividend
21 July 2000	Final date for receipt of elections for the Dividend Re-Investment Plan
25 July 2000	Annual General Meeting
11 August 2000	Payment of final dividend and purchase of shares under the Dividend Re-Investment Plan
24 August 2000	Posting of Dividend Re-Investment Plan share certificates
29 November 2000	Interim Statement published including interim dividend for the year ending 31 March 2001
11 December 2000	Ordinary shares first quoted ex-dividend
12 December 2000	Interim Statement posted to shareholders
15 December 2000	Record date for the interim dividend
9 February 2001	Payment of interim dividend
24 May 2001**	Preliminary Statement published including recommended final dividend for the year ended 31 March 2001
18 July 2001**	Annual General Meeting

**provisional dates

Information for Shareholders

continued

UK Taxation

Income tax on dividends

Dividends are normally paid with a tax credit attaching which, together with the dividend, constitutes an individual shareholder's income for tax return purposes. From 6 April 1999 with the abolition of advance corporation tax (ACT) the rate of tax credit is reduced to 10/90ths. However, as a result of a reduction in the rate of tax on dividend income from 6 April 1999 there should be no increase in the income tax borne by UK resident individual shareholders in respect of dividend income. Tax credits will in general no longer be repayable to UK resident individual shareholders whose tax liability is less than the associated tax credit.

Capital gains tax

The market value of GEC ordinary shares at 31 March 1982 depends on the treatment afforded to the capital repayment of 15 pence per 25 pence share made by GEC in November 1982 and the treatment of proceeds received in respect of the auction or exercise of Put Warrants in October 1998.

If the capital repayment in November 1982 has been treated as a part disposal for capital gains purposes, the market value is 163.1 pence per ordinary share of 5 pence each; where the November 1982 capital repayment has been treated as a reduction of a shareholder's capital gains cost, the market value is 160.1 pence per ordinary share of 5 pence each. These market values are adjustable for individuals by the indexation allowance for periods up to 5 April 1998 but not thereafter for disposals made after 5 April 1998.

The above market values will need adjustment for the treatment of proceeds received in respect of the auction of Put Warrants or the capital element received on exercise of Put Warrants to calculate the base cost.

To calculate the base cost of shares acquired since 31 March 1982, the cost of acquisition will, where appropriate, need to be adjusted for the capital repayment/Put Warrants referred to above, as adjusted for indexation up to 5 April 1998.

Former GEC shareholders issued with the Securities Package on completion of the merger of Marconi Electronic Systems into British Aerospace Plc, consisting of Marconi plc ordinary shares, British Aerospace Plc ordinary shares and Capital Amortising Loan Stock (CALS) will need to allocate the base cost of one GEC ordinary share to each element of the Securities Package as follows:

Marconi plc	Ordinary shares	82.7690871%
British Aerospace Plc	Ordinary shares	15.8827107%
British Aerospace Plc	CALS	1.3482022%

Shareholders are also referred to the Chairman's letter sent out with the interim dividend payment on 4 February 2000.

Shareholder Services

The Marconi Registrar

Enquiries concerning shareholdings in Marconi such as a change of address, dividend payments and share certificates should be addressed to:
The Marconi Registrar, Computershare Services PLC,
P. O. Box 82, The Pavilions, Bridgwater Road, Bristol BS99 7NH
Telephone: 0870 702 0118 Facsimile: 0870 703 6116

Dividend Re-Investment Plan

The Company operates a Dividend Re-Investment Plan. Details can be obtained from The Marconi Registrar, Computershare Services PLC.

The Marconi Share Purchase Scheme

The Company has appointed NatWest Stockbrokers Ltd to manage the Marconi Share Purchase Scheme, a facility open to individual Marconi shareholders who wish to acquire additional Marconi shares. Details can be obtained by writing to or telephoning:
The Marconi Share Purchase Scheme, NatWest Stockbrokers, Corporate and Employee Services, 55 Mansell Street, London E1 8AN
Telephone: 0870 600 2050

Individual Savings Account (ISA) and share dealing service

The Company has appointed Barclays Stockbrokers to manage the Company's ISA (limit £7,000 for year ending 5 April 2001, thereafter annual limit £5,000) and to provide shareholders and prospective shareholders with a share dealing service.
Details can be obtained by writing to or telephoning:
Barclays Stockbrokers Ltd, Client Acceptance, Tay House,
300 Bath Street, Glasgow G2 4LH
Telephone: 0845 601 5000 (ISA)
0845 702 3021 (share dealing service)

Share price information

The Marconi share price is available on Ceefax, Teletext and the FT Cityline service, telephone number 0906 843 3141 (calls charged at 60 pence per minute.

General enquiries

For enquiries relating to matters not mentioned above, please write to:
The Secretary, Marconi plc, One Bruton Street, London W1X 8AQ or telephone during normal office hours on +44 (0)20 7493 8484.

Annual General Meeting

The Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1P 3EE, 12 noon, Tuesday, 25 July 2000.

Unsolicited Mail

Marconi, like other companies, is obliged by law to make its share register available upon request to other organisations provided that the organisations concerned pay the appropriate statutory fee. If shareholders wish to restrict the receipt of unsolicited mail they may like to write to: The Mailing Preference Service, Freepost 22, London W1E 7EZ, who can help shareholders have their names removed from certain kinds of lists.

Designed and produced by
Merchant with Langsford Corporate Design
Printed by CTD

Marconi

One Bruton Street, London W1X 8AQ
Telephone: +44 (0)20 7493 8484

www.marconi.com