

## Financial review

### Overview

—Martin Greenslade discusses this year's results

**Martin Greenslade**  
Finance Director



As we all know, this has been an exceptionally turbulent year for the global economy and the business environment as a whole. The UK commercial property market has certainly endured its share of very tough conditions and our financial results have been impacted significantly as a result, with a loss after tax of £5.2bn largely due to a revaluation deficit of £4.7bn. With property values suffering sharp falls, we saw our adjusted net assets decline and our gearing rise. We ended the year with adjusted diluted net assets (NAV) per share of 593p, down 66.4%.

While our numbers demonstrate the challenging year we have had, they also reflect a strong and decisive response from management. Rapidly deteriorating market conditions required us to take tough decisions, and by acting quickly we mitigated the very worst effects of the current market. These actions included: the drawing down of our bank facilities, which ensured that funds remained available to us even if property values continued to fall; the disposal of Trillium, which, although at a loss, raised additional cash at a critical time; and the rebasing of our quarterly dividend from 14.9p per share (restated) to a final proposed dividend of 7.0p per share, reflecting a realistic view of the pressure on income ahead.

Through these and other actions we have achieved a substantial reduction in net debt, down 27% over the year.

The numbers also reflect the support provided by our shareholders, with the £755.7m of cash generated from the Rights Issue helping to strengthen our balance sheet.

Despite very difficult operating conditions, we increased revenue profit by 10.6% in the year. This is a positive achievement, but it is unlikely to be maintained. This year's figure was driven, in part, by lower interest rates on our floating rate debt. Interest rates will not remain at current levels indefinitely and margins will rise as and when we renew our banking facilities. Rental income is also likely to come under downward pressure from falling rental values and voids from tenant insolvencies, lease expiries, partially let developments and pre-development properties. And some of our actions to maintain liquidity and a sound capital base may also have a negative impact on our income statement. An example of this might be the sale of properties to fund our existing committed capital expenditure. Nevertheless, ensuring we have sufficient capital and liquidity will enable us to capitalise on opportunities which will undoubtedly arise in the coming years.

The pages that follow provide you with a detailed review of our figures. Given the scale of events during the year, I hope this overview helps put the results in context and conveys a clear picture of current financial dynamics.

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Finance Director

We completed the sale of Trillium, our outsourcing business, on 12 January 2009. The transaction included all of Trillium's operations with the exception of the Accor hotel portfolio, which is now included within our Retail Portfolio. As Trillium represented a separate major line of business for the Group, it has been treated as a discontinued operation for the year ended 31 March 2009. The income statement and the relevant notes for the prior period have been restated to assist comparison.

Additionally, all financial information on a 'per share' basis including last year's comparatives has been adjusted to reflect the Rights Issue which completed in March 2009. Further details are given below.

#### Headline results

The Group's loss before tax from continuing activities was £4,773.2m, compared to a loss of £988.0m for the year ended 31 March 2008. Revenue profit, our measure of underlying profit before tax, increased by 10.6% from £284.8m to £314.9m.

**Table 11**  
Reconciliation of loss before tax to revenue profit

	Year ended 31/03/09 £m	Year ended 31/03/08 £m
Loss before tax	(4,773.2)	(988.0)
Valuation deficit – Group	4,113.4	1,158.4
– joint ventures	630.3	134.2
Losses/(profits) on non-current property disposals – Group	130.8	(57.3)
– joint ventures	(2.9)	7.1
Joint venture net liabilities adjustment	(17.7)	–
Mark-to-market adjustment on interest rate swaps	102.1	21.9
Mark-to-market adjustment on interest rate swaps – joint ventures	15.4	–
Eliminate effect of bond exchange derecognition	11.7	7.6
Debt restructuring charges	0.7	1.1
Joint venture tax adjustment	1.3	3.1
Demerger costs	10.2	9.8
Profit on sale of trading properties – Group	(2.5)	(2.8)
– joint ventures	(5.5)	(8.3)
Long-term development contract profits	(3.8)	(2.0)
Write-down of trading properties	104.6	–
Revenue profit	314.9	284.8

The basic loss per share from continuing activities increased from a loss of 188.43p last year restated for the Rights Issue and the reclassification of Trillium to discontinued operations to a loss per share of 918.04p, with adjusted diluted earnings per share showing a 2.9% increase on the comparable period to 62.57p (2008: 60.79p).

The loss from discontinued operations for the year all relates to Trillium and amounted to £420.9m, which reflects the loss for the current year of £87.3m and a loss on disposal of £333.6m. The loss for the current year included a goodwill impairment charge of £148.6m and a deficit on revaluation of investment properties of £10.0m, partially offset by underlying profit from the Trillium business.

The combined investment portfolio (including joint ventures) decreased in value from £14.1bn to £9.4bn on the back of a valuation deficit of £4,743.7m or 34.2%. Net assets per share decreased by 1223p from 1862p at the end of March 2008 (restated for the Rights Issue) to 639p in March 2009, with adjusted diluted net assets per share decreasing from 1763p at March 2008 to 593p at March 2009.

#### Loss before tax

The main drivers of our loss before tax from continuing activities were the change in value of our investment portfolio (including any profits or losses on disposal of properties), impairment of our trading properties and the impact of interest rate swaps. The degree to which movement on these and other items led to the increase in our loss before tax from £988.0m last year to a loss of £4,773.2m this year, is explained in [Table 12](#) below.

**Table 12**  
Principal changes in loss before tax from continuing activities and revenue profit

	Loss before tax £m	Revenue profit £m
Year ended 31 March 2008	(988.0)	284.8
Valuation deficit	(3,451.1)	–
Impairment of trading properties	(104.6)	–
Loss on disposal of non-current properties	(178.1)	–
Interest rate swaps	(95.6)	–
Indirect costs	0.8	0.8
Interest on debt and bank borrowings	28.8	32.6
Joint venture net liabilities adjustments	17.7	–
Other	(3.1)	(3.3)
Year ended 31 March 2009	(4,773.2)	314.9

### Valuation deficit

The largest driver behind the increase in the year-on-year loss before tax was the revaluation deficit on our combined investment portfolio (including joint ventures) of £4,743.7m (2008: £1,292.6m). The 34.2% reduction in the market values of our properties is driven by a number of external factors including the overall economic environment and investor demand.

### Impairment of trading properties

Our trading properties are carried at the lower of cost and net realisable value. In accordance with our normal practice, a valuation exercise was undertaken by Knight Frank LLP at 31 March 2009 to review the net realisable values of our trading properties and this resulted in a £92.3m impairment (£104.6m including joint ventures). The impairment primarily applied to development land and infrastructure programmes, mainly at Ebbsfleet Valley in Kent.

### Interest rate swaps

We use interest rate swaps to manage our interest rate exposure as described in the paragraph on hedging below. The significant fall in interest rates this year has resulted in a charge to the income statement of £102.1m, representing the change in market value of these swaps over the year (£117.5m including joint ventures).

### Revenue profit

Revenue profit is our measure of the underlying pre-tax profit of the Group, which we use internally to assess our performance. It includes the pre-tax results of our joint ventures but excludes capital and other one-off items.

[Table 13](#) shows the composition of our revenue profit including the contributions from London and Retail.

**Table 13**

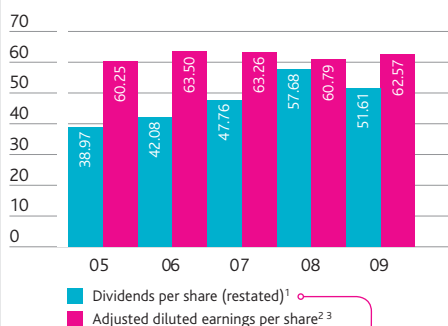
### Revenue profit

	Retail Portfolio £m	London Portfolio £m	31/03/09 £m	Retail Portfolio £m	London Portfolio £m	31/03/08 £m
Gross rental income <sup>1</sup>	374.6	352.8	727.4	370.6	342.5	713.1
Ground rents	(12.1)	(4.6)	(16.7)	(11.3)	(5.3)	(16.6)
Net service charge and property costs	(44.0)	(18.6)	(62.6)	(25.3)	(19.8)	(45.1)
Indirect costs	(38.9)	(35.8)	(74.7)	(40.7)	(36.0)	(76.7)
<b>Combined segment profit</b>	<b>279.6</b>	<b>293.8</b>	<b>573.4</b>	<b>293.3</b>	<b>281.4</b>	<b>574.7</b>
Unallocated expenses			(14.2)			(13.0)
Net interest – Group			(217.9)			(255.9)
– joint ventures			(26.4)			(21.0)
<b>Revenue profit</b>			<b>314.9</b>			<b>284.8</b>

1. Includes finance lease interest.

**Chart 14**

### Dividends and adjusted diluted earnings per share (p)



Gross rental income increased by £14.3m over last year, which was mainly due to purchases since 1 April 2007 and development properties, such as our schemes at Exeter, Bristol, Bankside and New Street Square. This was partially offset by a reduction in rental income from the net sales of investment properties. The increase in net service charge and property costs of £17.5m reflected the tougher climate facing our retail customers, with higher void costs and empty rates as well as an increase in our bad debt provisions and write off of pre-development costs.

Net interest expense was £32.6m lower than last year, reflecting lower average net debt over the period following disposals and lower interest rates particularly in the second half of the year.

### (Loss)/earnings per share

The basic loss per share from continuing activities was 918.0p, compared to a loss per share of 188.4p last year, the change being predominantly due to the revaluation deficit on the investment property portfolio (791.7p per share).

In the same way that we adjust profit before tax to remove capital and one-off items to give revenue profit, we also report an adjusted earnings per share figure. Adjusted diluted earnings per share from continuing activities increased by 2.9% from 60.8p per share for the year ended 31 March 2008 to 62.6p per share in the current period [Chart 14](#). This increase was largely attributable to reduced interest on borrowings but was lower than the increase in revenue profit due to a prior year tax benefit in last year's results.

#### Notes:

- The restated total dividend payable represents the theoretical dividend per share that would have been paid had the bonus shares inherent in the Rights Issue been in existence at the relevant dividend dates.
- The earnings per share for the years ended 31 March 2008, 31 March 2007, 31 March 2006 and 31 March 2005 have been adjusted for the bonus element inherent in the Rights Issue that was approved on 9 March 2009.
- The earnings per share for 2005 to 2007 includes the operating results of Trillium. 2008 and 2009 exclude the operating results of Trillium as these have been reclassified as discontinued operations.

## Property Income Distribution (PID)

Who can claim exemption from deduction of withholding tax on Property Income Distributions<sup>1</sup>?

- UK companies
- Charities
- Local Authorities
- UK Pension Schemes
- Managers of PEPs, ISAs and Child Trust Funds

Who is unlikely to be able to claim exemption from deduction of withholding tax on Property Income Distributions?

- Overseas shareholders<sup>2</sup>
- Individual private shareholders

1. See Total dividend information on how eligible shareholders can claim exemption.
2. May be able to reclaim some or all of the withholding tax under relevant double taxation treaty.

For further explanation of Property Income Distributions and Dividend Reinvestment Plan. [p140-141](#)

### Total dividend

We are recommending a final dividend payment of 7.0p per share. Taken together with the three quarterly dividends of 14.9p, our full year dividend will be 51.6p per share (2008: 57.8p) which represents a 10.5% reduction. These amounts have been restated to include the bonus factor inherent in the Rights Issue.

[Table 15](#) shows the dividend per share at the time of payment as well as the restated amount.

Our final proposed dividend of 7.0p is the amount we indicated at the time of our Rights Issue, when we explained that we were resetting our dividend to a lower base. It is also the amount we anticipate paying as our quarterly dividend throughout the next financial year. On an annualised basis, this will reduce our dividend from around £307m to £212m.

The table below sets out the percentage of dividends paid and payable which comprise Property Income Distributions (PID) from REIT qualifying activities. The PID element is subject to 20% withholding tax for relevant shareholders. Taking into account the proposed final dividend, the Group is expected to have satisfied its minimum PID requirement for 2008/09.

The Company offers shareholders the option to participate in a Dividend Reinvestment Plan (DRIP). For further details, please refer to the Shareholder centre within the Investor section of our corporate website [www.landsecurities.com](http://www.landsecurities.com).

[Table 15](#)  
Dividends

	Property Income Distribution (PID) pence	Non-property Income Distribution pence	Total pence	Total pence (restated)
First quarterly dividend (paid on 24 October 2008)	14.85	1.65	16.50	14.87
Second quarterly dividend (paid on 12 January 2009)	16.50	–	16.50	14.87
Third quarterly dividend (paid on 24 April 2009)	16.50	–	16.50	14.87
Final dividend (payable on 24 July 2009)	7.00	–	7.00	7.00
Total dividend for the year	54.85	1.65	56.50	51.61

### Net assets

At 31 March 2009, net assets per share was 639p, a decrease of 1223p compared to the year ended 31 March 2008. The reduction in our net assets was primarily driven by the lower value of our investment property portfolio, the impairment of trading properties and the loss on disposal of Trillium.

In common with other property companies, we calculate an adjusted measure of net assets which we believe better reflects the underlying net assets attributable to shareholders. Our adjusted net assets are lower than our reported net assets primarily due to an adjustment to our debt. Under IFRS we do not show our debt at its nominal value, although we believe it would be more appropriate to do so, and we therefore adjust our net assets accordingly. At 31 March 2009, adjusted diluted net assets per share were 593p per share, a decrease of 1170p or 66.4% from 31 March 2008.

[Table 16](#) summarises the main differences between net assets and our adjusted measure together with the key movements over the year.

[Table 16](#)  
Net assets attributable to equity holders of the Company

	2009 £m	2008 £m
Net assets at the beginning of the year	9,582.9	10,791.3
Adjusted earnings	325.0	314.6
Revaluation deficits on investment properties	(4,743.7)	(1,292.6)
Impairment of development land and infrastructure	(104.3)	–
(Losses)/profits on non-current asset disposals	(127.9)	50.2
Other	(119.5)	(45.1)
Loss after tax attributable to equity holders of the Company	(4,770.4)	(972.9)
(Loss)/profit on discontinued operations	(420.9)	142.1
Dividends paid	(302.4)	(308.4)
Rights Issue	755.7	–
Other reserve movements	(21.4)	(69.2)
Net assets at the end of the year	4,823.5	9,582.9
Mark-to-market on interest rate swaps	150.2	12.7
Debt adjusted to nominal value	(499.8)	(511.5)
Adjusted net assets at the end of the year	4,473.9	9,084.1

Note: To the extent tax is payable, all items are shown post-tax.

### Net pension surplus

The Group operates a defined benefit pension scheme which is closed to new members. At 31 March 2009 the net surplus was £3.0m. This was £8.0m lower than the surplus recognised at 31 March 2008, primarily due to lower than expected returns on scheme assets.

The key assumptions behind this surplus are shown in note 33 to the accounts, together with related sensitivities.

### Cash flow, net debt and gearing

During the year, net debt decreased by £1,460.9m to £3,923.6m. This was primarily driven by proceeds from the disposal of investment properties (£823.0m), the disposal of Trillium (£492.6m) and proceeds of £755.7m from the Rights Issue. Capital expenditure in the year was £515.9m, which was £895.9m below last year, reflecting a decrease in expenditure on developments and very few investment property acquisitions following the slowdown in the commercial property market.

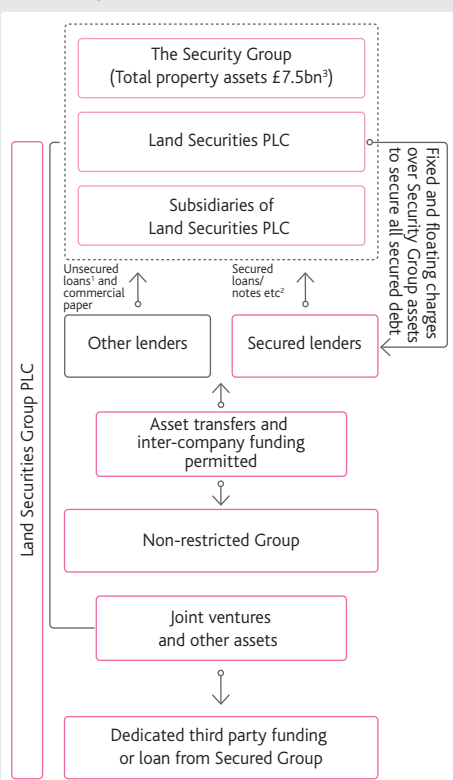
We invested a net £117.0m in our joint ventures, mainly on shopping centre developments in Bristol and Cardiff. The development in Bristol was completed and opened in September 2008. The Cardiff development is scheduled to complete in October 2009.

**Table 18**  
Gearing

	31/03/09 %	31/03/08 %
Gearing – on book value of balance sheet debt	81.4	56.2
Adjusted gearing*	96.4	64.9
Adjusted gearing* – as above plus notional share of joint venture debt	105.9	67.6
Group LTV	52.0	42.6

\*Book value of balance sheet debt increased to recognise nominal value of debt on refinancing in 2004 divided by adjusted net asset value.

**Chart 19**  
Funding structure



- Limited to the higher of £150m or 2% of total collateral value.
- The borrower under the Secured Bank facility is LS Property Finance Company Limited. Notes are issued from Land Securities Capital Markets PLC. Commercial paper is issued from Land Securities PLC.
- Source: Knight Frank LLP Valuation Report for 31 March 2009.

**Table 17**  
Cash flow and net debt

	Year ended 31/03/09 £m	Year ended 31/03/08 £m
Operating cash inflow after interest and tax (excluding REIT conversion charge)	367.2	315.4
REIT conversion charge	–	(316.2)
Dividends paid	(302.4)	(308.4)
Non-current assets:		
Acquisitions	(86.1)	(1,192.1)
Disposals	823.0	1,080.7
Investment in finance leases	–	(82.1)
Capital expenditure	(429.8)	(545.7)
	307.1	(739.2)
Trillium disposal:		
Gross proceeds	444.0	–
Net debt divested	48.6	–
	492.6	–
Loans advanced to third parties	(50.0)	–
Receipts from discontinued activities	–	424.9
Receipts from the disposal group (part of Trillium's PPP activities)	113.5	441.0
Joint ventures and associates	(117.0)	(0.2)
Purchase of own share capital	–	(87.6)
Proceeds from the Rights Issue	755.7	–
Fair value of interest rate swaps	(105.6)	(21.0)
Other movements	(0.2)	(5.3)
Decrease/(increase) in net debt	1,460.9	(296.6)
Opening net debt	(5,384.5)	(5,087.9)
Closing net debt	(3,923.6)	(5,384.5)

Our interest cover, excluding our share of joint ventures, has increased from 1.65 times in 2008 to 1.91 times in 2009. Under the rules of the REIT regime, we need to maintain an interest cover in the exempt business of at least 1.25 times to avoid paying tax. As calculated under the REIT regulations, our interest cover of the exempt business for the year to 31 March 2009 was 1.62 times.

Although net debt has decreased, gearing has increased, principally due to the impact of falling property values on our equity. Details of the Group's gearing are set out in Table 18, which also shows the impact of joint venture debt, although the lenders to our joint ventures have no recourse to the Group for repayment.

Adjusted gearing, which recognises the nominal value of our debt, increased from 64.9% at 31 March 2008 to 96.4% at 31 March 2009. Adjusted gearing including our share of joint ventures increased from 67.6% to 105.9% over the same period. In common with other property companies, we also show our Group LTV ratio.

### Financing strategy

The Group monitors and adjusts its capital structure with a view to promoting the long-term success of the business and maintaining sustainable returns for shareholders. A key element of the Group's capital structure is that the majority of its borrowings are secured against a large pool of our assets (the Security Group) determined by levels of LTV and Interest Cover Ratios (ICR), although it is LTV which is the more likely determinant of which operating environment applies. These ratios do not trigger an event of default until LTV exceeds 100% or historic or projected ICR is less than 1.0 times. However, our operating environment becomes more restrictive at higher levels of LTV/lower levels of ICR. There are minimal operational restrictions on the Group in Tier 1 (LTV below 55%) and Tier 2 (LTV: 55% to 65%). The main additional operating restriction in Tier 2 is the requirement to maintain a level of prescribed liquidity or pre-pay debt by amortisation (includes actual repayment and collateralisation), calculated on a 25-year mortgage annuity basis. In Initial Tier 3 (LTV: 65% to 80%), our operating environment would be more restrictive with provisions designed to encourage a reduction

in gearing including mandatory debt amortisation. Furthermore, none of the Group's credit facilities permit the drawing of additional funds if the Group is in Initial Tier 3. As there was a risk of our moving into Initial Tier 3 if property values continued to decline rapidly, we took the decision to draw down our available facilities in early 2009 as outlined in more detail below.

The last two years have seen an unprecedented period of instability in the financial markets which has severely impacted investor confidence, the availability and pricing of credit, and the pricing of property investments. During the last quarter of 2008, the pace of valuation decline exceeded the pace at which assets could be sold to counteract the impact of falling values on the Group's balance sheet position. This deterioration had an adverse effect on the Group's LTV ratios and lay behind the decision to raise £755.7m through a Rights Issue.

#### Rights Issue

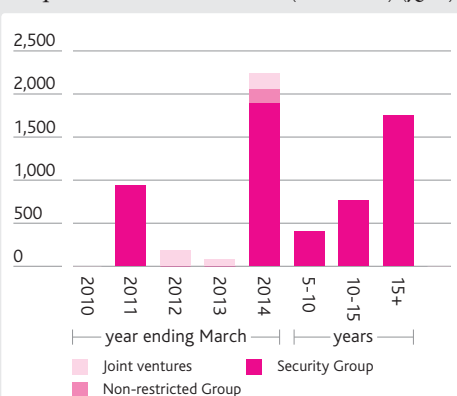
On 19 February 2009, the Group announced its intention to raise £755.7m (net of expenses) by way of a Rights Issue of 290,773,925 new ordinary shares at 270 pence per share on the basis of five new ordinary shares for every eight existing ordinary shares.

The Rights Issue was approved by shareholders in a General Meeting on 9 March 2009, nil-paid rights began trading the following day and proceeds were received shortly before the year end.

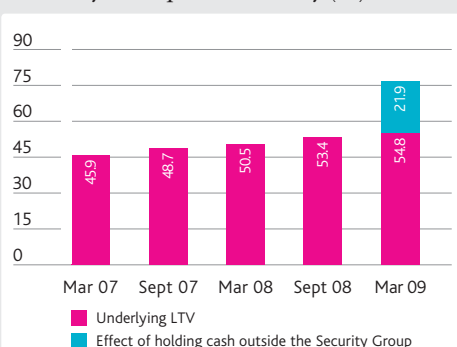
As the Land Securities closing share price on 9 March (380p) exceeded the subscription price of 270p, the Rights Issue is deemed to include a bonus element of 11.0%. As a result, all 'per share' information which pre-dates the Rights Issue is reduced by 9.0% (ignoring the restatement of the 2008 results due to the disposal of Trillium).

Read more about the Rights Issue. >p27

**Chart 20**  
Expected debt maturities (nominal) (£m)



**Chart 21**  
Security Group LTV history (%)



#### Financing and capital

Over the last 12 months, we continued to focus on our cash flows, the level of available bank credit facilities and the maturity of our debt **Chart 20**. During the year, we refinanced and extended our three existing committed bilateral facilities totalling £825m and established three new committed bilateral facilities totalling £115m. All the bilateral facilities, with the exception of a £40m facility, mature in the period from July to December 2010, with an option to extend the maturity for a further year. The ability to refinance existing facilities and negotiate new facilities against the current financial and economic backdrop, owes much to the quality and level of assets within the Security Group against which these facilities and Group bonds are secured, as well as the importance we place on our bank relationships. The average duration of the Group's debt is 9.7 years with a weighted average cost of debt of 4.1%.

In January 2009 the Group drew down £1.1bn of available credit facilities to ensure liquidity and provide operational flexibility by holding the funds outside the Security Group. At 31 March 2009 our net borrowings (including joint ventures) amounted to £4,732.6m, of which £2,298.6m was drawn under our syndicated and bilateral bank facilities and £57.8m related to finance leases. Committed but undrawn facilities amounted to £489.2m of which £300m cannot be drawn if we are operating in Initial Tier 3. In the Security Group, £5,720m of debt was secured against £7,453.3m of assets, giving a Security Group LTV ratio of 76.7%, up from 50.5% at 31 March 2008 **Chart 21**. As a result, we will enter Initial Tier 3 when the Security Group valuation report for 31 March 2009 is submitted.

Although the March valuation report shows a sharp decline in property values, it was the decision to draw down existing bank facilities and to hold high levels of cash outside the Security Group for liquidity reasons, which will result in this tier change. At 31 March 2009, the Group had cash and short-term instruments of £1,596.5m outside the Security Group. This cash is available to be injected into the Security Group to maintain its LTV at less than 80% to prevent it entering Final Tier 3. Our current cash holding provides the Group with protection against further valuation declines and the option to deploy capital should suitable opportunities arise. If all our cash and cash equivalents at 31 March 2009 had been injected into the Security Group, the Security Group LTV would have been 55.3% (Tier 2 regime). It is our intention to migrate back to a Tier 1 or 2 covenant regime in the medium term.

#### Hedging

We use derivative products to manage our interest rate exposure, and have a hedging policy which requires at least 80% of our existing debt plus our net committed capital expenditure to be at fixed interest rates for the coming five years. Specific hedges are also used in geared developments or joint ventures to fix the interest exposure on limited-recourse debt. At 31 March 2009, we had £2,672.0m of hedges in place. Our debt (net of cash and cash equivalents and including joint ventures) was 107% fixed. The slightly over-hedged position at the year end arose due to the receipt in March 2009 of the Rights Issue proceeds of £755.7m. Without the Rights Issue proceeds, we would have been 93.0% hedged.

#### Taxation

As a consequence of the Group's conversion to REIT status, income and capital gains from our qualifying property rental business are now exempt from UK corporation tax. The tax charge for the year of £0.5m (2008: £15.1m credit) comprises a prior year corporation tax charge of £0.3m and a net deferred tax charge of £0.2m. The tax loss arising on the write-down of trading properties below cost has eliminated taxable profits on all residual taxable activities in the period. No tax charge arose in respect of the disposal of Trillium.