

## Our risks and how we manage them

### Financial risks

We achieved over £500m of property sales in a deteriorating market.

Risk description	Impact	Mitigation
<b>Capital structure</b> <ul style="list-style-type: none"> <li>▪ Pace of valuation decline continues to exceed the pace at which assets can be sold.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Unable to counteract the impact of falling values on the Group's balance sheet.</li> <li>▪ Unable to progress investment opportunities.</li> </ul>	<ul style="list-style-type: none"> <li>▪ The Rights Issue strengthened the Group's balance sheet and will reduce the potential impact of prolonged falls in property values and position the Group to respond quickly to the turning point in the cycle.</li> <li>▪ Rights Issue strengthened the Group's position in refinancing its debt facilities.</li> <li>▪ Liquidity and gearing kept under constant review.</li> <li>▪ Wide variety of assets and knowledge of investor appetite ensure best possibility of achieving disposals.</li> <li>▪ Development commitments matched to sales.</li> </ul>
<b>Credit risk</b> <p>Investment counterparty risk</p> <ul style="list-style-type: none"> <li>▪ Failure of bank and financial institution counterparties.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Loss of cash and deposits.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Only use independently-rated banks and financial institutions with a minimum rating of A.</li> <li>▪ Weekly review of credit ratings of all financial institution counterparties.</li> <li>▪ Group Treasury ensures that funds deposited with a single financial institution remain within the Group's policy limits.</li> </ul>
<b>Liquidity risk</b> <ul style="list-style-type: none"> <li>▪ Restrictive covenant regime.</li> <li>▪ Limited market debt capacity.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Inability to fund operations and capital expenditure programme.</li> <li>▪ Inability to raise sufficient new funding.</li> </ul>	<ul style="list-style-type: none"> <li>▪ As at 31 March 2009, £1.6bn of cash and short-term deposits were held outside the Security Group. This balance is available to be injected into the Security Group to maintain its LTV at less than 80% to avoid entering Final Tier 3 with its additional financial and operational restrictions.</li> <li>▪ No financial covenant default is triggered until the applicable LTV ratio exceeds 100% or the ICR is less than 1.0.</li> <li>▪ Assets available within the Security Group to sell/raise new debt.</li> <li>▪ Ongoing monitoring and management of the forecast cash position.</li> <li>▪ Commitments are not taken on if funding is not available.</li> </ul>
<b>Market risk</b> <ul style="list-style-type: none"> <li>▪ Market risk exposure through interest rates, currency fluctuations and availability of credit.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Increased borrowing costs.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Group Treasury monitors compliance with the Group hedging policy.</li> <li>▪ Specific hedges used in geared joint ventures to fix the interest exposure on limited recourse debt.</li> <li>▪ Forward purchases of foreign currency to fix the Sterling value for any construction works not priced in Sterling.</li> </ul>
<b>Tax risk</b> <ul style="list-style-type: none"> <li>▪ Compliance with the Real Estate Investment Trust (REIT) taxation regime.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Increased tax payable.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Ongoing monitoring and management of the criteria to meet REIT status.</li> </ul>

Read how we have mitigated risk by widening the appeal of One New Change, EC4. > p33

# Property investment risks

Risk description	Impact	Mitigation
<h3>Occupier market conditions</h3> <ul style="list-style-type: none"> <li>▪ Prolonged downturn in tenant demand.</li> <li>▪ Reduced consumer spending leading to lower retail sales.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Threat of voids in the portfolio.</li> <li>▪ Cutbacks in retailer opening programme.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Committed development exposure limited to remaining space in St David’s 2 in Cardiff together with One New Change (due to complete in 2010) and Dashwood House in London. Other proposed developments are not committed and will only commence when market conditions are favourable or a pre-let of part is in place.</li> <li>▪ Void management through temporary lettings and void mitigation strategies. Large portfolio allows portfolio leasing deals and flexibility to further reduce voids.</li> <li>▪ Pre-letting of key units before committing to development. Limited Retail development pipeline concentrated primarily in Cardiff; most other schemes completed and substantially let already.</li> <li>▪ Ongoing sales programme to divest schemes and locations most likely to suffer adverse impact.</li> </ul>
<h3>Market cycles</h3> <ul style="list-style-type: none"> <li>▪ Property markets are cyclical.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Risks of negative interaction between falling property values and balance sheet gearing.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Target ranges for balance sheet gearing.</li> <li>▪ Secure income flows under UK lease structure.</li> </ul>
<h3>Property risk</h3> <ul style="list-style-type: none"> <li>▪ Asset value concentration.</li> <li>▪ Increased cost exposure on voids.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Poor performance of a single asset having material impact on overall performance.</li> <li>▪ Increase in void costs.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Large multi-asset portfolio.</li> <li>▪ Largest property (Cardinal Place) represents only 5.8% of combined portfolio.</li> <li>▪ Average investment property lot size of £44.6m.</li> <li>▪ Retail assets combine a range of highly diversified income streams in all major sub-sectors of retail property.</li> <li>▪ Void management and empty rates mitigation.</li> </ul>
<h3>Tenant risk</h3> <ul style="list-style-type: none"> <li>▪ Tenant concentration and failures.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Impact on revenue if a major occupier fails or does not renew leases.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Diversified tenant base.</li> <li>▪ Strong established locations and relationships with occupiers.</li> <li>▪ The Government is our largest single customer, representing 9.5% of gross rents; the next largest represents 4.2%.</li> <li>▪ Of our income, 72% is derived from tenants who make less than a 1% contribution to rent roll.</li> <li>▪ Regular credit review of major tenants.</li> </ul>
<h3>Health, safety and environmental risk</h3> <ul style="list-style-type: none"> <li>▪ Responsibility for the safety of visitors to our properties and our environmental performance.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Impact on reputation or potential criminal proceedings resulting in financial impact.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Annual cycle of health and safety audits.</li> <li>▪ Quarterly Board reporting.</li> <li>▪ Dedicated specialist personnel for environment and health and safety.</li> <li>▪ Established policy and procedures including award-winning health and safety system and ISO 14001 certified environmental system.</li> <li>▪ Active environmental programme addressing key areas of impact (energy and waste).</li> </ul>

Read more about our commitments and performance in this area. > p54-63

## Property development risks

Risk description	Impact	Mitigation
<p><b>Site assembly risk</b></p> <ul style="list-style-type: none"> <li>Third-party interests in part of site cannot be acquired.</li> </ul>	<ul style="list-style-type: none"> <li>Unable to progress development either in time, at all, or in budget.</li> </ul>	<ul style="list-style-type: none"> <li>Policy of buying into all or part of future development sites early as income-producing investments.</li> <li>Experience of Compulsory Purchase Order procedures.</li> </ul>
<p><b>Planning risk</b></p> <ul style="list-style-type: none"> <li>Development proposals fail to gain sufficient support and therefore planning consent.</li> </ul>	<ul style="list-style-type: none"> <li>Unable to progress developments in a timely manner.</li> </ul>	<p>Development expertise including:</p> <ul style="list-style-type: none"> <li>Skilled development management teams.</li> <li>Public consultation capabilities.</li> <li>Long-standing relationships with key development stakeholders.</li> <li>Reputation.</li> </ul>
<p><b>Construction risk</b></p> <ul style="list-style-type: none"> <li>Construction cost overruns or poor management of construction.</li> <li>New and different procurement methodologies and contract forms for London.</li> <li>Supplier capacity, capability and financial stability.</li> </ul>	<ul style="list-style-type: none"> <li>Returns are eroded by cost overruns or project completion is delayed.</li> <li>Different risk profiles and unfamiliar terms and conditions.</li> <li>Cost in excess of assumptions in appraisal.</li> <li>Lack of competition in tendering process.</li> <li>Poor supplier performance.</li> </ul>	<ul style="list-style-type: none"> <li>Transfer of risk to specialist contractors.</li> <li>Skilled in-house project management teams.</li> <li>Use of specialist advisers.</li> <li>Contingency provision in appraisals.</li> <li>Forward purchase of high inflation risk items.</li> <li>Closer, more open relationship with the supply chain.</li> </ul>
<p><b>Letting risk</b></p> <ul style="list-style-type: none"> <li>Development remains unlet after completion or fails to meet lettings target.</li> <li>Tenant requirement for incentive packages, including capital, increasing.</li> </ul>	<ul style="list-style-type: none"> <li>Impact on income and valuation.</li> </ul>	<ul style="list-style-type: none"> <li>Experienced and skilled in-house leasing teams.</li> <li>Risk evaluation model to assess earnings impact of developments remaining unlet.</li> </ul>