

## Land Securities

### Overall performance

**Q: At the interim results you said your priorities were to focus on balance sheet management, leasing to maximise income, all the while keeping an eye on the future and the recovery of occupational market. So how would you say you've done?**

A: [Francis Salway: FS] Well, at the time when values are falling very rapidly, balance sheet management becomes the priority. And in a year when there was limited liquidity in markets, we were very pleased to have achieved over £1.1bn of disposals, and that flowed on from £1.6bn of disposals in the previous year. And of course we had the Rights Issue when we raised £756m. So the effect of the actions this year has been to reduce our net debt by 27 per cent. That's a material change.

What it means is we've restored LTV ratios on our balance sheet, we've given ourselves cash liquidity facilities to meet maturing debt facilities and, as we look forward, we've got some capacity to take advantage of opportunity.

In terms of leasing activity, the key is always on developments. We completed four projects last year and they are now 72 per cent let, which we regard as being a good outturn for 2008/2009.

**Q: But you have generated the largest loss in the Company's history, and you've had to cut the dividend, so you must be disappointed by that.**

A: [FS] We recognise that this has been the year when there's been the sharpest falls in value on record for UK commercial property, and we've not been immune to that. And because valuation change now flows through to our pre-tax profit or loss, that has resulted in us announcing a substantial loss.

In terms of dividend, we went to our shareholders to raise more capital in spring of this year. And we're very conscious that at the time of asking for more capital we should give clarity on future outlook for dividend. We do think there will be some negative pressures on income so we've reset dividend at a level that we think will be sustainable and, ultimately, will allow future growth.

**Q: And, Martin, what, for you, are the key financial points?**

A: [Martin Greenslade: MG] Let me start by saying that the numbers that I'm going to explain have been restated for the Rights Issue and Trillium has been removed from the numbers as a discontinued operation following its sale.

But from continuing operations our pre-tax loss for the year was £4.77bn, and that's on the back of this valuation deficit of £4.74bn. Now at the revenue profit level, or our underlying pre-tax profit level, we saw an increase of just over 10 per cent, to £314.9m, and that's broadly on the back of lower interest charges. At the adjusted net asset level, we came in at 593p per share, and that was down just over 66 per cent on the year.

**Q: Looking at performance, you have underperformed the IPD index whereas, at the half year, you outperformed the benchmark, so why that swing in performance?**

A: [FS] A lot of it's down to the mix of our assets because, as you know, we're concentrated on shopping centres, retail warehouses and London offices. Those were the three weakest performing sectors of the UK commercial property market during the year. Our London offices and London Retail actually outperformed IPD. We were under in our Retail outside London. A lot of that was down to developments and development sites.

But if we take a slightly longer-term perspective, you'll remember that we outperformed very significantly last year. So over the two-year period, we're still ahead.

**Q: And, Martin, that decline in property values resulted in a more restrictive operating environment. So what's that doing to the business?**

A: [MG] First of all, it doesn't come as a surprise to us. We will move into a more restrictive operating environment in terms of our debt as we enter initial Tier 3. We precipitated that by drawing down on our debt facilities, and the reason we did that is to provide us with maximum flexibility. And we now have £1.6bn worth of cash sitting outside our security group and available for us to use.

In terms of the more restrictive operating environment that you refer to, it is more restrictive in the sense that we can't draw on any facilities that remain undrawn. But we can still do all of the things that property companies do, namely, buy assets, sell assets, develop assets, and we can still pay dividends from the security group.

**Q: And how long are you prepared to operate at this level? And do you have the cash to meet the £600m worth of capital expenditure that you talked about at the time of the Rights Issue?**

A: [MF] Since the Rights Issue we have managed that £600m of committed development capital expenditure down to the current figure of £370m. In terms of whether or not we have sufficient cash to meet that, we have £1.6bn of cash that we can use as we see fit, and so part of it can be used for that development CapEx.

**Q: And disposal activity picked up in the second half of the year. Should we expect this to continue? And to what extent is that distress selling?**

A: [FS] We were very clear at the time of the Rights Issue that we would match capital expenditure on developments and generally on the portfolio with continuing disposals - that is what we're seeing. But based on the data we've been talking about on our balance sheet, it certainly isn't distress selling.

## **Demerger, sale of Trillium and Rights Issue**

**Q: You've mentioned the sale of Trillium in January. It was at a large loss, so was that the right decision?**

A: [FS] We'd come to the view that Trillium wouldn't form part of the Group going forward in the long term. And to crystallise a sale at that stage in the cycle to strengthen our balance sheet was enormously valuable to us. And as we look back over that period we can see that it was one of the largest transactions that took place.

**Q: And it has been a year of significant corporate activity for you with the Rights Issue as well, so can we just be sure, is the demerger out of the question now?**

A: [FS] We made a very clear announcement at our interim results presentation in November last year that we'd stopped work on the demerger and it is off the agenda. We're focused on two best-in-class businesses covering London offices and Retail, where we've got unrivalled occupier relationships. And we think that having coverage of the two largest sectors in the UK commercial property market - London offices and Retail - will give us a real breadth of opportunity over the next couple of years.

**Q: And, Martin, on that Rights Issue, it generated £756m in net proceeds for the business, so what were the reasons again for that Rights Issue? And what will you do with the cash?**

A: [MG] Let me explain. We entered the financial year having made disposals of £1.6b. During the course of this financial year we either extended existing bank facilities or put in place new bank facilities over £1b. We continue to make assets sales and we sold the Trillium business. So we did many actions to protect our balance sheet. But in the second half of the year we saw values fall at such a rate that we couldn't make disposals to keep up with that.

To give you an example, our assets fell by 25 per cent just in the second half of the year. So in January we went to our shareholders. I'm delighted to say that our Rights Issue was extremely well supported by them. And that's when we raised the £756m you refer to.

**Q: And you are confident that you have enough flexibility now to deal with anything the market throws at you?**

A: [MG] We've got £1.6bn of cash that's available to us to use, so I'd say that's a considerable degree of flexibility either to protect our balance sheet by paying down debt facilities, or to use that cash to take advantage of opportunities that will arise over the coming months and years.

## **Business performance**

**Q: Looking at the businesses in more detail, how resilient are the London and Retail portfolios? What are we seeing in terms of increase in occupiers going into administration, for example?**

A: [FS] The UK lease structure generally gives great resilience in terms of income. But we have to accept that during an economic downturn there is pressure on income. As we've commented before, the pressure generally comes from insolvencies in the retail sector and, in London Offices, from lower renewal rates on lease expiry.

So if we look first at units going into administration, it was just over 5.5 per cent in our Retail portfolio, but much, much lower in London Offices - only 0.3 per cent. So, across the business as a whole, 3.7 per cent of our income is in administration, but 60 per cent of those units are still occupied and, in the Retail sector, trading.

In terms of London Offices and renewal rates, we're very pleased that, where we've had lease expiries or break clauses over the last year, we've had as much as 73 per cent either renewed, re-let or continued ongoing discussions with the tenant who's still in occupation.

**Q: And looking at lease expiries, Martin, to what extent does that put rental income at risk?**

A: [MG] I think what we will see in the coming years, we will see pressure on our top line rental income. We're going to see that from a number of factors. We're going to see it from voids. We're going to see it from the impact of voids, which is service charge costs that aren't recovered and empty rates.

We're also going to see an impact from sales that we make to fund our development capital expenditure, because we will continue to make sales and so that will reduce some of our income. We will see also an impact from pausing on our development pipeline in certain properties, where we'll see interest no longer capitalised, so all of these factors are going to have an impact on our overall income. But do bear in mind we took that into account when we rebased the dividend.

**Q: And, as Martin says, you're pausing some of your development, so why have you put a stop to the Leeds development? And what else can you tell us about your development activity?**

A: [FS] If I start with a scheme that's current at the moment, which is the development we're doing with Liberty in Cardiff St David's 2, we're now, by income, 50 per cent let or in solicitors' hands and we've seen a pickup in level of interest from retailers, which we think will continue in the run up to opening, and after opening.

In Leeds we've announced that we'll be deferring the likely completion date of that scheme, and we're seeking to put in place a degree of pre-letting before we start construction.

**Q: And how have pre-packs, the move to monthly rents, the reduction in service charges affected the business?**

A: [FS] I think it is all-round flexibility. This is the sort of time in the cycle when you show flexibility in terms of your dealings with your key occupiers. So, yes, we have offered monthly rents to a number of retailers, but on a basis that gives us some benefits. We have also taken the lead in seeking to reduce service charges. But that's what businesses do in this environment - they try and reduce the cost base. And, do remember, we're a beneficiary to the extent there's vacant units in a property - it's lower service charge outgoings for us as well.

And on pre-packs it has to be the right thing to get some continuity of business where one can. The issue is whether there is fair treatment between different landlords. And I think the industry as a whole has made real steps towards getting more equal treatment of the various creditors.

**Q: And these moves are examples of what you mean by maximising income in these difficult times?**

A: [FS] They're some examples, but the key thing is getting lettings. And one statistic that I think might surprise people, after we've had so much negative press comment on the retail sector, is over the last year we did just under 300 Retail lettings- that is what is maximising income.

## **Debt and cash**

**Q: With the intention at the date of the Rights Issue to keep the cash outside of your debt structures, why, then, did you pay down £300m worth of debt in March?**

A: [MG] That £300m of debt relates to cash that we drew from our existing bank facilities before the Rights Issue. And what we have now is £1.6bn of cash sitting outside the security group. And what we have to do is balance the flexibility of holding that cash in cash form against the cost of doing that. And we took the view that that £300m would not be used before it needed to be repaid to the bank as those facilities mature.

**Q: And what else can you tell us about the profile of your debt maturities?**

A: [MG] We have £640m of bank facilities that mature in the 2010 calendar year. Now all of those facilities can be pushed out for a further year, so to between July and December 2011.

**Q: And do you have enough earnings to cover the dividend?**

A: [MG] We don't set out to have a specific level of earnings cover. But at the time of the rights issue, when we reset the dividend level, the 7p per quarter dividend translates to an annual amount of around £212m. That compares with the £314.9m of revenue profit that we've just announced for the year past. So you can see that there's plenty of headroom there for the types of pressures that I've just outlined that will come through on rental income.

## Outlook

**Q: And, Francis, given the limited visibility, what's your outlook for the year ahead?**

A: [FS] The first thing I'd say is that the change in property values and in market sentiment since we announced our Rights Issue has been as we expected and as we modelled. And I think we're beginning to see a two-way pull.

The higher yields available on property are now beginning to attract investor interest on the best let properties. On the other hand, the economy is weak, there is negative pressure on rents and rental values are falling. And on less well let properties that's feeding through into falling capital values.

So it is to a degree, as we indicated at the beginning of the year, the trend in values is still negative but the pace of falls in values is slightly less rapid than it was. And as we look forward we will have a period when properties behave in slightly different ways, according to sector and according to characteristics. And in terms of opportunity, we're now in a flexible position. We are alive to potential opportunities, but we're also prepared to be patient.