CANARY WHARF GROUP PLC

Extract from the Report and Financial Statements of the Group for the year ended 31 December 2010. The 2010 Report and Financial Statements are currently being produced and will be distributed to Shareholders at a later date. The information in these extracts does not comprise statutory accounts within the meaning of the Companies Act 2006.

HIGHLIGHTS

- On 4 October 2010, **the Company paid an interim dividend of** 11.736p per share totalling **£75.0m.**
- **Net assets increased to £2,387.9m at 31 December 2010, an increase of** £332.5m or **16.2% from** £2,055.4m at **30 June 2010** and by £462.9m **or 24.0% from** £1,925.0m at **31 December 2009** The increases were partly attributable to the increase in value of the property portfolio and partly to the profit after tax for the year.
- **Adjusted NAV per share was £3.90 at 31 December 2010, an increase of** 22p or **6.0% from** £3.68 at **30 June 2010 and an increase of** 43p or **12.4%** from £3.47 **over the year.**
- **Adjusted NNNAV per share increased to £3.36 at 31 December 2010, up by** 19p or **6.0% from** £3.17 at **30 June 2010, and by** 5p or **1.5% from** £3.31 at **31 December 2009.**
- **The market value of the retained investment property portfolio increased by 4.7% to £4,638.5m** over the six months ended 31 December 2010 **and 9.7% since 31 December 2009.**
- Including development sites, **the market value of the retained property portfolio was £4,907.0m at 31 December 2010** against £4,694.5m at 30 June 2010 and £4,448.0m at 31 December 2009.
- **The weighted average initial yield for the office portfolio** valuation **was 4.8%** at 31 December 2010, an improvement of 20 bps since 30 June 2010. **The initial yield for the retail portfolio was 4.9%,** an improvement of 30 bps since 30 June 2010.
- **The weighted average equivalent yield for the office portfolio** valuation **was 5.2%** at 31 December 2010, an improvement of 50 bps since 30 June 2010 and 31 December 2009. **The equivalent yield for the retail portfolio was 5.4%,** an improvement of 30 bps since 30 June 2010 and 90 bps in the year.
- At 31 December 2010 **the Group's retained investment portfolio** totalling 6.9m sq ft **was 97.1% let** (31 December 2009 – 8.0m sq ft of which 96.2% was let including the Lehman building, as fully let).
- At 31 December 2010 **the weighted average unexpired lease term** for the retained investment portfolio **was 16.9 years** (or 15.7 years assuming the exercise of break options).
- **Operating profit** for 2010 **reduced to £179.2m from £281.4m**. **Profit after tax** for the year **increased to £168.2m** (2009 – £87.0m).
- **The Group completed the sale of 25 Bank Street to J.P. Morgan for** a gross consideration of **£495.0m and agreed** terms with AIG for **the termination of the rental cover facility** on the building **for** a receipt of **£144.5m.**
- **The sale of 5 Churchill Place was completed for** a total consideration of **£208.0m** reflecting an initial yield of 5.9%.
- **The Group acquired the substantial majority of the drawn balance under the Drapers Gardens** construction **loan** facility for £112.8m. **Subsequently** the joint venture entities which owned **Drapers Gardens sold** the property **for** a gross consideration of **£242.5m reflecting an initial yield of 5.2%** and the loan facility was repaid.
- **The Group entered** into **a joint venture with Land Securities for the development of 20 Fenchurch Street.**
- **The Group restructured existing leases and granted new leases to Barclays Capital over** a total of **1,152,000 sq ft,** consolidating the occupation of Barclays Capital from three into two buildings on the Estate.
- **The Group** also **concluded lettings of** approximately **187,000 sq ft to Shell and** further **lettings over an additional 200,000 sq ft** during the period.
- **The Group acquired 1 Park Place**, a building located adjacent to the Estate **for £17.5m** with two alternative planning permissions for 214,000 sq ft or 950,000 sq ft. **The Group** also **acquired the remaining interests in Heron Quays West** in June 2010, a site with planning consent for 1.3m sq ft of office space.
- **Further progress was made on the Crossrail station project** which continues to be on schedule and within budget.

RESULTS IN BRIEF

	2010 £m	2009 £m
Rental income (excluding adjustment for UITF 28)	**287.5**	318.4
Exceptional item:		
– write off of Lehman incentives	**(53.6)**	–
Operating profit	**179.2**	281.4
Exceptional items:		
– release impairment of investments in associates before interest and tax	**4.1**	13.8
– profit on sale of investment property	**158.8**	–
– termination of AIG facility	**144.5**	–
– breakage costs on interest rate swaps	**(46.9)**	–
– net (loss)/gain on repurchase of securitised debt	**(5.5)**	68.4
Profit on ordinary activities before tax	**219.7**	134.8
Profit before tax excluding exceptional items	**18.3**	52.6
Tax	**(51.5)**	(47.8)
Profit for the financial year	**168.2**	87.0
Dividend paid	**(75.0)**	–
Basic and diluted earnings per share	**26.3p**	13.6p

CHAIRMAN'S AND CHIEF EXECUTIVE'S STATEMENT

Introduction

Canary Wharf Group's operations throughout 2010 achieved success both at Canary Wharf and also in the City of London. Through a combination of sales and lettings, more than 2.5m sq ft of office transactions were completed on our properties at Canary Wharf, which are close to fully let (97.1%). During the year, the retail malls at Canary Wharf, which are also fully let, experienced increases in footfall, rent and turnover. Significant tenant demand remains.

Over the year, the overall market value of properties held for investment increased by £411.5m, or 9.7% to £4,638.5m. The market value of the offices alone increased by 8.0% whilst the market value of the retail portfolio increased by 25% over the year. Adjusted net asset value per share at 31 December 2010 rose to £3.90, a 12.4% rise over the year. Rental levels at Canary Wharf have remained stable, not having seen the volatility of office rental values experienced elsewhere in London over the last two years. Bearing in mind the diminished availability of Grade A office space in central London, we expect rental levels at Canary Wharf to increase in 2011.

Operational Review

Activities in Canary Wharf

The Group's largest single transaction was the sale at the year-end of 25 Bank Street to J.P. Morgan. This, together with the termination of the related AIG facility, produced an aggregate consideration of £639.5m. As part of this transaction, the Group will continue construction up to grade level at the JP Morgan Riverside South site where there is currently permission for development of up to 1.9m sq ft.

At the beginning of 2010, the Group sold 5 Churchill Place for £208.0m, demonstrating continued investment demand for the high quality Grade A assets which are the Group's particular strength and for which it is well known. Reflecting our confidence in future demand at Canary Wharf, we purchased the 1 Park Place site for £17.5m with a view to future redevelopment of this strategic site located at the heart of Canary Wharf. This site already has the benefit of two pre-existing planning consents for 214,000 sq ft and 950,000 sq ft respectively. This acquisition was followed by the purchase of the last two units to complete land assembly of the Heron Quays West site where there is an existing 1.3m sq ft planning consent.

Leasing activity at Canary Wharf was strong throughout 2010. We started the year with the restructuring and consolidation of leases to Barclays Capital, involving the extension of leases of 1.1m sq ft until 2032. A significant letting to a new arrival on our Canary Wharf Estate was to Shell, which leased 187,000 sq ft in 40 Bank Street. A further 200,000 sq ft was let to a variety of high quality tenants further diversifying the tenant mix on the Estate.

Taken together, the transactions involving Barclays Capital, Shell and J.P. Morgan represent a significant vote of confidence in the stability and future of London and Canary Wharf.

The occupation of the newly leased space and the arrival of J.P. Morgan staff will, during the next 12 months, increase the existing working population at Canary Wharf by more than 11,000, taking the total to over 105,000. This daily population will have obvious consequential benefits for the Group's retail operations. The increase in value of our existing retail property during the year reflected a 5.0% increase in footfall and the arrival of such names as Aquascutum, Tiffany & Co and Jaeger, all of whom opened new units at Canary Wharf. This was in spite of the weekend disruptions to service on the Jubilee line caused by continuing work on the still incomplete improvements to the signalling system.

The management of our retail assets continued to be active during the year, including the conversion of some car parking areas below shop level into new retail space for the expansion of existing units. This process is expected to continue and we are also pursuing further opportunities to extend the retail offering in order to respond to increasing demand for restaurants and shops.

Construction on the Estate importantly included the Group's building of the Crossrail station at Canary Wharf which is on schedule and on budget. A £350.0m funding agreement was signed for Transport for London ensuring funding is in place to complete this work by the Group. During the year the Government gave full backing to the Crossrail project and we are naturally pleased that this project, essential for the future prosperity of London, continues on schedule for completion in 2018.

Activities in the City

Our activity outside the Canary Wharf district was marked by the completion of the construction in the City of London of the Drapers Gardens joint venture development in which the Group had a 20% share. Construction of Drapers Gardens was managed by the Group and the building then let to BlackRock for a term of 25 years. In addition, the substantial majority of the loan facility for this development was purchased by the Group. Subsequently, our entire interest in this project was disposed of successfully. Reflecting the comprehensive nature of the Group's capabilities, all the elements which went into ensuring the success of this venture; construction, letting, loan acquisition and eventual sale, were handled by the Group.

In December the Group concluded a 50:50 joint venture agreement with Land Securities for what will be an iconic development at 20 Fenchurch Street, where construction has already started. The Group will be the sole construction manager of this project, as well as the joint development manager. In order to maintain flexibility to pursue future development opportunities, 35.0% of the project was syndicated on an equal pro rata basis to Qatar Holdings, China Investment Corporation, and Morgan Stanley Real Estate Special Situations Fund. The Group will retain in full, the profits from its role as construction manager and joint development manager.

Financial

Net assets increased from £2,055.4m at 30 June 2010 to £2,387.9m at 31 December 2010, an increase of £332.5m or 16.2%. Over the full year, net assets increased by £462.9m from £1,925.0m, an increase of 24.0%. These increases were attributable in part to the increase in the carrying value of the Group's investment portfolio by £369.7m and in part to the retained profit for the year. The increase since 30 June 2010 is also post the interim dividend of £75.0m paid in October 2010.

The recovery in the property market continued in the second half of the year, albeit at a slightly slower pace than in the first half. At 31 December 2010 the weighted average equivalent yield for the office property was 5.2%, an improvement of 50 bps since 30 June 2010. The weighted average equivalent yield for the retail portfolio hardened by 30 bps to 5.4%. These reductions in yields underpinned an increase in the carrying value of the retained investment portfolio of 4.9% since June, taking the increase for the year to 9.0%.

Adjusted NAV per share increased from £3.68 at 30 June 2010 to £3.90 at 31 December 2010, an increase of 22p or 6.0%. Over the full year, adjusted NAV per share increased by 12.4% from £3.47, an increase of 43p.

Profit before tax for 2010 was £219.7m in comparison with £134.8m for 2009. The results for 2010 were robust and included a number of exceptional items, in particular, the profit realised on sale of 25 Bank Street (£158.8m) and the amount received on termination of the related AIG facility (£144.5m). These exceptional profits were partially offset by the write off of Lehman incentives in the first half of the year (£53.6m) and the costs associated with prepaying the loans secured against 5 Churchill Place and 10 Cabot Square/20 Cabot Square (£46.9m). Earnings per share for 2010 were 26.3p compared to 13.6p in 2009.

At 31 December 2010, the Group had unsecured cash deposits of £879.1m. The weighted average cost of debt was stable at 6.3% and the weighted average maturity was 14.9 years which compares with the weighted average unexpired lease length assuming exercise of all break options of 15.7 years. This matching of income to debt maturities is a demonstration of the Group's financial planning which underlies its strong financial position at the year end.

The results for the year are covered in more detail in the 'Business Review – Operating Results'.

Conclusion

None of the success achieved in 2010 would have been possible without the continued commitment of all staff and the steadfast support of shareholders for which the Board expresses its thanks.

The Group is well capitalised with strong financial and human resources. This enables us, with our deep and proven management experience, to work our capital selectively and efficiently. We are looking actively at other opportunities in Central London as well as those on the Estate where we can maximise our capabilities in construction, development, marketing and finance and to create value for all our shareholders.

We are mindful of the continuing uncertainty over the pace of economic recovery. However, the Board believes the Group is strongly positioned to take advantage of opportunities in what is set to be a supply constrained market of quality grade A space.

BUSINESS REVIEW

The following 'Business Review' aims to provide shareholders with an overall summary of the business of the Group both during the year ended and as at 31 December 2010, as well as summarising significant events which have occurred subsequent to this date.

A list of defined terms used throughout these financial statements is provided in 'Definitions'.

Central London office leasing market overview

The following commentary on the Central London office market was provided by CBRE.

Demand and take up

The Central London market enjoyed a strong end to the year as take-up was buoyed by some very large deals in December 2010. As a consequence take-up for the fourth quarter was 4.5m sq ft, pushing the total for 2010 to 15.0m sq ft which was the strongest annual performance since 2006. This was 67.0% higher than for 2009 with sharp increases experienced across all types of space, particularly prelets.

Despite lingering uncertainty surrounding the economic outlook, occupiers have continued to press ahead with a number of large occupational decisions. With a number of the largest requirements now satisfied, it is possible that the first half of 2011 could see a weaker level of transactions. However, from 2012 take-up should rise strongly as the UK economic recovery becomes fully entrenched and a number of lease expiries in the next three years should also help stimulate demand.

Supply and demand

Against the backdrop of very strong demand and a limited amount of development activity, London availability was 14.6m sq ft at the end of 2010 which represents a 31.0% fall since the market peak in the second quarter of 2009. Reflecting a similar trend, the Central London vacancy rate fell from 5.9% to 5.5%. This compares to 7.2% at the end of last year and is the lowest since 2008.

Development completions are expected to fall sharply in 2011, reaching just 1.2m sq ft, before rising to 2.4m sq ft in 2012. With demand expected to be relatively strong over the period, availability will fall steadily over the next two years before rising as development activity picks up again.

Rental outlook

Rental growth continued across most Central London markets during 2010, although the pace slowed in the final quarter. City rents moved to £55.00 per sq ft at the end of 2010, from a low of £42.00 per sq ft in 2009 representing a 31.0% increase. By comparison rental levels at Canary Wharf have remained relatively stable at £37.50 per sq ft, not having seen the volatility of office rental values experienced elsewhere in the Central London market over the last two years.

Rent free periods on 10 year leases ended the year down as landlords reacted to market conditions. Consequently City rent frees had tightened to 24 months by the year end.

The tight supply conditions expected this year will continue to support rental growth over the next 2-3 years.

BUSINESS REVIEW (Continued)

Property portfolio

The Group is engaged in property investment and development and is currently primarily focused on the development of the Estate. The Group is also involved, through joint ventures, in the development of Wood Wharf and the redevelopment of 20 Fenchurch Street in the City. At 31 December 2010 the retained investment portfolio comprised 16 completed properties (out of the 35 constructed on the Estate) totalling 6.9m sq ft of NIA. The properties included in the Group's investment portfolio to be retained at 31 December 2010 are shown in the table below.

Property address	NIA sq ft	Leased %	**External valuation £m**	Principal tenants and sub tenants
One Churchill Place	1,014,400	100.0	**725.0**	Barclays Bank, BGC
10 Cabot Square/5 North Colonnade	639,000	99.6	**350.0**	Barclays Capital, WPP Group
20 Cabot Square/10 South Colonnade	562,000	99.8	**310.0**	Barclays Capital
One Canada Square	1,236,200	90.5	**647.2**	Bank of New York Mellon, Moody's, HSBC, Mirror Group, State Street, FSA, NYSE
33 Canada Square	562,700	100.0	**366.0**	Citi
20 Bank Street	546,500	100.0	**418.0**	Morgan Stanley
40 Bank Street	607,400	86.8	**350.0**	Shell, Skadden, Allen & Overy, ANZ, JLL
50 Bank Street	209,800	100.0	**152.5**	Northern Trust, Goldenberg Hehmeyer
10 Upper Bank Street	1,000,400	100.0	**715.0**	Clifford Chance, FTSE, Total
Cabot Place Retail	139,600	100.0	**161.4**	Boots, Tesco, Zara and other retail tenants
Canada Place Retail	72,200	100.0	**166.2**	Gap, Next and other retail tenants
Jubilee Place Retail	89,400	100.0	**108.0**	Boots, M&S Food, Wagamama and other retail tenants
Churchill Place Retail	22,400	100.0	**19.3**	Barclays Bank, Jamie's Italian and other retail tenants
16-19 Canada Square	211,500	100.0	**68.8**	Waitrose Food & Home, Reebok, Plateau Restaurant
Reuters Plaza	8,900	100.0	**13.8**	Carluccio's, Smollensky's
Park Pavilion	22,000	100.0	**19.3**	Lloyds Bank, Canteen, The Parlour, Roka and Wahaca
Car parks	–	–	**48.0**	
Total	6,944,400	97.1	**4,638.5**	

At 31 December 2010 the investment property portfolio was 97.1% let (31 December 2009 – 96.2%). In calculating the occupancy level at 31 December 2009, 25 Bank Street was treated as fully let because of the subleases in the building and the 4 years' cover provided by AIG.

As well as the rental income generated from completed properties, income is generated from managing the entire Estate which, in addition to the completed properties owned by the Group, includes 19 properties totalling 8.7m sq ft in other ownerships.

The properties of the Group are under lease to a range of tenants. At 31 December 2010 the weighted average unexpired lease term for the office investment portfolio was approximately 16.9 years, or 15.7 years assuming the exercise of outstanding break options (31 December 2009 – 15.8 years or 14.8 years respectively). At 31 December 2009 the calculation of the weighted average lease term took into account the restructuring of leases with Barclays Capital, excluded 5 Churchill Place which was subject to an agreement for sale, and substituted the original term of the Lehman lease with the 4 years' cover provided by AIG. Of the office square footage under lease at 31 December 2010 79.6% does not expire or cannot be terminated by tenants during the next 10 years.

Property sales

In December 2010 the Group announced the sale of 25 Bank Street to J.P. Morgan for a gross consideration of £495.0m. The building, which comprises more than 1.0m sq ft, will become the new European headquarters of J.P. Morgan's investment banking operations in 2012. The building was valued at £360.0m at 31 December 2009, reducing to £350.0m at 30 June 2010. Prior to the sale of the building, the Group agreed terms with AIG for the termination of the rental cover facility relating to the building in consideration for a receipt of £144.5m (see 'Business Review – Lehman'). The combined receipt of £639.5m compares with a market valuation, including the AIG arrangement, of £550.0m at 30 June 2010 (see 'Business Review – Balance Sheet and key performance indicators').

Following the sale of 25 Bank Street, the directors are of the view that the Group is in a strong position to respond to the anticipated tightening in the occupier market.

In January 2010, the Group completed the sale of 5 Churchill Place for a gross consideration of £208.0m reflecting an initial yield of 5.9%.

Lehman

In September 2008 Lehman went into administration however the Administrator continued to pay rent on 25 Bank Street until the first quarter of 2010. Following Lehman's administration Nomura subleased approximately 420,000 sq ft from the Administrator on a 2 year sublease, subject to a break option in September 2010. This break option was subsequently exercised.

At 31 December 2009 lease incentives included £53.6m attributable to Lehman's lease at 25 Bank Street. As the Administrator ceased paying rent on the building with effect from 31 March 2010, the remaining Lehman incentives were written off to the profit and loss account in the first half of the year and treated as an exceptional item.

A facility with AIG provided for payment of up to the full amount of the contracted rent at the election of the Group in the event of default, for a period of 4 years from the date of first drawdown following rental default. Any amounts drawn down under this facility were repayable from recoveries received from the Administrator, from Lehman's parent company guarantee, or from rentals in the property which exceed the contracted rents that would have been received from Lehman under its lease.

In November 2010 terms were agreed with AIG for the termination of the facility in consideration for a payment to the Group of £144.5m. This sum comprised the net present value of the available drawings under this facility, net of facility fees payable to AIG and anticipated recoveries from Lehman's parent company guarantee.

Leasing

In addition to the Barclays Capital restructuring and new leases in respect of 1,152,000 sq ft in 10 Cabot Square and 20 Cabot Square completed in January 2010, the terms of which were summarised in the 2009 Report & Financial Statements, the Group completed letting transactions totalling approximately 387,000 sq ft in the year as detailed below.

In June 2010 the Group completed the letting of approximately 187,000 sq ft of space to Shell in 40 Bank Street. Shell has taken a lease on 10 floors for a term of 15 years (subject to a tenant break option at the expiry of year 10) at a rent of £37.50 per sq ft for the office space. With the exception of one floor, all of the 187,000 sq ft was leased in shell and core condition and has a rent free period of 42 months. The leases have a 12 month penalty if the break option at year 10 of the term is exercised. This space was previously leased to Barclays Capital. A further 95,000 sq ft leased to Barclays Capital in 40 Bank Street was leased back to the Group with effect from October 2010.

In February 2010 KPMG exercised break options in relation to its leases over 4 floors in One Canada Square totalling approximately 109,800 sq ft and in addition exercised an option to sublease to the Group (for the remaining term of approximately 6.75 years) a further floor in the building comprising 28,600 sq ft. The options to determine these leases were granted in connection with KPMG's relocation to a new headquarters building constructed at 15 Canada Square. The leases on the 5 floors terminated on 30 June 2010. Of these floors, 4 have subsequently been re-leased in their current condition, subject to minor refurbishment works.

Including these floors, the following leases were completed in the period in respect of space in One Canada Square:

- FSA took an additional 27,900 sq ft on level 25 bringing its current occupancy to over 136,000 sq ft in the building.
- HSBC leased 82,150 sq ft on levels 7-9, formerly occupied by KPMG, for 5 years subject to annual rolling break options.
- NYSE relocated from 25 Bank Street and leased 28,500 sq ft on level 38 for 10 years with a break option at the end of the fourth year.
- Regus renewed its lease over 14,445 sq ft on level 29 for a 10 year term subject to a 24 month rent free period.
- Samsung Electronics took a lease of 1,844 sq ft on level 34.
- Knight Frank renewed its lease of 981 sq ft on level 6.

A surrender was agreed of J.P. Morgan's space on floors 44-46 of One Canada Square totalling 87,500 sq ft. This space was previously leased to April 2013 and J.P. Morgan has paid a surrender premium equivalent to the foregone rent and service charges, together with dilapidations. Gaining this space early is of benefit to the Group given the current limited availability on the owned Estate and will allow early leasing of the space combined with the benefit of the rental prepayment.

In 40 Bank Street, levels 6 and 7 comprising 38,200 sq ft, have been taken by Jones Lang LaSalle on a lease to 2017. In addition Interquest has taken 2,650 sq ft on level 18 for a term of 10 years, subject to a 5 year break option, and Servcorp took a lease of 2,898 sq ft on the same floor for a similar term.

BUSINESS REVIEW (Continued)

Subsequent to the year end, Servcorp took an additional 1,877 sq ft on level 18 and China Construction Bank has taken 1,997 sq ft adjacent to their existing unit on that floor.

Expiries and break options over 44,500 sq ft in One Canada Square have been exercised by other tenants, of which 22,100 sq ft was with effect from March 2010 and the remainder from June 2010 or later.

All options on sublet space back to the Group have been exercised. At 31 December 2010, the estimated net present value of sublet liabilities was approximately £37.6m discounted at 6.3%, being the Group's weighted average cost of debt (31 December 2009 – £72.9m, discounted at 6.4%). These sublet commitments have been reflected in the market valuation of the Group's properties. The reduction in sublet liabilities reflects the letting to Shell of 187,000 sq ft of space in 40 Bank Street previously leased to Barclays Capital, the surrender of space sublet in 25 Bank Street prior to its sale to J.P. Morgan, and the expiry of certain other subleases.

Development properties

In January 2010 the Group acquired a long leasehold interest in 1 Park Place for £17.5m. This site, which is located adjacent to the Estate, benefits from two alternative planning consents for approximately 214,000 sq ft or 950,000 sq ft of development. Although the Group has yet to announce plans for this site it offers a significant opportunity for future development.

In addition, in June 2010 the Group acquired the remaining interests at Heron Quays West and as a result the Group has secured full control of this important development site with consent for office space of 1.3m sq ft. Consent has also been granted on the adjacent Newfoundland site for 0.2m sq ft of mixed use development.

Of the remaining development sites, 25 Churchill Place can accommodate up to approximately 0.5m sq ft of new development and North Quay has planning consent for 2.4m sq ft.

In summary, the total development capacity at each of the Group's development sites is as follows:

	NIA m sq ft
Based on existing planning permissions:	
- 25 Churchill Place	0.53
- North Quay	2.39
- Heron Quays West	1.33
- Newfoundland	0.23
- Crossrail retail	0.11
- 1 Park Place (proposed development)	0.70
	5.29
Wood Wharf (25.0% share of 4.62m sq ft)	1.15
Sold to J.P. Morgan:	
- Riverside South (the Group acting as development and construction manager)	1.90

The Group has continued to work with Ballymore and BWB on the redevelopment of Wood Wharf. The master plan for the scheme, in which the Group has a 25.0% interest, sets a framework for approximately 7.0m sq ft gross of mixed commercial, residential and retail development. Outline consent for 4.6m sq ft net was granted in May 2009. Further design work has been carried out on the first phase of office buildings and related infrastructure and detailed consent was granted on three buildings totalling 1.5m sq ft in July 2009.

The site at Riverside South was acquired by J.P. Morgan in November 2008 and the Group was appointed to act as development and construction manager under a contract with an original term to October 2013. In conjunction with J.P. Morgan's acquisition of 25 Bank Street, this contract was modified and extended to October 2016. As part of this modification, the Group's option to purchase the site was changed to a right of first offer.

During the course of 2009 and 2010 design and infrastructure works were completed on site. J.P. Morgan has now given the go ahead to bring the development to street level.

Up to the end of 2010 the Group received £68.5m as an advance of developers' profit in conjunction with the scheme and a further £7.5m is receivable in May 2011. These sums will be set against the Group's entitlement to future profits if J.P. Morgan proceeds with full construction.

Drapers Gardens

Practical completion was achieved on Drapers Gardens in November 2009. The scheme comprised approximately 290,000 sq ft of prime commercial office space. The Group had a 20.0% interest in the property and acted as development manager with responsibility for the day to day management of this scheme. In January 2010 the Group purchased for a cash consideration of £112.8m the substantial majority of the drawn balance under the Drapers Gardens construction loan facility. The Group then provided funding under the terms of this facility for the remaining costs of completing the project.

In February 2010 the Group announced that BlackRock had taken a lease on the whole of Drapers Gardens for a term of 25 years at a rent of £49.00 per sq ft on the office accommodation, with a rent free period of 36 months. The rent is subject to open market reviews on every fifth anniversary of the term commencement and, in the case of the first rent review, subject to a floor of 2.5% and a cap of 4.5% compounded annually over the preceding 5 years. The net annual rent on the property will be £12.8m on the expiry of the rent free period in March 2013.

In August 2010 the entities which owned the Drapers Gardens property exchanged contracts to sell the property with completion occurring in November 2010. The gross aggregate consideration was £242.5m, reflecting an initial yield of 5.2%, prior to a deduction for the rent free period granted to BlackRock.

Fenchurch Street

In October 2010 the Group announced the formation of the 20 Fenchurch Street Limited Partnership, a 50:50 joint venture partnership with Land Securities to develop 20 Fenchurch Street. The existing property, which was acquired as a cleared site with some ancillary retail neighbouring holdings, was sold by Land Securities to the partnership for a consideration of £90.2m, in line with the March 2010 valuation. After syndication, the Group has retained a 15.0% equity interest in the project.

Planning consent for the proposed 37 storey building was granted in October 2009. It will provide approximately 690,000 sq ft of world class space in floor plate sizes of 14,000 sq ft to 28,000 sq ft, with a sky garden on the top 3 floors. Construction commenced on site in January 2011.

Land Securities and the Group have been appointed as joint development managers and both are responsible for leasing, with Land Securities taking the lead. Canary Wharf Contractors Limited, a wholly owned subsidiary of the Group, has been appointed as construction manager.

Crossrail

In December 2008 the Group concluded agreements with the Secretary of State for Transport and TfL's subsidiary, CLRL, to contribute £150.0m towards the cost of the new Crossrail station at Canary Wharf.

The Group has taken responsibility for the design and construction of the Crossrail station, bearing the time and cost risks for a fixed price of £500.0m, of which £350.0m will be met from the Crossrail project's budget. The Group will bear the risk in relation to costs above the fixed price limit. The Group's anticipated contribution of £150.0m will be credited against any transport Section 106 contributions for certain agreed development sites on the Estate (comprising North Quay, Heron Quays West including Newfoundland and Riverside South) which may be required as part of proposed alterations to the London Plan. Accordingly, costs incurred on construction of the station are allocated to the Group's properties held for development.

Construction commenced on the Crossrail station at Canary Wharf in May 2009 and costs incurred to the end of 2010 totalled £105.4m. The station box is expected to be completed and handed over to CLRL by summer 2012 and the project is on schedule and on budget. The first trains are due to run in 2018 when Crossrail opens for passenger service. Planning permission has also been granted for a 100,000 sq ft retail area above the station which will be subject to a long lease to the Group.

Valuations

The net assets of the Group, as stated in its consolidated balance sheet at 31 December 2010, were £2,387.9m. In arriving at this total:

(i) properties held as investments were carried at £4,498.3m, which represents the market value of those properties of £4,638.5m at that date as determined by the Group's external valuers, CBRE, Savills or Cushman, less an adjustment of £140.2m for tenant incentives; and

(ii) properties held for development were carried at £299.7m, representing their cost to the Group.

In January 2010 the Group completed the sale of 5 Churchill Place for a gross consideration of £208.0m. The carrying value of the building at 31 December 2009 was £177.7m which was calculated by reference to the gross aggregate consideration, adjusted for a fitout allowance and rental support to be provided by the Group in respect of two unlet floors of £2.2m per annum for 5 years.

BUSINESS REVIEW (Continued)

In December 2010, 25 Bank Street was sold for a gross consideration of £495.0m. The market value of the building at 31 December 2009 was £360.0m, reducing to £350.0m at 30 June 2010.

The valuations at 31 December 2010 are based on assumptions which include future rental growth, anticipated void costs, the appropriate discount rate or yield and, in the case of development properties, the estimated costs of completion. In valuing the properties on the Estate the valuers also take account of market evidence which included the sales of 5 Churchill Place and 25 Bank Street, and the lettings completed in the year referred to earlier in this 'Business Review'.

As previously disclosed, a number of properties are subject to leases back to the Group. These have been taken into account in the valuations summarised in the table below, which shows the carrying value of the Group's properties for accounts purposes in comparison with the supplementary valuations provided by the external valuers.

		31 December 2010		30 June 2010		31 December 2009	
	Notes	**Carrying value £m**	**Market value in existing state £m**	Carrying value £m	Market value in existing state £m	Carrying value £m	Market value in existing state £m
Retained portfolio:							
Investment properties	(1)/(5)	**4,498.3**	**4,638.5**	4,276.9	4,432.0	4,102.8	4,227.0
Properties held for development		**299.7**	**268.5**	294.0	262.5	247.5	221.0
Sold properties:		**4,798.0**	**4,907.0**	4,570.9	4,694.5	4,350.3	4,448.0
Investment property held for sale	(2)/(5)	**–**	**–**	–	–	177.7	192.0
Investment property sold in year	(3)/(5)	**–**	**–**	348.3	350.0	304.0	360.0
		4,798.0	**4,907.0**	4,919.2	5,044.5	4,832.0	5,000.0
Property under construction – Riverside South	(4)	**74.6**	**127.3**	72.0	124.9	56.8	115.1
		4,872.6	**5,034.3**	4,991.2	5,169.4	4,888.8	5,115.1

Note:

1 The carrying value of investment properties represents market value less an adjustment for UITF 28. Market value in existing state is stated before adjustment for UITF 28. The UITF 28 adjustment attributable to investment properties at 31 December 2010 was £140.2m (30 June 2010 – £155.1m, 31 December 2009 – £124.2m).

2 The investment property held for sale comprised 5 Churchill Place which was sold in January 2010. At 31 December 2009, the market value in existing state was stated before adjustment for UITF 28 and was calculated by reference to the sale price of £208.0m less adjustments for a fitout allowance and provisions for rent free and rental support commitments. The UITF 28 adjustment attributable to this property at 31 December 2009 was £14.3m. This building reached practical completion in August 2009.

3 The investment property sold in the year comprised 25 Bank Street which was sold in December 2010. Market value in existing state is stated before adjustment for UITF 28. The UITF 28 adjustment attributable to investment property sold in the year was £1.7m at 30 June 2010 and £56.0m at 31 December 2009.

4 The property under construction comprises Riverside South. The carrying value in the balance sheet at 31 December 2010 is stated net of £55.6m of costs transferred to cost of sales (30 June 2010 – £51.9m, 31 December 2009 – £40.2m) and £19.0m transferred to payments on account (30 June 2010 – £20.1m, 31 December 2009 – £16.6m). The market value in existing state at 31 December 2010 includes the present value of the minimum developer's profit which will be generated from the development of the Riverside South site assuming J.P. Morgan does not proceed with full build out, discounted at 6.3%, being the Group's weighted average cost of debt, and excludes the profit already recognised in the profit and loss account on the disposal of the site in 2008.

5 The total carrying value of the investment property portfolio at 31 December 2010 was £4,498.3m (30 June 2010 – £4,625.2m, 31 December 2009 – £4,584.5m). The total market value of the property portfolio at 31 December 2010 was £4,638.5m (30 June 2010 – £4,782.0m, 31 December 2009 – £4,779.0m).

The valuation of the investment portfolio to be retained on the basis of market value increased by £206.5m or 4.7% in the second half of the year. After also allowing for adjustments in respect of lease incentives and capital expenditure, the carrying value of the investment portfolio increased by £207.7m or 4.9% over the six months. The increase was primarily driven by the reduction in yields in the market as detailed below. Over the full year, the market value of the retained investment portfolio increased by £411.5m or 9.7% and the carrying value increased by £369.7m or 9.0%.

At 31 December 2010 the weighted average initial yield for the office portfolio was 4.8% (30 June 2010 – 5.0%, 31 December 2009 – 6.3%) and the weighted average equivalent yield was 5.2% (30 June 2010 – 5.7%, 31 December 2009 – 5.7%). The weighted average initial yield for the retail portfolio was 4.9% (30 June 2010 – 5.2%, 31 December 2009 – 5.7%) and the weighted average equivalent yield was 5.4% (30 June 2010 – 5.7%, 31 December 2009 – 6.3%).

CBRE and Savills have provided a joint opinion as at 31 December 2010 that the market value of sites held for development, comprising North Quay, Heron Quays West, Newfoundland, 1 Park Place, 25 Churchill Place and the Crossrail retail site, was £268.5m. This compares with a carrying value for accounts purposes of £299.7m, including £77.9m (31 December 2009 – £57.0m) of costs allocated in respect of Crossrail. In valuing the sites held for development, the valuers have allowed for estimated costs to complete, including an allowance for fitout and developer's profit. In addition they have allowed for letting, disposal, marketing and financing costs. The market value of £268.5m represents a reduction of 1.7%, after additions, over the market value at 31 December 2009. At 31 December 2010 the market value of these sites was £31.2m below their carrying value. In assessing the requirement for an impairment provision the directors have had regard to the net realisable value of the sites as supplied by the external valuers. On this basis the directors have concluded that no provision for impairment is required as at 31 December 2010.

The market value of the entire property portfolio to be retained increased by £191.8m or 4.1% in the second half of the year, adjusting for additions. For the full year market value increased by £336.0m or 7.4%. These movements were driven by the factors referred to above.

Operating results

The following review of the Group's operating results relates to the year ended 31 December 2010. The comparatives relate to the year ended 31 December 2009.

Turnover of the Group is generated primarily by the rents and service charges earned from its property interests on the Estate, together with the recognition of amounts in respect of work performed under long term contracts. Before exceptional items, turnover for 2010 was £374.5m, against £481.3m for 2009, of which rental income was £248.7m (2009 – £267.2m). The impact of UITF 28 (excluding the exceptional write off of Lehman incentives) was to reduce rental income by £38.8m compared with £51.2m for 2009. Excluding the impact of UITF 28, rental income decreased from £318.4m in 2009 to £287.5m in 2010, a fall of 9.7%, primarily attributable to the exercise of break options and the cessation of rent from the Administrator on 25 Bank Street. During 2010 the Group recognised £18.3m of income in connection with the termination by tenants of certain leases on the Estate (2009 – £13.5m).

In the first quarter of 2010 the Administrator ceased paying rent on 25 Bank Street. Lease incentives attributable to Lehman's lease were previously being amortised over the period to the first open market rent review in November 2013 but, following the Administrator ceasing to pay rent, the remaining incentives, totalling £53.6m, were written off to the profit and loss account in the first half of the year and treated as an exceptional item.

Service charge income increased from £73.8m for 2009 to £74.3m for 2010, an increase of £0.5m or 0.7% and miscellaneous income, including insurance rents and the provision of tenant specific services outside the standard service charge, fell from £21.1m for 2009 to £17.8m for 2010, primarily as a result of lower insurance premiums.

Turnover for 2010 also included £15.4m recognised on the construction of the development property at Riverside South which is accounted for as a long term contract in accordance with SSAP 9. In 2009, turnover from long term contracts totalled £105.7m and the reduction in turnover from this source was attributable to the completion in that year of 15 Canada Square (KPMG) and 30 North Colonnade (Fitch).

Cost of sales includes rents payable and property management costs, movements on provisions for vacant leasehold properties and certain other lease commitments, as well as costs allocated to cost of sales on the construction of presold properties. Rents payable and property management costs were £98.9m for 2010 in comparison with £91.0m for 2009. Taking into account service charge and miscellaneous income totalling £92.1m for 2010, a deficit was recorded on property management of £6.8m (2009 – profit of £3.9m).

Provisions of £1.8m relating to the remaining vacant leasehold property, rent support commitments and certain other obligations were released in 2010 compared with £1.5m in 2009.

Cost of sales for 2010 also included £2.4m of dilapidations and other costs attributable to the termination of leases, as compared with £8.9m in 2009. In addition 2010 included £10.4m of costs relating to long term contracts, net of a release of £5.0m of surplus accruals relating to properties completed in prior years (2009 – £65.9m). No profit has been recognised on the long term contract entered into in connection with the sale of Riverside South although the potential surplus has been taken into account in calculating adjusted NAV (see 'Balance Sheet and Key Performance Indicators'). The previous year included £39.8m of profit recognised on presold properties.

Gross profit (net property income) for 2010 was £211.0m, a reduction of £106.0m in comparison with 2009. The reduction was primarily attributable to the write off of Lehman incentives of £53.6m, a reduction of £34.8m in profit recognised on presold properties and the reduction in rental income.

Administrative expenses for 2010 were £40.1m in comparison with £38.4m for 2009. The increase in administrative expenses was primarily attributable to expenses associated with property lettings during the year, which were partly offset by a reduction in payroll costs.

Other operating income excluding exceptional items totalled £8.3m for 2010 (2009 – £2.8m). During the period the Group earned additional fees in connection with one of the properties completed in 2009.

BUSINESS REVIEW (Continued)

Operating profit for the year was £179.2m in comparison with £281.4m for 2009. The reduction in operating profit of £102.2m was largely attributable to the factors impacting on gross profit detailed above.

In 2010, a net provision release of £4.1m was recognised in relation to the impairment of the Group's investments in its associates and joint ventures which has been treated as an exceptional item. This amount included a release of the impairment provision held against the Group's investment in Drapers Gardens following the sale of the building.

In 2009, a net release of £13.8m in the provision against the Group's investments in associates was recognised in the profit and loss account and treated as an exceptional item. The release of a provision against the Drapers Gardens project was partly offset by a charge of £5.6m recognised in relation to the Group's investment in WWLP.

In December 2010 the Group completed the disposal of 25 Bank Street for a gross consideration of £495.0m which resulted in a profit of £158.8m. In conjunction with the sale of 25 Bank Street, the Group agreed terms with AIG for the termination of the rental cover facility on this building for a net receipt of £144.5m. Both of these amounts have been taken to the profit and loss account and treated as exceptional items.

Net interest payable for 2010 excluding exceptional items was £214.5m, against £228.8m for 2009. The reduction was attributable to interest income recognised by the Group on the Drapers Gardens construction loan and the repayment of the loans secured against the buildings located at 5 Churchill Place and at 10 Cabot Square and 20 Cabot Square.

The interest rate swap associated with the construction loan facility secured against 5 Churchill Place was broken at the same time as the loan was repaid at a cost of £15.9m. In addition, the interest rate swap associated with the loan facility secured against the buildings at 10 Cabot Square and 20 Cabot Square was broken at a cost of £23.7m. Deferred financing costs of £6.3m, which were previously being amortised over the term of the loan to January 2013, and repayment fees of £1.0m have also been written off. These charges have been taken to the profit and loss account and treated as exceptional items.

In April 2009 the Group repurchased an aggregate principal amount of £119.7m of certain Notes for a consideration, excluding accrued interest, of £35.5m. These Notes remain in issue and continue to be fully hedged. However, from the perspective of the consolidated accounts the hedges are deemed to be uneconomic. Accordingly, after allowing for the mark to market on related interest rate swaps at the date of the repurchase totalling £14.6m, the Group recognised a gain of £68.4m which was treated as an exceptional item. The movement in the mark to market of the hedges in the current year of £5.5m has also been treated as an exceptional item.

The profit on ordinary activities after interest for 2010 was £219.7m in comparison with a profit of £134.8m for 2009. The results for 2010 included a number of exceptional items, comprising: the profit on sale of 25 Bank Street of £158.8m; the net receipt of £144.5m from the termination of the AIG facility; the write off of unamortised lease incentives of £53.6m in respect of the Lehman lease; a provision release of £4.1m in respect of the investment in associates; a charge of £5.5m in respect of the movement in fair value of hedges deemed uneconomic following the acquisition of certain Notes in 2009; and charges of £46.9m in relation to closing out certain interest rate swaps and debt. Excluding exceptional items, the profit on ordinary activities after interest for 2010 was £18.3m in comparison with £52.6m for 2009. The reduction in pre-exceptional profit of £34.3m was largely attributable to the recognition of profits on presold properties totalling £39.8m in 2009 compared with £5.0m in 2010.

Tax for 2010 comprised a corporation tax charge of £35.7m (2009 − £30.7m) and a deferred tax charge of £15.8m (2009 − £17.1m).

Profit after tax for 2010 was £168.2m in comparison with £87.0m for 2009. Basic and diluted earnings per share for 2010 were 26.3p in comparison with 13.6p for 2009.

Excluding the exceptional items totalling £201.4m referred to above and tax relief of £19.4m thereon, the adjusted loss per share for 2010 was 2.2p (2009 – earnings per share of 0.8p). The weighted average number of shares in issue was 639.0m at both 31 December 2010 and 31 December 2009. There were no instruments which gave rise to a dilution of earnings as defined by FRS 22 at either 31 December 2010 or 31 December 2009.

Tax

If the Group were to dispose of its property portfolio at the market value disclosed in this 'Business Review', a tax liability of £104.8m would arise (31 December 2009 – £78.0m). This liability is stated after taking into account the tax liabilities relating to deferred accounting profits on properties under construction held for sale and the benefit of the remaining EZAs which would be crystallised as a balancing allowance. This amount includes tax on trading profits and net chargeable gains that would arise on the sale of properties under construction and properties held for development, including land interests. This contingent liability is included in calculating adjusted NAV.

BUSINESS REVIEW (Continued)

Balance sheet and key performance indicators

On the basis of the Group's statutory balance sheet, which does not reflect any revaluation of properties held for development or under construction, net assets at 31 December 2010 were £2,387.9m in comparison with £2,055.4m at 30 June 2010 and £1,925.0m at 31 December 2009. The increase in net asset value for the year was attributable to the revaluation surplus on investment properties of £369.7m and the profit after tax for the year of £168.2m, partly offset by the dividend paid of £75.0m.

The Group's main objective is to maximise net assets through managing its property investment and development activities, although the Group is impacted by movements in the wider property market. The Board considers that the most appropriate indicator of the Group's performance is the movement in adjusted NAV per share. This measure serves to capture the Board's judgements concerning, inter alia, letting strategy, redevelopment and financial structure.

Adjusted NAV takes into account the valuation of properties under construction and properties held for development which are held in the balance sheet at cost. It also adds back the provision for deferred tax required by accounting standards but which, in the judgement of the directors, is for the most part unlikely to crystallise.

Adjusted NAV per share at 31 December 2010 is set out in the table below, which for comparison purposes also includes adjusted NNNAV per share.

	Note	**31 December 2010 £m**	30 June 2010 £m	31 December 2009 £m
Net assets per consolidated balance sheet		**2,387.9**	2,055.4	1,925.0
Add back deferred tax		**85.8**	74.1	70.0
Net assets prior to deferred tax		**2,473.7**	2,129.5	1,995.0
Revaluation of property portfolio:				
– investment property	1	**–**	200.0	190.0
– properties held for development	2	**(31.2)**	(31.5)	(26.5)
– property under construction	3	**52.7**	52.9	58.3
Adjusted net assets		**2,495.2**	2,350.9	2,216.8
Fair value adjustments in respect of financial assets and liabilities less tax relief at 28.0%		**(155.2)**	(147.4)	69.3
Contingent tax on property disposals	4	**(104.8)**	(87.7)	(78.0)
Undiscounted deferred tax		**(89.5)**	(89.6)	(91.2)
Adjusted NNNAV		**2,145.7**	2,026.2	2,116.9
Adjusted net assets per share	5	**£3.90**	£3.68	£3.47
Adjusted NNNAV per share	5	**£3.36**	£3.17	£3.31

Note:
1 The market value of 25 Bank Street reflected in the balance sheet at 30 June 2010 of £350.0m (31 December 2009 – £360.0m) excluded the benefit of the arrangement with AIG which provided for the payment of 4 years' contracted rent upon default by Lehman as the arrangement was not transferable to a purchaser of the property. The market value of this building, adjusted to include the arrangement with AIG was £550.0m (31 December 2009 – £550.0m). The valuation uplift did not allow for the annual commitment fees payable by the Group to AIG of approximately £3.6m per annum payable over the entire term of the Group's securitisation.
2 Revalued at market value in existing state.
3 Deferred profit on construction of Riverside South (refer to 'Business Review – Valuations').
4 Refer to 'Business Review – Tax'.
5 Calculated by reference to the closing number of shares of 639.0m at each balance sheet date. There were no dilutive instruments outstanding at any of the balance sheet dates.

Adjusted NAV per share increased by 12.4% from £3.47 at 31 December 2009 to £3.90 at 31 December 2010. The increase from £3.68 at 30 June 2010 was £0.22 or 6.0%. These increases were attributable to the increase in the valuation of the Group's portfolio and the profit for the year, including the profit on sale of 25 Bank Street.

BUSINESS REVIEW (Continued)

Over the period since December 2005 the Company paid distributions totalling £483.9m, equivalent to 76p per share.

In arriving at adjusted NAV per share the provision recognised in accordance with FRS 19 has been added back. FRS 19 requires, inter alia, provision for deferred tax on capital allowances claimed, notwithstanding that no tax would become payable unless the related properties were disposed of. In contrast no provision is required for the tax which would become payable if the Group was to dispose of its properties at their revalued amount. This inconsistency in the standard has therefore been reversed in calculating adjusted NAV per share. In calculating NNNAV per share, however, the full undiscounted liability has been deducted, along with the contingent tax payable on disposal of properties at their revalued amount. NNNAV per share also factors in the fair value of financial assets and liabilities.

Principal risks and uncertainties

The principal risks and uncertainties facing the business are monitored through continuous assessment, regular formal quarterly reviews and discussion at Audit Committee and Board level. Board and Audit Committee discussion focuses on the risks identified as part of the Group's system of internal control which highlights key risks faced by the Group and allocates specific day to day monitoring and control responsibilities as appropriate. The current key risks include the cyclical nature of the property market, financing risk, concentration risk and policy and planning risks. The turmoil in the financial markets during 2008 and the first half of 2009 resulted in an unusually pronounced negative impact on the real estate market, although the market has since staged a partial recovery.

Cyclical nature of the property market

The valuation of the Group's assets is subject to many external economic and market factors. The turmoil in the financial markets during 2008 and 2009 was reflected in the property market by such factors as the oversupply of available space in the office market, a significant decline in tenant demand for space in London and a change in the market perception of property as an investment resulting in a negative impact on property valuations in general. In the latter half of 2009 and during the course of 2010 there were signs of a tightening of supply which has been reflected in an increase in valuations and a compression in yields. Changes in the financial and property markets are kept under constant review so that the Group can react appropriately and adjust the business plan of the Group accordingly. The impact of the ongoing uncertainty in the financial and property markets continues to be closely monitored.

Financing risk

The broader economic cycle inevitably leads to movements in inflation, interest rates and bond yields. The Group finances its operations largely through a mixture of surplus cash, secured borrowing and debentures. The Group borrows at both fixed and floating rates and uses interest rate swaps to modify exposure to interest rate fluctuations. After taking account of interest rate hedging and cash deposits held as collateral, all of the Group's facilities are fixed long term loans. Further details on the management of treasury risks can be found in the section 'Business Review – Treasury objectives and risks'.

The ongoing uncertainty in financial markets continues to significantly limit the availability of funding. In common with other UK property companies, lack of financing facilities may have an impact on the business of the Group if the lending market remains limited for the foreseeable future.

Concentration risk

The majority of the Group's real estate assets are currently located on or adjacent to the Estate with tenants that are mainly linked to the financial services industry. Wherever possible steps are taken to mitigate or avoid material consequences arising from this concentration. The focus of the Group continues to remain on and around the Estate. However, where value can be added the Group will consider opportunities elsewhere.

Policy and planning risks

All of the Group's assets are currently located within London. Appropriate contact is maintained with local and national government, but changes in governmental policy on planning or tax could limit the ability of the Group to maximise the long term potential of its assets. These risks are closely monitored.

Treasury objectives and risks

The principal objectives of the Group's treasury function are to ensure the availability of finance to meet the Group's current and anticipated requirements and to minimise the Group's cost of capital. The treasury function operates as a cost centre rather than a profit centre and does not engage in trading of financial instruments.

The Group's financial instruments, other than derivatives, comprise borrowings, cash and liquid resources and various items such as trade debtors and trade creditors that arise directly from its operations. The Group enters into derivative transactions (principally interest rate swaps) only in order to manage the interest rate risk arising from the Group's variable rate borrowings. The Board reviews and agrees policies for managing the risks associated with the Group's financial instruments and these policies, which have been applied consistently throughout the year, are summarised in the following paragraphs.

Interest rate risk

The Group finances its operations through a mixture of surplus cash, bank borrowings and debentures. The Group borrows in sterling at floating rates of interest and then uses interest rate swaps to generate the desired interest profile and to manage the Group's exposure to interest rate fluctuations. The Group's policy is to keep the majority of its borrowings at fixed rates and at both 31 December 2010 and 31 December 2009 all of the Group's borrowings were fixed after taking account of interest rate hedging and cash deposits held as cash collateral.

BUSINESS REVIEW (Continued)

Liquidity risk
The Group's policy is to ensure continuity of funding and at 31 December 2010 the average maturity of the Group's debt was 14.9 years (2009 – 14.0 years). Shorter term flexibility is achieved by holding cash on deposit and through construction facilities typically with a term of 3-6 years arranged to fund the development of new properties. None of the Group's facilities matures before 2014.

The Group's loan facilities are secured on certain individual properties, are not subject to cross default provisions and are non recourse.

Loan covenants
The Group's loan facilities are subject to financial covenants which include maximum LTV ratios and minimum ICRs. The key covenants for each of the Group's facilities are as follows:

(i) CWF II securitisation, encompassing seven investment properties representing 70.5% of the investment property portfolio by value. The principal amount outstanding at 31 December 2010 was £2,462.1m or £2,342.4m excluding the repurchased Notes.

Maximum LMCTV ratio of 100%. Based on the valuations at 31 December 2010, the LMCTV ratio at the interest payment date in January 2011 would have been 73.7%.

The securitisation has no minimum ICR covenant. The Group has the ability to remedy a breach of covenant by depositing eligible investments (including cash). The final maturity date of the securitisation is 2035, subject to earlier amortisation on certain classes of Notes.

(ii) Loan of £568.1m secured against One Churchill Place, representing 15.6% of the investment property portfolio by value.

This facility is not subject to any LTV or ICR covenants and has a final maturity of 2034, subject to amortisation over that term.

(iii) Loan of £350.0m secured against the retail and infrastructure parking properties of the Group, representing 13.9% of the investment property portfolio by value.

Maximum LTV ratio of 70.0%. Based on the valuations at 31 December 2010, the LTV was 54.6%.

Minimum ICR covenant of 120.0%. The covenant was satisfied throughout the year. The Group has the ability to remedy any potential breach of covenant by depositing cash.

The facility repayment date is 17 December 2014.

Credit risk
Swap counter parties of the Group's derivative financial instruments are all rated 'A' or better on the S&P rating system. Cash deposits are placed on the money market for varying periods of time with banks that are all 'A' rated or above, or remain on deposit with major UK clearing banks.

Borrowings

At 31 December 2010, net debt (after cash in hand and cash collateral) stood at £2,292.3m, down from £2,843.1m at 31 December 2009, and comprised:

	31 December 2010 £m	31 December 2009 £m
Securitised debt	**2,423.7**	2,484.7
Loans	**919.4**	1,276.4
Finance lease obligations	**41.6**	41.2
Construction loan	**–**	123.4
Total borrowings	**3,384.7**	3,925.7
Less:		
- cash collateral for borrowings	**(194.4)**	(139.4)
- cash collateral for construction	**(5.1)**	(18.3)
- other cash collateral	**(13.8)**	(10.0)
	(3,171.4)	3,758.0
Less: cash deposits	**(879.1)**	(914.9)
Net debt	**2,292.3**	2,843.1

BUSINESS REVIEW (Continued)

The Group's borrowings are secured against designated property interests, have no cross default provisions and are subject to lending covenants that include maximum LTV ratios and minimum ICRs as outlined earlier in the loan covenants section of the 'Business Review – Treasury objectives and risks'. For all of its loans, the Group was in compliance with its lending covenants at 31 December 2010 and throughout the year then ended.

In January 2010 the Group sold 5 Churchill Place and repaid the drawn balance of £123.5m under its construction loan facility. At the same time the Group broke the interest rate swap associated with this facility at a cost of £15.9m.

In November 2010 the Group repaid the remaining balance of a bank loan of £348.7m secured against 10 Cabot Square and 20 Cabot Square. This loan had a scheduled repayment date of January 2013. The associated interest rate swap arrangement was broken at a cost of £23.7m. In addition, deferred financing costs of £6.3m which were previously being amortised over the term of the loan to January 2013, and repayment fees of £1.0m were written off to the profit and loss account.

Following repayment of the loan referred to above, 10 Cabot Square and 20 Cabot Square were transferred to the Group's securitisation in substitution for 25 Bank Street and 40 Bank Street. 25 Bank Street was subsequently sold to J.P. Morgan and 40 Bank Street was held debt free at the year end.

The decrease in total borrowings from £3,925.7m to £3,384.7m reflects the repayment of the loans referred to previously and scheduled amortisation. The increase in cash and term deposits from £1,082.6m to £1,092.4m is primarily attributable to the sales of 5 Churchill Place and 25 Bank Street, and the termination of the AIG rental cover facility, partly offset by the loan repayments referred to earlier.

At 31 December 2010 the fair value adjustment in respect of the Group's financial assets and liabilities calculated in accordance with FRS 13 (excluding debtors and creditors falling due within one year) was a liability of £215.5m before tax relief (31 December 2009 – asset of £96.2m).

At 31 December 2010, the Group's weighted average cost of debt was 6.3% excluding credit wraps (or 6.3% including credit wraps) in comparison with 6.3% excluding credit wraps (or 6.4% including credit wraps) at 31 December 2009.

Cash flow

Net cash inflow from operating activities for 2010 was £227.3m in comparison with £331.4m for 2009, a reduction of £104.1m. This reduction was primarily attributable to receipts in connection with properties in the course of construction during 2009.

Returns on investments and servicing of finance resulted in an outflow of £247.6m for 2010 compared with £242.0m for 2009. The increase in net cost was primarily attributable to the fall in margins earned on the Group's cash balances. The total for 2010 included £40.6m of swap and debt breakage costs, whereas the previous year included financing costs of £12.7m.

Capital expenditure and financial investment for 2010 resulted in a cash inflow of £659.9m, compared with an outflow of £112.9m for 2009. 2010 expenditure included £93.5m of development expenditure and net investments and loans to associated and joint venture undertakings in the year of £15.2m. The total for the year also included net proceeds of £190.0m from the sale of 5 Churchill Place and £469.7m from the sale of 25 Bank Street. The 2009 amount included £90.8m of development expenditure incurred on properties excluding presold properties and funding of the Group's investment in associated undertakings of £5.2m.

The financing cash outflow for 2010 was £549.4m compared with £62.9m for 2009. The total for 2010 included £123.5m relating to the repayment of the Group's construction loan and £366.9m relating to the repayment of the loan secured against 10 Cabot Square and 20 Cabot Square and other scheduled amortisation. The cash outflow for 2009 included £35.5m incurred on the partial buyback of the Notes, which was partly offset by £20.5m drawn down under the Group's construction loan facility.

CONSOLIDATED PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31 DECEMBER 2010

	2010 **£m**	2009 £m
Turnover:		
– before exceptional item	**374.5**	481.3
Exceptional item:		
– write off of Lehman incentives	**(53.6)**	–
	320.9	481.3
Cost of sales	**(109.9)**	(164.3)
GROSS PROFIT	**211.0**	317.0
Administrative expenses	**(40.1)**	(38.4)
Other operating income	**8.3**	2.8
OPERATING PROFIT	**179.2**	281.4
Exceptional items:		
– release of impairment of investments in associates before interest and tax	**4.1**	13.8
– profit on sale of investment property	**158.8**	–
– termination of AIG facility	**144.5**	–
Interest receivable	**25.8**	14.2
Interest payable:		
– before exceptional item:		
– Group	**(236.2)**	(242.7)
– associates	**(4.1)**	(0.3)
Exceptional items:		
– net (loss)/gain on repurchase of securitised debt	**(5.5)**	68.4
– breakage costs on interest rate swaps and debt	**(46.9)**	–
	(292.7)	(174.6)
PROFIT ON ORDINARY ACTIVITIES BEFORE TAX	**219.7**	134.8
Tax	**(51.5)**	(47.8)
PROFIT FOR THE FINANCIAL YEAR	**168.2**	87.0
Basic and diluted earnings per share	**26.3p**	13.6p

CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES FOR THE YEAR ENDED 31 DECEMBER 2010

	2010 £m	2009 £m
Profit for the financial year after tax:		
– Group	**168.2**	73.5
– share of profits of associated undertakings	**–**	13.5
Unrealised movement on revaluation of investment properties	**369.7**	173.7
TOTAL RECOGNISED GAINS AND LOSSES RELATING TO THE YEAR	**537.9**	260.7

CONSOLIDATED NOTE OF HISTORICAL COST PROFITS AND LOSSES FOR THE YEAR ENDED 31 DECEMBER 2010

	2010 £m	2009 £m
Reported profit on ordinary activities for the financial year before tax	**219.7**	134.8
Realisation of property revaluation losses in previous years	**(82.7)**	–
Historical cost profit for the financial year before tax	**137.0**	134.8
Historical cost profit for the financial year after tax	**85.5**	87.0

CONSOLIDATED BALANCE SHEET AT 31 DECEMBER 2010

	2010 £m	2009 £m
FIXED ASSETS		
Investment properties	**4,498.3**	4,584.5
Properties held for development	**299.7**	247.5
Other tangible fixed assets	**1.0**	1.5
Investments	**53.9**	37.4
	4,852.9	4,870.9
CURRENT ASSETS		
Debtors: Amounts due in more than one year	**140.2**	194.5
Debtors: Amounts due within one year	**69.4**	53.2
Cash at bank and in hand	**1,092.4**	1,082.6
	1,302.0	1,330.3
CREDITORS: Amounts due within one year	**(371.5)**	(377.0)
NET CURRENT ASSETS	**930.5**	953.3
TOTAL ASSETS LESS CURRENT LIABILITIES	**5,783.4**	5,824.2
CREDITORS: Amounts due after more than one year	**(3,279.3)**	(3,811.5)
Provisions	**(116.2)**	(87.7)
NET ASSETS	**2,387.9**	1,925.0
CAPITAL AND RESERVES		
Called up share capital	**6.4**	6.4
Reserves:		
– share premium	**146.2**	146.2
– revaluation reserve	**2,148.0**	1,695.6
– capital redemption reserve	**0.7**	0.7
– special reserve	**264.8**	264.8
– profit and loss account	**(178.2)**	(188.7)
SHAREHOLDERS' FUNDS	**2,387.9**	1,925.0

DEFINITIONS

Act	The Companies Act 2006
Administrator	PricewaterhouseCoopers LLP, administrator of Lehman
AIG	American International Group, Inc
Ballymore	Ballymore Properties Limited
Barclays Bank	Barclays Bank PLC
BlackRock	BlackRock Investment Management (UK) Limited
Board	Board of directors of Canary Wharf Group plc
bps	Basis points
BWB	British Waterways Board
CBRE	CB Richard Ellis Limited, Surveyors and Valuers
Chairman	Chairman of the Company
Chief Executive	Chief Executive of the Company
City	The City of London
CLRL	Cross London Rail Links Limited
Company	Canary Wharf Group plc
Cushman	Cushman & Wakefield, Real Estate Consultants
CWF II	Canary Wharf Finance II plc
Drapers Gardens	Drapers Gardens scheme in the City of London
Estate	Canary Wharf Estate including Heron Quays West, Newfoundland, Riverside South, North Quay and Park Place
EZA	Enterprise Zone Allowance
Fitch	Fitch Ratings Limited
FRS 13	Financial Reporting Standard 13 (Derivatives and Other Financial Instruments)
FRS 19	Financial Reporting Standard 19 (Deferred tax)
FRS 22	Financial Reporting Standard 22 (Earnings per share)
FSA	The Financial Services Authority
Group	Canary Wharf Group and its subsidiaries
ICR	Interest Cover Ratio
Land Securities	Land Securities Group plc
Lehman	Lehman Brothers Limited (in administration)
Lloyds	Lloyds Banking Group
LMCTV	Loan Minus Cash to Value
London Plan	Mayor of London planning document published by the Greater London Authority
LTV	Loan to Value
m	million
Moody’s	Moody’s Investor Services Limited
Morgan Stanley	Morgan Stanley & Co Limited
NAV	Net Asset Value
NIA	Net Internal Area
NNNAV	Triple Net Asset Value
Nomura	Nomura International plc
Notes	Notes of the Group’s securitisation
S&P	Standard & Poors
Savills	Savills Commercial Limited
Shell	Shell International Limited
Skadden	Skadden Arps Slate Meagher & Flom LLP
sq ft	square foot/feet
SSAP 9	Statement of Standard Accounting Practice 9 (Stocks and Long Term Contracts)
TfL	Transport for London
UITF 28	Urgent Issue Task Force 28 (‘Operating Leases’)
WWLP	Wood Wharf Limited Partnership