CANARY WHARF GROUP PLC

Extract from the Report and Financial Statements of the Group for the year ended 31 December 2009. The 2009 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

- **Adjusted net asset value per share was £3.47 at 31 December 2009, an increase of** 59p or **20.5% from** £2.88 at **30 June 2009 and an increase of** 15p or **4.5%** from £3.32 **over the year.**
- **Net assets increased to £1,925.0m at 31 December 2009, an increase** of £410.7m or **27.1% from** £1,514.3m at **30 June 2009** and by £260.7m **or 15.7% from** £1,664.3m at **31 December 2008.** The increases were partly attributable to increases in the value of the property portfolio and partly to the profit after tax for the year.
- **Adjusted NNNAV per share increased to £3.31 at 31 December 2009, up by** 27p or **8.9% from** £3.04 at **30 June 2009, and decreased by** 7p or **2.1% from** £3.38 at **31 December 2008.**
- The **market value of investment properties, property under construction and properties held for development totalled £5,000.0m at 31 December 2009,** £4,603.5m at 30 June 2009 and £4,925.5m at 31 December 2008.
- The **weighted average initial yield for the office portfolio** valuation **was 6.3%** at 31 December 2009, an improvement of 100 bps since 30 June 2009 and of 60 bps since 31 December 2008. The **initial yield for the retail portfolio was 5.7%,** an improvement of 70 bps since 30 June 2009 and 60 bps in the year.
- The **weighted average equivalent yield for the office portfolio** valuation **was 5.7%** at 31 December 2009, an improvement of 60 bps since 30 June 2009 and of 80 bps since 31 December 2008. The **equivalent yield for the retail portfolio was 6.3%,** an improvement of 90 bps since 30 June 2009 and 30 bps in the year.
- At 31 December 2009 the **Group's retained investment portfolio** totalling 8.0m sq ft **was 96.2% let** including the Lehman building (31 December 2008 – 7.9m sq ft of which 99.7% was let).
- At 31 December 2009 **the weighted average lease term** for the retained investment portfolio **was 15.8 years** (or 14.8 years assuming the exercise of break options).
- **Operating profit** for 2009 **fell to £281.4m from £369.6m** as a result of the completion of three pre-sold properties. **Profit before tax** for the year **was £134.8m** (2008 – £268.9m).
- In April 2009 the **Group repurchased certain securitisation Notes** with an aggregate principal amount of £119.7m **recognising a gain of £68.4m.**
- In December 2009 the **Group exchanged contracts for the sale of 5 Churchill Place for** a total consideration of **£208.0m** reflecting an initial yield of 5.9%. The transaction completed in January 2010.
- In 2009 **leasing transactions over approximately 125,000 sq ft were achieved.**
- **Practical completion** (Note (vi)) was **achieved on**:
  - **15 Canada Square,** a 400,000 sq ft building pre-sold to KPMG;
  - **30 North Colonnade**, a 300,000 sq ft building pre-sold to Fimalac for occupation by Fitch; and
  - **5 Churchill Place,** a 300,000 sq ft building which was 83.0% pre-let to JPMM.
- **Substantial progress was made on the Crossrail station project** which continues to be on schedule and within budget.
- Subsequent to the year end, in addition to completing the disposal of 5 Churchill Place, the Group:
  - **announced** the **restructuring of leases and grant of new leases to Barclays Capital** over 1,152,000 sq ft, consolidating their occupation from three into two buildings on the Estate.
  - **acquired 1 Park Place** at Canary Wharf **for £17.5m** with two alternative planning permissions for either 214,000 sq ft or 950,000 sq ft.
  - **acquired** the **substantial majority of** the **drawn balance under the Drapers Gardens** construction **loan** facility; and
  - **announced** the **letting of** the **Drapers Gardens** joint venture project of approximately 290,000 sq ft to BlackRock.

RESULTS IN BRIEF

	2009 £m	2008 £m
Rental income	**318.4**	287.5
Operating profit	**281.4**	369.6
Exceptional items:		
– movement of impairment on investment in associates before interest and tax	**13.8**	(23.2)
– profit on sale of development property	**–**	118.6
– net gain on repurchase of securitised debt	**68.4**	–
Profit on ordinary activities before tax	**134.8**	268.9
Profit before tax excluding exceptional items	**52.6**	173.5
Tax	**(47.8)**	(19.4)
Profit for the financial year	**87.0**	249.5
Dividend per share	**–**	16.0p
Basic and diluted earnings per share	**13.6p**	39.0p

CHAIRMAN'S AND CHIEF EXECUTIVE'S STATEMENT

2009 was a productive year for the Company despite adverse market conditions continuing into the first half. Adjusted NAV per share was £3.47 at 31 December 2009, an increase of 20.5% against £2.88 at 30 June 2009 and up by 4.5% against £3.32 at 31 December 2008. At the year end, occupancy levels in property owned by the Group stood at 96.2% and the average length of unexpired leases, all with upwards only rent review provisions, was 15.8 years (after substituting the term of the Lehman lease with the four years cover provided by AIG). Moreover, of the space under lease 68.0% does not expire or cannot be terminated in the next 10 years.

Reflecting these strengths, and the general improvement in the London market for prime property, the net assets of the Company increased by 27.1% to £1,925.0m in the second half of the year and for 2009 as a whole increased by 15.7%. The market value of the property portfolio increased by 7.6% during the second half of 2009 to £5,000.0m, reversing the fall in value during the first half of the year.

Several large transactions under negotiation in 2009 were completed soon thereafter in 2010 including the restructuring of existing leases and a new lease with Barclays Capital, the Drapers Gardens debt acquisition and letting, the purchase of additional land on the Estate at 1 Park Place and the completion of the sale of 5 Churchill Place which all provided an encouraging start to 2010.

The Central London office rental market is generally benefiting from increased demand for high quality space, matched by only a limited supply of appropriate modern buildings in the City of London and Canary Wharf. While many of the leading global and European financial institutions are located at Canary Wharf, over 30.0% of occupiers come from other sectors. This diversity continues to increase as a range of occupiers are attracted by the Group's ability to provide high quality large floor plates on competitive terms, as well as more flexible space and leases to occupiers with smaller requirements.

Financial Review

Net assets increased from £1,514.3m at 30 June 2009 to £1,925.0m at 31 December 2009 an increase of £410.7m, or 27.1%. Over the full year to 31 December 2009, net assets increased by £260.7m from £1,664.3m, an increase of 15.7%. These increases were attributable in part to the rise in the value of the group's investment portfolio since 30 June 2009, and in part to retained profit after tax for the year of £87.0m.

The second half of the financial year witnessed a recovery in both the property investment market and latterly the occupational market. The weighted average initial yield for the office portfolio strengthened from 7.3% at 30 June to 6.3% at 31 December 2009, whilst the weighted average equivalent yield for offices improved from 6.3% to 5.7%. For the retail portfolio, equivalent yields hardened from 7.2% to 6.3% over the same period. This movement in yields was reflected in an increase in the market value of the retained investment portfolio of 7.5% since June and over the full year the investment portfolio increased in value by £128.2m or 3.0% excluding additions (see 'Business Review – Valuations').

Turnover excluding income recognised on construction contracts was £375.6m, up from £357.4m in the previous year. Gross profit on this basis was £277.2m in comparison with £257.2m for 2008. The total profit before tax for the year was £134.8m compared with £268.9m for the previous year, which reflected the successful completion of long term building contracts on three pre-sold buildings and a resulting decline in both reported annual turnover and operating profits. This is nevertheless a resilient result for 2009 reflecting the health of the underlying portfolio and testament to the strength of the Group's rental income stream from long term leases.

Profit after tax for the year was £87.0m in comparison with £249.5m for the previous year.

The weighted average cost of debt at 31 December 2009 was 6.4% and the weighted average maturity was 14.0 years.

OPERATIONAL REVIEW

The group made good progress across all its operations during 2009 and also concluded finance orientated transactions such as the repurchase of certain Notes at a discount, generating a recognised gain of £68.4m.

Leasing

Lettings on 125,000 sq ft were achieved during the year to a variety of office tenants in what was generally a difficult letting market. Subsequent to the year end, the Barclays Capital restructuring and a new lease on an aggregate of 1,152,000 sq ft and the letting of approximately 290,000 sq ft at Drapers Gardens were also completed.

Retail space at Canary Wharf remains in strong demand from well respected fashion retailers and restaurants. Occupancy levels remain high with all units in the malls either let or in solicitors' hands. In response to this impressive level of demand, seven new units were opened during 2009 in a 37,000 sq ft expansion of the retail offering. Retail rental levels have also again improved. Reflecting these factors the valuation of the retail increased 15.5% in the second half of 2009 alone and 5.8% year on year.

Rent due under the lease of the Lehman building, which is partially occupied by the administrator of that firm, was paid in full during 2009, although the administrator has indicated it intends to vacate shortly approximately half of the building. The remaining half continues to be occupied by various sub-tenants including Nomura and there is still the full benefit of the four year rent guarantee from AIG which can be triggered by the Group when most appropriate.

Construction

During the year practical completion was achieved on the pre-sold buildings at 15 Canada Square, 5 Churchill Place and 30 North Colonnade. Construction is also continuing on the Riverside site which was pre-sold to JP Morgan in 2008. JP Morgan has the option of not proceeding with further construction on this site following completion of the infrastructure works which Canary Wharf Contractors Limited is undertaking for them. If construction of the Riverside building does not continue, Canary Wharf Group will be paid for the completed work and also retain £76.0m representing a portion of Developer's Profits relating to the development (of which £61.0m had been received by the year end).

Construction started on the Crossrail project when work commenced in May 2009 on the Crossrail station at Canary Wharf. Canary Wharf Group is constructing this station which will include around 100,000 square feet of additional retail space. Work on the station box at Canary Wharf is on budget and on schedule for completion in 2012. On the Jubilee Line, when work is completed, which is expected to be in October 2010, capacity will increase by some 45.0%. Notwithstanding weekend interruptions last year due to service upgrades on the DLR which have now finished, transportation facilities are significantly improved with an additional 50.0% capacity on DLR trains now operating between Canary Wharf and Bank.

Away from Canary Wharf

Off the Estate, the Group has completed the development of Drapers' Gardens which is a site in close proximity to the Bank of England and which is 20% owned by the Group. Following completion of the development work, the building was let by the Group on behalf of the owning consortium to BlackRock at a rent of £49.0 per sq ft. In January 2009 the significant majority of the undrawn debt for this development was acquired for the sum of £112.8m. It is notable that this project, the first of this type undertaken by the Group away from the Canary Wharf Estate, has been completed with a most satisfactory result.

On the Wood Wharf site which adjoins the Estate, detailed consent was secured in July 2009 for 3 buildings totalling 1.5m sq ft (net). This site already has outline permission for 4.6m sq ft net of office, hotel, residential and retail and is owned through a joint venture in which Canary Wharf Group has a 25.0% interest equivalent to 1.15m sq ft.

Future Development

The Company owns land which is available for building and has current planning permission for a combined total of 4.5m sq ft of future development on the Canary Wharf Estate itself in addition to the 4.6m sq ft net on the adjoining Wood Wharf site. Subsequent to the year end, the 1 Park Place site was acquired for £17.5m. This site has two alternative planning permissions for either a 214,000 sq ft. or for a 950,000 sq ft. building. Located at the centre of the Canary Wharf Estate, this site offers substantial potential for future development.

These projects all demonstrate the Group's construction and development capabilities, both within the Canary Wharf estate and beyond.

CONCLUSION

The Group has the resources to undertake projects both on the Estate and beyond to meet future demand as the shortage of good quality central London office space with large floor plates becomes increasingly pronounced. The Group also has significant cash reserves providing financial stability. During the year, the Company's largest shareholder, Songbird Estates plc, underwent a major recapitalisation which attracted significant investment from Qatar Holding and China Investment Corporation, which are two of the world's largest sovereign wealth funds.

Progress over the last year has only been possible in the prevailing conditions with much hard work and with the continuing steadfast commitment of staff at all levels for which the Board expresses its appreciation.

The Board looks forward to further progress in 2010.

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 2009 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 CB Richard Ellis.

Demand and take-up

Leasing activity in the Central London market enjoyed a very strong end to 2009, when 3.6m sq ft was leased in the final quarter, which was the highest level of quarterly take up since 2008. This pushed annual take up to 9.0m sq ft, which is a 23.0% fall on 2008. The strong take up levels continued into the first two months of 2010 with both January and February recording take up of over 1.0m sq ft which is on par with the long term average.

In the short term, the Central London office market rebound is set to continue as the amount of space under offer, which is a good indicator of leasing activity over the next few months, is 0.3m above trend at 3.2m sq ft. Over the medium term, the office market is expected to receive support from an improving economy with London forecast to recover from the recession more quickly than the UK. Financial and business services employment, the mainstay of demand in the London office market, will benefit from the recovery.

Supply and development

The strong leasing activity during the last two quarters of 2009 reduced the availability of space quite dramatically. There was 18.5m sq ft available across Central London at the end of 2009, most of which was secondhand. The sharp reduction in supply translated through to vacancy rates. The overall rate for Central London was 7.2%, and the highest rate was in the City where it is 8.5%. These rates are some way off the peaks set during previous market downturns, particularly during the 1990s recession.

Availability is expected to decline over the next few years as take up erodes the current supply, with declines in new space availability especially pronounced. This will be accentuated by the relatively limited level of development completions anticipated in the next two years with 4.1m sq ft of development completions expected during 2010 and just over 1.0m sq ft in the following year.

Rental Outlook

Central London rents stabilised and in some instances rose toward the end of 2009. The City and Midtown recorded the first rises in top prime rents since the fourth quarter of 2007. City prime rents rose to £43.50 per sq ft from £42.00 per sq ft with a similar increase in Midtown to £42.50 per sq ft. Rents in the other Central London markets were unchanged.

Meanwhile rent frees came under pressure as landlords reacted to the improving market conditions, pushing rent frees on a 10 year lease down slightly to 30-33 months in the City, while rent frees in the West End were unchanged.

Further tightening in availability over the next two years is expected to produce strong rental growth as the supply/demand imbalance intensifies. Reflecting this, City prime rents have risen since the start of the year, while at Canary Wharf, prime rents, which were around £35.00 per sq ft at year end, have shown signs of increasing over the first quarter of 2010 to around £37.50 per sq ft.

BUSINESS REVIEW (Continued)

Property portfolio

The Group is engaged in property investment and development and is currently 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 Drapers Gardens, which reached practical completion in November 2009. At 31 December 2009 the retained investment portfolio comprised 18 completed properties (out of the 35 constructed on the Estate) totalling 8.0m sq ft of NIA. The properties included in the Group's investment portfolio to be retained at 31 December 2009 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	**675.0**	Barclays Bank, BGC, LOCOG
10 Cabot Square/5 North Colonnade	639,000	100.0	**305**	Barclays Capital, WPP Group
20 Cabot Square/10 South Colonnade	562,000	99.8	**275**	Barclays Capital
One Canada Square	1,236,200	94.7	**629**	Bank of New York Mellon, Moody's, JP Morgan, KPMG, Mirror Group Newspapers, State Street, FSA
33 Canada Square	562,700	100.0	**350**	Citi
20 Bank Street	546,500	100.0	**400**	Morgan Stanley
25-30 Bank Street	1,023,300	98.9	**360**	Lehman, Nomura
40 Bank Street	607,400	64.4	**290**	Skadden, Allen & Overy, BGC, ANZ, JLL, Euronext
50 Bank Street	209,800	100.0	**142**	Northern Trust, Goldenberg Hehmeyer
10 Upper Bank Street	1,000,400	100.0	**665**	Clifford Chance, Infosys, FTSE, Total
Cabot Place Retail	139,600	92.0	**129**	Boots, Tesco, Zara and various retail tenants
Canada Place Retail	72,200	100.0	**130**	HMV, Gap, Next and other retail tenants
Jubilee Place Retail	89,400	100.0	**90**	Boots, Marks & Spencer Food, Wagamama and other retail tenants
Churchill Place Retail	22,400	100.0	**15**	Barclays Bank, Jamie's Italian and other retail tenants
16-19 Canada Square	211,500	100.0	**55**	Waitrose Food & Home, Reebok, Plateau Restaurant
Reuters Plaza	8,900	100.0	**9**	Carluccio's, Smollensky's
Park Pavilion	22,000	100.0	**15**	Lloyds Bank, Canteen, The Parlour, Roka and Wahaca
Car parks	–	–	**50**	
Total	7,967,700	96.2	**4,587**	

The principal tenants have been updated to reflect the lease restructuring with Barclays Capital which was completed in January 2010 (see 'Business Review – Barclays Capital').

In addition to the properties shown in the table above, practical completion of 5 Churchill Place was achieved in August 2009 (see 'Business Review – Construction'). Contracts were exchanged for the sale of this property in December 2009 for a total consideration of £208.0m and the transaction was completed in January 2010. The sale will be reflected in the accounts for the six months ended 30 June 2010, therefore the building is carried in the balance sheet at 31 December 2009 at the anticipated net proceeds.

At 31 December 2009 the investment property portfolio was 96.2% let allowing for the Morgan Stanley break in 20 Cabot Square and the recently announced restructuring of leases with Barclays Capital (see 'Business Review – Barclays Capital'). In calculating the year end occupancy level, 25 Bank Street has been treated as fully let because of the subleases in the building and the four years' cover provided by AIG (see 'Business Review – Lehman').

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 17 properties totalling 7.6m sq ft in other ownerships.

The properties of the Group are under lease to a range of tenants. At 31 December 2009 the weighted average unexpired lease term for the office investment portfolio was approximately 18.4 years, or 17.4 years assuming the exercise of outstanding break options (31 December 2008 – 18.0 years or 15.2 years respectively). The calculation of the weighted average lease term takes account of the recently announced restructuring of leases with Barclays Capital, excludes 5 Churchill Place and assumes the 25 Bank Street lease with Lehman remains in place. Substituting the original term of the Lehman lease with the 4 years' cover provided by AIG serves to reduce the weighted average unexpired lease term to 15.8 years (or 14.8 years assuming the exercise of outstanding break options). Of the square footage under lease 68.0% does not expire or cannot be terminated by tenants during the next ten years.

BUSINESS REVIEW (Continued)

Lehman

In September 2008 Lehman went into administration. Nomura has taken a two year sublease of 358,000 sq ft of the 1,023,000 sq ft leased by Lehman. This sublease will expire in March 2011, subject to breaks in September and December 2010. An additional 115,000 sq ft is sublet to tenants such as Jones Lang LaSalle and NYSE Euronext. An arrangement with AIG, supported by cash collateral, provides for drawings of an amount equal to any contracted rent shortfall, in the event of whole or partial default on rental payments due under the lease for a period of four years from the date of first draw down on this facility.

The Administrator acting on behalf of Lehman has advised that as from 1 January 2010 Lehman will pay rent in respect of 290,146 sq ft only, being the area of 25 Bank Street which it currently occupies and not for the whole of the building. The Administrator has also advised that it proposes to move from the building by 31 March 2010 and from that date will cease paying rent. Notwithstanding this, the Group continues to demand full performance of Lehman's obligations under the lease and payment of rent on the whole of 25 Bank Street is being pursued in line with a recent High Court ruling on administrator liability. There has been no draw down under the AIG facility at the date these financial statements were approved. Sub-tenants, including Nomura, will continue to pay rent directly to the CWFII securitisation.

Barclays Capital

Subsequent to the year end, the Group and Barclays Bank concluded a series of transactions to rationalise and consolidate the occupation of Barclays Capital from three into two existing buildings on the Estate.

Barclays Capital will take a lease of 345,953 sq ft in 20 Cabot Square recently vacated by Morgan Stanley. This lease will be on the same lease terms and rental outgoings as the restructured leases referred to below. In return the Group will take back, via subleases, the leases on 301,676 sq ft in 40 Bank Street from Barclays Capital in two tranches. The first tranche of 206,708 sq ft has been leased back with an effective date of 1 November 2009 and the second tranche of 94,968 sq ft will be taken back on 1 October 2010.

Barclays Capital's existing leases in 5 North Colonnade and 10 South Colonnade were restructured and new leases granted such that the rent will be £27.50 per sq ft subject to annual RPI increases with a 0% floor and a 5.0% cap compounded annually over the first five years. Subsequently there will be annual RPI increases in rent over the rest of the term until the expiry of the lease in June 2032.

The new lease on 10 Cabot Square is an overriding lease and Barclays Capital will assume responsibility for the space on levels 9 and 10 (103,854 sq ft) which is leased by WPP until 2016. The rent on this space in 2016 will be at the then passing rent under the overriding lease, which is subject to the same RPI uplifts as the restructured leases. As a result of the restructuring, Barclays Capital will eventually occupy approximately 1,152,000 sq ft in two buildings.

The Group will pay a sum of £27.0m to Barclays Capital as a premium for the grant of the take back leases on 40 Bank Street to reflect the tenant fitting out works carried out by Barclays Capital on certain floors. The Group will also pay an inducement to Barclays Capital of approximately £16.0m for the restructuring of the leases on 5 North Colonnade and 10 South Colonnade and a further £11.0m will be paid in relation to construction services to be provided on the former Morgan Stanley space in 20 Cabot Square.

Leasing

In addition to the Barclays Capital restructuring and new leases in respect of 1,152,000 sq ft completed in January 2010, the Group completed letting transactions totalling approximately 125,000 sq ft during 2009.

- The FSA has taken leases on levels 26 and 27 in One Canada Square totalling approximately 55,800 sq ft at a rent of £35.00 per sq ft on terms expiring in 2018. One of the leases has a tenant break clause effective at the end of the fifth year. In addition the FSA is occupying level 24 on a short term basis pending completion of the fit-out on their new space and has an option on a further floor.
- Euler Hermes restructured its lease for approximately 49,000 sq ft on level 35 and part of level 36, One Canada Square for a term to October 2020.
- Global Sage has taken 2,584 sq ft on part of level 28, One Canada Square.
- MetLife Inc has taken 10,871 sq ft on part of level 28, One Canada Square following expiry of their original lease.
- Novartis has taken 1,995 sq ft on part of level 34, One Canada Square.
- CFA took an additional lease of 1,039 sq ft on part of level 10, One Canada Square.
- Premier FX Investing is taking a lease of 3,553 sq ft on part of level 19, 40 Bank Street.

BUSINESS REVIEW (Continued)

The above transactions have been concluded on a variety of leases for short to medium terms and at rents of between £29.00 per sq ft (for a 10 year fixed term with 15 months rent free) and £42.00 per sq ft (for a three year term with four months rent free).

With effect from 1 February 2010, Morgan Stanley exercised its break option relating to the lease of 20 Cabot Square. Until vacating the building in August 2009 Morgan Stanley occupied approximately 345,500 sq ft over six floors at 20 Cabot Square, and continues to lease 546,500 sq ft at 20 Bank Street on a lease expiring in 2028 and to own and occupy the 448,500 sq ft building at 25 Cabot Square.

As part of the agreement with State Street covering the construction of its new headquarters at 20 Churchill Place, State Street exercised options to determine its leases over two floors in One Canada Square totalling approximately 58,000 sq ft. In addition, State Street has exercised an option to sublease to the Group (for the remaining term of approximately nine years) one floor in One Canada Square, totalling approximately 26,200 sq ft, which was subleased from another tenant in the building. The options to determine these leases were granted in order to provide for the relocation of State Street to 20 Churchill Place, which completed in December 2008. State Street continues to occupy approximately 57,000 sq ft in One Canada Square on leases which expire in 2018.

Following its acquisition of Bear Stearns, JP Morgan has determined its leases over three floors in One Canada Square totalling approximately 70,000 sq ft. JP Morgan continues to occupy a further three floors of One Canada Square totalling approximately 87,000 sq ft on leases which have a tenant break in April 2013.

Subsequent to the year end, in February 2010 KPMG exercised breaks in relation to their leases over four floors in One Canada Square totalling approximately 109,796 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 28,579 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 (see 'Business Review – Construction'). The leases on the five floors will now terminate on 30 June 2010.

In addition breaks over 40,500 sq ft in One Canada Square have been exercised by other tenants, of which 22,100 sq ft is with effect from March 2010 and 18,400 sq ft is effective from July 2010 or later.

The current status of the floors in One Canada Square referred to above or, where applicable, the proposed work to be carried out, is summarised in the table below.

Floor	Tenancy	Status
27	State Street	Relet to FSA until 2018
26	State Street	Relet to FSA until 2018, tenant break at year 5
25	JP Morgan/State Street	Stripped to shell and core, under option to FSA
24	State Street	Relet to FSA on short term basis
31	JP Morgan	Refurbished to new Cat A – marketing floor
7–9/38–39	KPMG	To be stripped to shell and core
50	JP Morgan	To be refurbished to Cat A

All options to sublet space back to the Group have now been exercised. At 31 December 2009, adjusting for the Barclays lease restructuring, the estimated net present value of sublet liabilities was approximately £72.9m discounted at 6.4% being the Group's weighted average cost of debt (31 December 2008 – £20.6m, discounted at 6.2%). The increase in sublet liabilities reflects the take back of space in 40 Bank Street in connection with the restructuring of the Barclays Capital leases. These sublet commitments have been reflected in the market valuation of the Group's properties.

BUSINESS REVIEW (Continued)

Construction

In April 2009 the Group completed the construction of a 400,000 sq ft building at 15 Canada Square which was pre-sold to KPMG in November 2006. The profit on sale of this building has been recognised over the period of its construction.

In August 2009 the Group completed the construction of a 314,000 sq ft building at 5 Churchill Place of which 262,000 sq ft had been pre-let to JP Morgan. The Group exchanged contracts for the sale of this property for £208.0m in December 2009 and completed the transaction in January 2010. In accordance with the Group's policy of recognising profit on disposals at the date of completion, no profit was recognised in 2009 and the property was carried as an investment property held for sale at 31 December 2009 at the anticipated net proceeds. In connection with this sale the Group has agreed to provide a fit-out allowance for the unlet floors and rental support in respect of the unexpired rent free period on the JP Morgan space and, for up to five years, on the unlet space.

In September 2009 practical completion was achieved on 30 North Colonnade, a 330,000 sq ft building which was pre-sold to Fimalac for occupation by Fitch. The profit on this building has been recognised over the period of its construction.

In addition to the above, practical completion was achieved during the year on the expansion of two of the Group's retail malls, including a new retail building adjoining One Canada Square, Park Pavilion. This expansion has provided approximately 37,500 sq ft of lettable retail space which is fully let to tenants including Barclays, Jamie's Italian, Lloyds, Roka, Wahaca, Canteen and Drake & Morgan.

Development properties

The undeveloped site at 25 Churchill Place can accommodate up to approximately 515,000 sq ft of new development and at North Quay planning consent has been granted for 2.4m sq ft. There is further development capacity at Heron Quays West subject to acquiring the remaining leasehold interests on the site which are outside the control of the Group. Consent has been granted to increase the development of office space on this site to 1.3m sq ft. Consent has also been granted on the adjacent Newfoundland site for 220,000 sq ft of mixed use development.

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	0.5
- North Quay	2.4
- Heron Quays West	1.3
- Newfoundland	0.2
- Crossrail retail	0.1
	4.5
Acquired subsequent to year end:	
- 1 Park Place	1.0
	5.5
Sold to JP Morgan:	
- Riverside South	1.9
	7.4
Wood Wharf (25% share of 4.6m sq ft)	1.2

Subsequent to the year end the Group acquired the long leasehold interests in 1 Park Place for £17.5m. This site benefits from two planning consents for 214,000 sq ft or approximately 950,000 sq ft of development. Although the Group has yet to announce plans for the site, it offers a significant opportunity for future development.

The site at Riverside South was acquired by JP Morgan in November 2008 for £237.9m and the Group recorded a profit on disposal of £118.6m. JP Morgan has instructed the Group to complete on its behalf the design and infrastructure works for a new European headquarters building. Should JP Morgan decide to proceed with full construction, the Group will act as Development and Construction Manager. If construction is postponed, or deferred altogether, the Group will retain £76.0m representing a portion of the developer's profit related to the development, of which £61.0m had been received by 31 December 2009. If JP Morgan proceeds with full construction, additional fees will be due.

BUSINESS REVIEW (Continued)

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.

Practical completion was achieved on Drapers Gardens in November 2009. The scheme comprises approximately 290,000 sq ft of prime commercial development. The Group holds 20.0% of the share capital in the companies that own the property and continues to act as Development Manager with responsibility for the day to day running of the scheme. Subsequent to the year end 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.

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 five years.

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 Crossrail’s £15.9bn budget. 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 2009 totalled £70.1m. The station box is expected to be completed and handed over to CLRL by summer 2012 and currently the project is ahead of schedule and on budget. The first trains are due to run in 2017 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 2009, were £1,925.0m. In arriving at this total:

(i) properties held as investments were carried at £4,406.8m, which represents the market value of those properties of £4,587.0m at that date as determined by the Group’s external valuers, CBRE, Savills and Cushman, less an adjustment of £180.2m for tenant incentives;

(ii) 5 Churchill Place, for which an agreement for sale was entered into in December 2009, was held at £177.7m representing the anticipated net proceeds less an adjustment of £14.3m for tenant incentives; and

(iii) properties held for development were carried at £247.5m, representing their cost to the Group.

In valuing the properties on the Estate the valuers take account of market evidence which included the exchange of contracts in December 2009 to sell 5 Churchill Place, the lettings completed in the second half of the year and the advanced stage of negotiations with Barclays Capital at the balance sheet date on the lease restructurings referred to earlier in this ‘Business Review’.

The valuation of the investment portfolio to be retained, on the basis of market value, and adjusting for additions, increased by £319.4m or 7.5% in the second half of the year. After also allowing for adjustments in respect of lease incentives, the carrying value of the investment portfolio increased by £346.1m or 8.5% over the six months. The increase was primarily driven by the reduction in yields in the market by approximately 60 bps. Over the full year, the carrying value of the investment portfolio increased by £128.2m or 3.0%. At 31 December 2009 the weighted average initial yield for the office portfolio was 6.3% (30 June 2009 – 7.3%, 31 December 2008 – 6.9%) and the weighted average equivalent yield was 5.7% (30 June 2009 – 6.3%, 31 December 2008 – 6.5%). The weighted average initial yield for the retail portfolio was 5.7% (30 June 2009 – 6.4%, 31 December 2008 – 6.3%) and the weighted average equivalent yield was 6.3% (30 June 2009 – 7.2%, 31 December 2008 – 6.6%). The directors are of the view that the Group is in a strong position to respond to the anticipated recovery in the occupier market.

BUSINESS REVIEW (Continued)

CBRE and Savills have provided a joint opinion as at 31 December 2009 that the market value of sites held for development, comprising North Quay, Heron Quays West, Newfoundland, 25 Churchill Place and the Crossrail retail, was £221.0m. This compares with a carrying value for accounts purposes of £247.5m. In valuing the sites held for development, the valuers have allowed for estimated costs to complete, including an allowance for fit-out and developer's profit. In addition they have allowed for letting, disposal, marketing and financing costs. The market value of £221.0m represents a reduction of 28.2%, after additions, over the market value at 31 December 2008 but an increase of 4.3% since June 2009. At 31 December 2009 the market value of these sites was £26.5m below their carrying value which includes an allocation of the Group's contribution to Crossrail incurred to date. 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 2009.

The investment portfolio also included 5 Churchill Place which was sold in January 2010 for £208.0m less certain adjustments as disclosed in the 'Business Review – Construction'. The consideration reflected an initial yield of 5.9%. After allowing for incentives, rental support and certain other adjustments the Group recognised a revaluation surplus of £45.5m on this property at 31 December 2009 following its completion during the year.

The market value of the entire property portfolio increased by £353.1m or 7.6% in the second half of the year, adjusting for additions. For the full year market value reduced by £21.0m or 0.4%. These movements were driven by the factors referred to above.

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 2009		30 June 2009		31 December 2008	
	Note	**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
Investment properties	1	**4,406.8**	**4,587.0**	4,040.6	4,247.5	4,245.5	4,483.0
Investment property held for sale	2	**177.7**	**192.0**	–	–	–	–
		4,584.5	**4,779.0**	4,040.6	4,247.5	4,245.5	4,483.0
Property under construction		**–**	**–**	142.9	170.0	125.7	182.5
Properties held for development		**247.5**	**221.0**	221.7	186.0	199.8	260.0
		4,832.0	**5,000.0**	4,405.2	4,603.5	4,571.0	4,925.5
Properties under construction held for sale	3	**56.8**	**115.1**	126.7	329.5	222.5	536.6
		4,888.8	**5,115.1**	4,531.9	4,933.0	4,793.5	5,462.1

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 2009 was £180.2m (30 June 2009 – £206.9m, 31 December 2008 – £237.5m).

2 The investment property held for sale comprises 5 Churchill Place which was sold in January 2010. The market value in existing state is stated before adjustment for UITF 28 and is calculated by reference to the sale price of £208.0m less adjustments for a fit-out 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 (30 June 2009 – £nil, 31 December 2008 – £nil). This building reached practical completion in August 2009.

3 Properties under construction held for sale comprised: at 31 December 2009 – Riverside South; at 30 June 2009 – Riverside South and 30 North Colonnade; and at 31 December 2008 – Riverside South, 30 North Colonnade and 15 Canada Square. The carrying value in the balance sheet at 31 December 2009 is stated net of £42.0m (30 June 2009 – £120.7m, 31 December 2008 – £229.1m) transferred to cost of sales, £14.8m (30 June 2009 – £9.5m, 31 December 2008 – £0.4m) transferred to payments on account and £nil (30 June 2009 – £3.5m, 31 December 2008 – £6.9m) of costs accrued in accordance with SSAP 9. The market value in existing state at 31 December 2009 comprises the present value of the minimum developer's profit which will be generated from the development of the Riverside South site assuming JP Morgan does not proceed with full build out, discounted at 6.4%, 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.

The valuations are based on assumptions which include future rental income, anticipated void costs, the appropriate discount rate or yield and, in the case of development properties, the estimated costs to completion. The valuers also make reference to market evidence of transaction prices for similar properties on the Estate.

BUSINESS REVIEW (Continued)

Operating results

The following review of the Group's operating results relates to the year ended 31 December 2009. The comparatives relate to the year ended 31 December 2008.

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 on long term contracts. Turnover for 2009 was £481.3m, against £697.2m for 2008, of which rental income was £267.2m (2008 – £242.0m). The impact of UITF 28 was to reduce rental income by £51.2m compared with £45.5m for 2008. Excluding the impact of UITF 28, rental income increased from £287.5m in 2008 to £318.4m in 2009, an increase of 10.7%, primarily attributable to the benefit of rent reviews and fixed rental increases and increased retail rents. During 2009 the Group recognised £13.5m of income in connection with the termination by tenants of certain leases on the Estate (2008 – £24.3m).

Service charge income increased from £67.3m for 2008 to £73.8m for 2009, an increase of £6.5m or 9.7% and miscellaneous income, including insurance rents and the provision of tenant specific services outside the standard service charge, fell from £23.8m for 2008 to £21.1m for 2009.

Turnover for 2009 also included £105.7m recognised on the construction of development properties that have been pre-sold and are accounted for as long term contracts in accordance with SSAP 9 (2008 – £339.8m). The reduction in turnover from this source was accounted for by the completion in 2008 of 20 Churchill Place and by the completion in 2009 of 15 Canada Square and 30 North Colonnade.

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 pre-sold properties. Rents payable and property management costs were £91.0m for 2009 in comparison with £92.2m for 2008. Taking into account service charge and miscellaneous income totalling £94.9m for 2009, a profit was recorded on property management of £3.9m (2008 – deficit of £1.1m). This profit was attributable to the completion of buildings and fit-out works during the year on space which service charges are now recorded.

Provisions of £1.5m relating to the remaining vacant leasehold property, rent support commitments and certain other obligations were released in 2009 compared with £0.3m in 2008.

Cost of sales for 2009 also included £8.9m of dilapidations and other costs attributable to the termination of leases, as compared with £8.3m in 2008. In addition 2009 included £65.9m of costs relating to long term contracts (2008 – £188.7m), resulting in £39.8m of profit being recognised on such contracts (2008 – £151.1m).

Gross profit for 2009 was £317.0m, a fall of £91.3m over 2008, which was primarily attributable to the fall in profit recognised on long term contracts following the completion of these projects.

Administrative expenses for 2009 were £38.4m in comparison with £40.2m for 2008. The reduction in administrative expenses was primarily attributable to a reduction in leasing expenses.

Operating profit for the year was £281.4m in comparison with £369.6m for 2008. The reduction in operating profit of £88.2m was largely attributable to completion of long term contracts on pre-sold buildings.

In 2009 a net release of £13.8m in the provision against the Group's investment in its associates was recognised in the profit and loss account and treated as an exceptional item (2008 – charge of £23.2m). The release of the 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 November 2008, the Group sold Riverside South to JP Morgan for an initial consideration of £237.9m. As a result the Group recognised a profit of £118.6m net of historical costs incurred by the Group on the site and selling fees in that year. This has been shown as an exceptional item after operating profit in accordance with FRS 3.

Net interest payable for 2009 excluding exceptional items was £228.8m, against £196.1m for 2008. The increase was attributable to lower rates of interest earned on the Group's cash balances. Finance costs incurred on the construction loan of £4.8m were capitalised as part of the construction cost of 5 Churchill Place (2008 – £5.6m).

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 has been treated as an exceptional item. The movement in the mark to market of the hedges since the date of repurchase has been included within interest payable.

The profit on ordinary activities after interest for 2009 was £134.8m in comparison with £268.9m for 2008. The results for both years included certain exceptional profits and losses as described above. Excluding exceptional items, the profit on ordinary activities after interest for 2009 was £52.6m (2008 – £173.5m).

BUSINESS REVIEW (Continued)

Tax for 2009 comprised a corporation tax charge of £30.7m (2008 – £8.8m) and a deferred tax charge of £17.1m (2008 – £10.6m).

The profit after tax for 2009 was £87.0m in comparison with £249.5m for 2008. Basic and diluted earnings per share for 2009 were 13.6p in comparison with 39.0p for 2008.

The adjusted basic and diluted earnings per share for 2009 excluding exceptional items was 0.8p (2008 – 24.1p). Adjusted earnings per share for 2009 has been calculated by reference to the profit after tax excluding exceptional items comprising the net provision release of £13.8m in respect of the Group's investment in associates and the net gain of £68.4m on the repurchase of securitised debt. In 2008 exceptional items comprised the profit on disposal of the Riverside South site of £118.6m and the charge of £23.2m in respect of associates. The weighted average number of shares in issue was 639.0m at both 31 December 2009 and 31 December 2008. There were no instruments which gave rise to a dilution of earnings as defined by Financial Reporting Standard 22 (Earnings per share) at 31 December 2009 or 31 December 2008.

Tax

In 2009, and going forward, EZAs and plant and machinery capital allowances will shelter a small part of taxable profits. If the Group were to dispose of its property portfolio at the market value disclosed in this 'Business Review', a tax liability of £78.0m would arise (31 December 2008 – £78.5m). 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.

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 2009 were £1,925.0m in comparison with £1,514.3m at 30 June 2009 and £1,664.3m at 31 December 2008. The increase in net asset value for the year was primarily attributable to the revaluation surplus on investment properties of £173.7m and the profit after tax for the year of £87.0m.

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.

BUSINESS REVIEW (Continued)

Adjusted NAV per share at 31 December 2009 is set out in the table below, which for comparison purposes also includes adjusted NNNAV per share.

	Note	**31 December 2009 £m**	30 June 2009 £m	31 December 2008 £m
Net assets per Consolidated Balance Sheet		**1,925.0**	1,514.3	1,664.3
Add back deferred tax		**70.0**	70.5	52.9
Net assets prior to deferred tax		**1,995.0**	1,584.8	1,717.2
Revaluation of property portfolio:				
– investment property	1	**190.0**	175.0	155.0
– properties held for development	2	**(26.5)**	(35.7)	60.2
– properties under construction to be retained	3	**–**	27.1	56.8
– properties under construction to be sold	4	**58.3**	87.3	130.2
Adjusted net assets		**2,216.8**	1,838.5	2,119.4
Fair value adjustments in respect of financial assets and liabilities less tax relief at 28.0%		**69.3**	230.8	188.7
Contingent tax on property disposals	5	**(78.0)**	(38.8)	(78.5)
Undiscounted deferred tax		**(91.2)**	(90.1)	(67.8)
Adjusted NNNAV		**2,116.9**	1,940.4	2,161.8
Adjusted net assets per share	6	**£3.47**	£2.88	£3.32
Adjusted NNNAV per share	6	**£3.31**	£3.04	£3.38

Note:
1 The market value of 25-30 Bank Street reflected in the balance sheet at 31 December 2009 of £360.0m (30 June 2009 – £375.0m, 31 December 2008 – £410.0m) excludes the benefit of the arrangement with AIG which provides for the payment of 4 years' contracted rent upon default by Lehman as the arrangement cannot be transferred to a purchaser of the property. The market value of this building, adjusted to include the arrangement with AIG, is £550.0m (30 June 2009 – £550.0m, 31 December 2008 – £565.0m). The valuation uplift does not allow for the ongoing commitment fees payable by the Group to AIG of approximately £3.6m per annum.
2 Revalued at market value in existing state.
3 Revalued at market value in existing state. 5 Churchill Place was completed in the year and transferred to investment properties held for sale.
4 Uplift to market value on pre-sold properties under construction at the balance sheet date of £58.3m (30 June 2009 – £202.8m, 31 December 2008 – £314.1m) less cumulative profit of £nil recognised to 2009 (30 June 2009 – £115.5m, 31 December 2008 – £183.9m) (refer to 'Business Review – Valuations').
5 Refer to 'Business Review – Tax'.
6 Calculated by reference to the closing number of shares of 639.0m at each balance sheet date. There were no dilutive instruments outstanding at either date.

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 the adjusted NAV per share. In calculating the 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.

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 since the year end there have been 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.

BUSINESS REVIEW (Continued)

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 being closely monitored in light of the forthcoming general election.

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 below.

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 2009 and 31 December 2008 all of the Group's borrowings were fixed after taking account of interest rate hedging and cash deposits held as cash collateral (see Note 16(8)).

Liquidity risk
The Group's policy is to ensure continuity of funding and at 31 December 2009 the average maturity of the Group's debt was 14.0 years (2008 – 14.8 years). Shorter term flexibility is achieved by holding cash on deposit and through construction facilities typically with a term of 3 to 6 years arranged to fund the development of new properties. None of the Group's facilities matures before 2013.

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

BUSINESS REVIEW (Continued)

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 61.2% of the investment property portfolio by value. The principal amount outstanding at 31 December 2009 was £2,519.6m or £2,399.8m excluding the repurchased Notes.

Maximum LMCTV ratio of 100%. Based on the valuations at 31 December 2009, the LMCTV ratio at the interest payment date in January 2010 would have been 83.8%, excluding the £224.0m of cash collateral posted by AIG in respect of the 25 Bank Street facility, and 76.2% including such cash collateral.

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 £576.2m secured against One Churchill Place, representing 14.7% of the investment property portfolio by value.

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

(iii) Loan of £358.9m secured against 10 Cabot Square and 20 Cabot Square, representing 12.6% of the investment property portfolio by value. Both properties are now primarily let to Barclays Capital.

Maximum LTV ratio of 85.0%. Based on the valuations at 31 December 2009 the LTV ratio at the interest payment date in January 2010 would have been 62.7%.

This facility is also subject to a minimum ICR test of 100%. During the year Morgan Stanley gave notice to break its lease on 20 Cabot Square with effect from February 2010. To prevent the serving of the notice leading to a breach of the minimum ICR test, a portion of the swap was broken at a cost of £8.1m and a new swap entered into which serves to fix the rate of interest at a weighted average, including margin, of 5.6%. The ICR covenant was satisfied throughout the year. Following the restructuring of the Barclays Capital leases the Board anticipates that the Group will be able to meet the ICR covenants for the remaining term of the loan to January 2013.

The Group has the ability to remedy a breach of ICR or LTV covenants by depositing cash.

(iv) Loan of £350.0m secured against the principal retail and infrastructure parking properties of the Group, representing 11.5% of the investment property portfolio by value.

Maximum LTV ratio of 75.0%, reducing to 70.0% from March 2010. Based on the valuations at 31 December 2009, the LTV was 66.8%.

On 7 March 2009 the maximum ICR covenant increased from 110.0% to 120.0%. The maximum ICR covenant was satisfied throughout the year. The Group has the ability to remedy any potential breach of covenant by depositing cash.

On 17 December 2009, the facility repayment date was extended from 7 March 2011 to 17 December 2014. An upfront arrangement fee of £4.0m was paid and the margin on the loan was fixed at 2.75% for the duration of the loan. The negative mark to market valuation on the pre-existing swaps, amounting to £19.97m, was blended into a new 5 year swap, executed at an all-in rate of 4.425%. The interest rate on the loan is therefore fixed at 7.2%.

(v) Construction loan facility of £155.0m secured against 5 Churchill Place of which £123.4m was drawn down at 31 December 2009.

This loan was repaid in January 2010 following the sale of the property.

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.

BUSINESS REVIEW (Continued)

The Drapers Gardens entities entered into a £172.5m construction loan facility with Lehman which was subsequently syndicated to certain other banks with Lehman retaining a minority share. Following Lehman being placed into administration there was an interruption to the funding being provided by Lehman and the Group made additional loans totalling £1.0m (31 December 2008 – £0.7m) to the joint venture to fund its 20.0% share of the shortfall. Lehman subsequently recommenced funding and all of its lending obligations were satisfied up to 31 May 2009. For the remainder of the year, funding for the project was provided by one member of the syndicate on a super senior loan basis. Subsequent to the year end, in January 2010, the Group acquired the substantial majority of the drawn balance of the loan for £112.8m.

Borrowings

At 31 December 2009, net debt (after cash in hand and cash collateral) stood at £2,843.1m, down from £2,900.8m at 31 December 2008, and comprised:

	31 December 2009 £m	31 December 2008 £m
Securitised debt	**2,484.7**	2,637.5
Loans	**1,276.4**	1,305.6
Finance lease obligations	**41.2**	41.6
Construction loan	**123.4**	99.9
Total borrowings	**3,925.7**	4,084.6
Less:		
- cash collateral for borrowings	**(139.4)**	(135.0)
- cash collateral for construction	**(18.3)**	(25.1)
- other cash collateral	**(10.0)**	(12.4)
	3,758.0	3,912.1
Less: cash deposits	**(914.9)**	(1,011.3)
Net debt	**2,843.1**	2,900.8

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 2009 and throughout the year then ended.

The decrease in total borrowings from £4,084.6m to £3,925.7m reflects the repurchase of securitised debt and scheduled amortisation, partially offset by an additional £20.5m drawn down under the Group's construction loan facility. The reduction in cash and term deposits from £1,183.8m to £1,082.6m is primarily as a result of the funding of construction costs and the repurchase of securitised debt, which was partly offset by receipts in the period under the long term contracts relating to Riverside South and 15 Canada Square. The construction loan secured against 5 Churchill Place was repaid in January 2010 upon completion of the sale of the property.

At 31 December 2009 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 an unrecognised asset of £96.2m before tax relief (31 December 2008 – asset of £262.1m).

At 31 December 2009, the Group's weighted average cost of debt was 6.3% excluding credit wraps (or 6.4% including credit wraps) in comparison with 6.0% excluding credit wraps (or 6.2% including credit wraps) at 31 December 2008.

BUSINESS REVIEW (Continued)

Cash flow

Net cash inflow from operating activities for 2009 was £331.4m in comparison with £184.8m for 2008, an increase of £146.6m. This increase was primarily attributable to an increase in the net proceeds from properties in the course of construction which were pre-sold. Excluding this item operating cash inflows increased from £266.1m to £295.5m.

Returns on investments and servicing of finance resulted in an outflow of £242.0m for 2009 compared with £186.7m for 2008. The reduction in returns on investments was primarily attributable to the fall in margins earned on the Group's cash balances. The total for 2009 included £8.1m of swap breakage costs. There were no such costs in 2008.

Capital expenditure and financial investment for 2009 resulted in a cash outflow of £112.9m, compared with an inflow of £59.2m for 2008. 2009 expenditure included £90.8m of development expenditure, excluding expenditure on pre-sold buildings, and funding of the Group's investment in associated undertakings of £5.2m. The 2008 amount included £167.1m of development expenditure incurred on properties excluding pre-sold properties, and funding of the Group's investment in associated undertakings of £8.7m, offset by proceeds from the sale of the Riverside South site of £237.9m.

The financing cash outflow for 2009 was £62.9m compared with an inflow of £93.2m for 2008. 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. The 2008 cash outflow included £59.6m drawn down under the Group's construction loan facility and £50.0m drawn down under the Group's retail loan facility.

CONSOLIDATED PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31 DECEMBER 2009

	2009 £m	2008 £m
Turnover	**481.3**	697.2
Cost of sales	**(164.3)**	(288.9)
GROSS PROFIT	**317.0**	408.3
Administrative expenses	**(38.4)**	(40.2)
Other operating income	**2.8**	1.5
OPERATING PROFIT	**281.4**	369.6
Exceptional items:		
– movement of impairment on investment in associates before interest and tax	**13.8**	(23.2)
– profit on sale of development property	**–**	118.6
Interest receivable	**14.2**	47.0
Interest payable:		
– before exceptional item:		
– Group	**(242.7)**	(242.6)
– associates	**(0.3)**	(0.5)
Exceptional item:		
– gain on repurchase of securitised debt	**68.4**	–
	(174.6)	(243.1)
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION	**134.8**	268.9
Tax	**(47.8)**	(19.4)
PROFIT FOR THE FINANCIAL YEAR	**87.0**	249.5
Basic and diluted earnings per share	**13.6p**	39.0p

CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES FOR THE YEAR ENDED 31 DECEMBER 2009

	2009	2008
	£m	£m
Profit for the financial year after tax:		
– Group	**73.5**	273.2
– share of profit/(losses) of associated undertakings	**13.5**	(23.7)
Unrealised movement on revaluation of investment properties	**173.7**	(1,689.9)
TOTAL RECOGNISED GAINS AND LOSSES RELATING TO THE YEAR	**260.7**	(1,440.4)

CONSOLIDATED BALANCE SHEET AT 31 DECEMBER 2009

	2009 £m	2008 £m
FIXED ASSETS		
Investment properties	**4,584.5**	4,245.5
Properties under construction	**–**	125.7
Properties held for development	**247.5**	199.8
Other tangible fixed assets	**1.5**	1.9
Investments	**37.4**	22.7
	4,870.9	4,595.6
CURRENT ASSETS		
Debtors: Amounts due in more than one year	**194.5**	243.7
Debtors: Amounts due within one year	**53.2**	80.4
Cash at bank and in hand	**1,082.6**	1,183.8
	1,330.3	1,507.9
CREDITORS: Amounts falling due within one year	**(377.0)**	(372.4)
NET CURRENT ASSETS	**953.3**	1,135.5
TOTAL ASSETS LESS CURRENT LIABILITIES	**5,824.2**	5,731.1
CREDITORS: Amounts falling due after more than one year	**(3,811.5)**	(3,995.4)
Provisions	**(87.7)**	(71.4)
NET ASSETS	**1,925.0**	1,664.3
CAPITAL AND RESERVES		
Called up share capital	**6.4**	6.4
Reserves:		
– share premium	**146.2**	146.2
– revaluation reserve	**1,695.6**	1,521.9
– capital redemption reserve	**0.7**	0.7
– special reserve	**264.8**	264.8
– profit and loss account	**(188.7)**	(275.7)
SHAREHOLDERS' FUNDS	**1,925.0**	1,664.3

CONSOLIDATED CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2009

	2009 £m	2008 £m
NET CASH INFLOW FROM OPERATING ACTIVITIES	**331.4**	184.8
Returns on investments and servicing of finance	**(242.0)**	(186.7)
Capital expenditure and financial investment	**(112.9)**	59.2
Tax	**(14.8)**	–
Equity dividend paid	**–**	(102.2)
	(369.7)	(229.7)
Cash outflow before management of liquid resources and financing	**(38.3)**	(44.9)
Management of liquid resources	**4.8**	107.3
Financing	**(62.9)**	93.2
(DECREASE)/INCREASE IN CASH IN THE YEAR	**(96.4)**	155.6

DEFINITIONS

Administrator	Administrator of Lehman Brothers Limited (in administration)
AIG	American International Group, Inc
Ballymore	Ballymore Properties Limited
Barclays Bank	Barclays Bank PLC
BlackRock	BlackRock Investment Management (UK) Limited
bn	billion
Board	Board of directors of Canary Wharf Group plc
bps	Basis points
BWB	British Waterways Board
Cat A	Category A fit-out
CBRE	CB Richard Ellis Limited, Surveyors and Valuers
City	The City of London
CLRL	Cross London Rail Links Limited
Company	Canary Wharf Group plc
Cushman	Cushman & Wakefield, Real Estate Consultants
CWEL	Canary Wharf Estate Limited
CWF II	Canary Wharf Finance II plc
CWHL	Canary Wharf Holdings Limited
Drapers Gardens	Drapers Gardens scheme in the City of London
Estate	Canary Wharf Estate including Heron Quays West, Riverside South and North Quay
EZAs	Enterprise Zone Allowances
Fimalac	F Marc de Lachariere
Fitch	Fitch Ratings Limited
FRNs	Floating Rate Notes
FRS 3	Financial Reporting Standard 3 (Reporting Financial Performance)
FRS 13	Financial Reporting Standard 13 (Derivatives and Other Financial Instruments)
FRS 19	Financial Reporting Standard 19 (Deferred tax)
FSA	Financial Services Authority
Group	Canary Wharf Group and its subsidiaries
HMRC	Her Majesty's Revenue and Customs
ICR	Interest Cover Ratio
JPMM	JP Morgan Markets
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
SFL	Songbird Finance Limited
Skadden	Skadden Arps Slate Meagher & Flom LLP
Songbird	Songbird Estates plc
sq ft	square feet/square foot
SSAP 9	Statement of Standard Accounting Practice 9 (Stocks and Long Term Contracts)
SSAP 19	Statement of Standard Accounting Practice 19 (Accounting for Investment Properties)
TfL	Transport for London
UITF 28	Urgent Issue Task Force 28 ('Operating Leases')
VAT	Value Added Tax
WPP	WPP plc
WWLP	Wood Wharf Limited Partnership