Half-yearly results presentation – 12 November 2008
Speaker notes

Speaker: Francis Salway, Chief Executive

Slide 1 - Introductory slide

Good morning and welcome.

As always, this is your opportunity for relief from BlackBerrys and mobile phones, so please take it.

We have been through a period of massive upheaval in financial markets. It has impacted on confidence, on availability of capital and, hence, on pricing of investments.

But it is my experience that in downturns it is income that ultimately provides support to values. And the property sector has income flows with good defensive qualities, which bring broad stability of earnings. Martin and I will be focusing particularly on income and resilience of income.

Slide 2 – Business highlights

I have picked out three highlights from the half year. The first relates to our success on letting up the two developments we completed. They are 92% let. Our office refurbishment in Eastbourne Terrace in Paddington was fully pre-let before completion and our development with Hammerson of Cabot Circus in Bristol was over 90% let at the time of opening.

In terms of our income statement, we saw 13.3% growth in underlying revenue profit. This was supported by growth in rental income on our like-for-like investment portfolio at 3.7% if you exclude development pipeline properties which are naturally being vacated in the run up to redevelopment.

We have also recently had changes on our board. It was with great regret that we lost Paul as our Chairman to become a Government Minister in the Treasury. But we are known for having a strong board, and I am sure it will come as no surprise that we have continuity with the appointment of Alison Carnwath as our new Chairman, who is here this morning.

Slide 3 – Demerger

On demerger, the activity around a potential sale of Trillium continues but, as with other transactions, involves a more protracted process in current market conditions.

In terms of the demerger of our London and Retail businesses, we announced our plans to demerge almost a year ago today. And we said then that demerger would – and I quote – “be executed only when market conditions are favourable”.

The preparatory work has progressed well and all three businesses have seen operational benefits, but, market conditions certainly cannot be described as favourable. Our board continues to believe in the benefits of specialisation, but has decided that, given the current financial environment, it would not now be in our shareholders interest to proceed with demerger. So, the file is closed. Our current focus is 100% on effective management of the business in these challenging times.

I will now handover to Martin who will cover the detailed financial results.

Speaker: Martin Greenslade, Group Finance Director

Slide 5 – Financial highlights

Thank you Francis. Good morning everyone.

This morning we have reported a pre-tax loss of £1.74bn pounds on the back of a valuation deficit of £1.72bn. This deficit represents a 12.7% decline in the value of our assets since 31 March and Francis will provide further details in a minute.

Revenue profit at £195.8m was 13.3% higher than last year. This performance resulted from higher net rental income and a lower interest charge on PPP assets held for sale. As you will recall, there is an interest cost associated with owning these PPP investments but we do not recognise any related income. With the creation of the TIP fund last year and the sale of the majority of these assets into that fund, the interest cost on assets held for sale has reduced to just £6.5m this period, an improvement of £18.9m.

Adjusted diluted earnings per share at 41.83p showed similar growth to revenue profit, up 14.7%.

On the back of the valuation decline, adjusted diluted NAV per share declined by 20.7% to 1552p. I will describe the main components of this in a moment.

Finally, we have confirmed the second quarterly dividend at 16.5p, which is the same level as our first quarter dividend. Our dividend cover at the half year was 1.3 times.

Let's turn now to our consolidated income statement…

Slide 6 – Consolidated income statement

I will highlight just a few key items. Underlying operating profit was up over 6%, with Retail little changed but increases in London and Trillium. More on that in a moment.

Demerger costs in the half year were £16.4m. As Francis explained, having made good progress on our internal preparations towards demerger, we have ceased work given current market conditions. I would not, therefore, expect further costs in the second half, other than in relation to the potential sale of Trillium.

The valuation surplus on this slide relates to our subsidiaries only and includes investment properties in Trillium, principally on Royal Mail and Accor. Under IFRS the performance of our joint ventures comes through on a post tax basis further down the income statement. In the appendix section of your packs, pages A2 and A3, you will find a proportionately consolidated income statement and balance sheet. The negative return on JVs which you see on this slide is due to a £206.4m valuation deficit in those JVs.

During the current period, we took the decision to impair the goodwill associated with Trillium, resulting in an exceptional charge of £147.6m. A number of Trillium's new business prospects, in particular the ongoing activities associated with the TIP fund, require long term debt to enhance returns. Given the current credit markets, we have taken a prudent view of the discounted cashflows off our Trillium business with the result that we have chosen to impair the associated goodwill.

The majority of our disposal activity occurred in the early part of the period enabling us to generate a very small profit on disposal of £1.5m compared to £79.0m in the first half of last year. As I mentioned on my first slide, the establishment of the TIP fund and the transfer of assets into it has resulted in a lower interest cost in the period and this is reflected here with a reduction in net interest payable of £14.4m.

Discontinued operations relates to the PPP assets held for sale, where the disposal of a number of these investments contributed to the £14.7m profit in the first half.

Slide 7 – Rental income analysis

The main driver behind operating profit for London and Retail is changes to gross rental income, the breakdown of which is shown here. In our Retail Portfolio like-for-like income increased by £4.2m, largely due to the impact of rent review settlements, offset by a fall in income on properties that are being prepared for development. We have separated these properties within the like-for-like category because of the distortion they create. This can be seen in London, where, in the like-for-like portfolio, rents on investment properties increased by some £3.4m but this was offset by a decline in rental income of £3.2m on our pre-development properties. The main growth came from new Scotland Yard and 47 Mark Lane, while Arundel Great Court was the main pre-development property where income declined. The loss of this income will continue to be felt in the second half of 2008.

Completed developments, particularly in London, were the main driver behind higher rental income contributing £29.4m and offsetting the £21m decline caused by our net disinvestment of standing investment properties compared to 2007.

Turning now to Trillium….

Slide 8 – Trillium

The factors behind Trillium's performance in the first half of this year were very similar to those I presented for the last financial year in May. Operating profits were up 5.5% versus the comparable period due to the performance of new contracts and around £17.7m of one-off items.

On the DWP contract, the department continues to use its vacation allowance and vacations resulted in a net loss of income of £12.4m compared to last year. This decline in operating profits was more than offset by indexation, which increased income by £5.5m, and one-off including historic shared savings which contributed £17.7m. DWP's underlying operating profits, excluding these one-off items, was £41.5m.

The Norwich Union and DVLA contracts showed strong growth in operating profit. These contracts benefited from the additional income generated from completed refurbishments and scope extensions.

The decline in operating profit from the Telereal II contract is in line with expectations as part of this contract has now expired. The remainder of the Telereal II contract will expire in March 2010.

The Royal Mail contract shows a loss of £2.6m in the half year. Having reviewed our assumptions on vacant space in the current market environment, we have increased our onerous leave provision on this space by £4.3m, offsetting our net rental income of £1.7m.

Accor's apparent strong performance versus the comparable period reflects the fact that this business was not at its full run rate in the prior period.

Bid costs were higher, largely due to expenditure on the Defence Training Review opportunity where we have moved into the design phase of what is effectively a three million sq ft development.

Below underlying operating profit are a few other Trillium-related items. I have already covered goodwill and Francis will cover the valuation deficit in a minute. Disposal of the freehold space vacated by DWP resulted in a modest profit of £2.2m compared to last year which included the sale of Hinchley Wood. That brings me to PPP assets which is the subject of the next slide.

Slide 9 – PPP investments and Trillium Investment Partners

During the period we sold a further 13 projects into the Trillium Investment Partners fund, resulting in a profit on disposal of £17.3m.

At the period end we had £165.9m of PPP assets held for sale on our balance sheet.

With regard to our remaining 10% share in the fund, which is accounted for as an associate, the loss largely relates to movements on swaps and hedges in the fund. However, my advice to you in May was to look at the cash. In this six month period, we received a distribution of £2.0m on our book investment of £42m.

Slide 10 – Movement in revenue profit

This slide summarises the previous information, showing you the main reasons for the increase in our revenue profit.

Net rental income was £18.4m higher driven by completed developments, particularly in London partly offset by our net disinvestment of standing investment properties. Against this, there were higher interest costs which I will cover in a moment.

The next three items relate to Trillium. Operating profits including joint ventures at Trillium increased by £2.8m, principally DWP and Accor offset by bid costs. As mentioned earlier, interest associated with assets held for sale declined by some £18.9m compared to last year. Other interest in Trillium rose to reflect higher capital employed in Norwich Union, DVLA and a full six month effect of Accor.

Turning to the rest of the Group, interest increased by £9.2m. This reflects the fact that we stopped capitalising interest on the completed developments at Princesshay and New Street Square, resulting in an increased interest cost of £3.1m. In addition, we paid the REIT conversion charge in July 2007 and therefore the comparable period included only three months of related interest costs, the difference being around £4m.

Finally, service charge and direct recoveries fell, mainly associated with voids on two pre-development properties, namely Arundel Great Court and Leeds Plaza.

Slide 11 – Movement in adjusted diluted NAV

This slide sets out the drivers behind the 20.7% decline in adjusted NAV.

As you would expect the most significant factor is valuation declines, represented by the first three bars. Developments marginally outperformed as they accounted for 14.8% of investment properties by value but only 11.5% of the valuation deficit.

Including joint ventures, our disposals made a small profit of £3.4m, while our PPP assets contributed a further £14.7m to adjusted NAV.

Dividends equated to about three-quarters of the adjusted earnings. With goodwill impairment, demerger costs and a small other reserve movement, our adjusted diluted NAV ended the period at 1552p. Just for the record, our diluted triple net assets per share were 1668p.

Slide 12 – Cash flow and debt

Let's move on to cash flow and net debt. The increase in operating cash flow compared to last year is due to lower interest costs and lower tax payments following REIT conversion.

The reduction in dividend cash outflow reflects the payment of two quarterly dividends this year versus the payment of a final dividend of 34.0p last year.

As you would expect, total capital expenditure was significantly lower than last year. Investment property acquisitions were £32.4m compared to £552.7m last year when we acquired Thomas More Square and the further 50.5% interest in Times Square in Queen Victoria Street. Trillium property acquisitions and capital expenditure was also much lower as the prior year includes the acquisition of the remaining nine Accor hotels and capital expenditure on Norwich Union and DVLA properties.

Development expenditure was also lower reflecting the completion of Princesshay and New Street Square.

Disposals includes £103m from assets sold into Trillium investment partners and £212.5m from investment property sales, some of which exchanged last year but cash was received in the period, and £30.5m from the sale of Trillium freehold properties.

The cash inflow from joint ventures reflects the disposal of Empress State into a 50:50 joint venture with Liberty International and the proceeds from gearing the joint venture, partially offset by further investment in Cabot Circus and St David's shopping centres.

The net of all those cash flows resulted in a reduction in net debt of £175m.

Slide 13 – Gearing

Despite the reduction in net debt, the fall in property values has resulted in a rise in gearing. Adjusted gearing, which we feel is the more appropriate measure, increased from 64.9% at 31 March to 79.3% at 30 September which is equivalent to 45.4% on an LTV basis.

With the disposal of the majority of our PPP assets held for sale into the TIP fund, our interest cover ratio increased from 1.93x to 2.14x. But you can see from the slide, excluding the disposal group interest, our interest cover has remained broadly stable.

Slide 14 – Security Group

In response to a number of questions I have received about debt covenants, I wanted to remind you about our debt structure. Essentially, we have a secured group, shown here on the right hand side, and a non restricted group shown on the left hand side. The non restricted group includes Trillium, other than the Accor properties, and our joint ventures and sundry other assets. We can, and do, raise some debt against these assets. However, the overwhelming majority of our external debt is lent to the secured group, which provides fixed and floating charges over the majority of our investment properties. At 30 September, we had just under £10 billion of assets in the Security Group, securing £5.34 billion of debt, giving an LTV ratio of 53.4%.

Now, how does our covenant structure work? Well, the first thing to say is that financial covenants do not trigger an event of default until LTV exceeds 100% or our projected interest cover ratio is less than 1 times. However, what is more relevant is that our secured debt structure is characterised by different operating environments (or Tiers) which respond to changes in LTV and ICR – although I have to say that it is LTV which is more likely to determine which operating environment applies. What happens is that the operating environment becomes more restrictive at higher levels of LTV or lower levels of ICR. There are minimal operating restrictions on the group in Tier 1 and Tier 2, which means up to an LTV of 65%, although we are required to put in place a liquidity facility progressively as our LTV moves up from 55% to 70%. In Tier 3, our operating environment does become more restrictive with provisions designed to encourage a reduction in gearing including mandatory debt amortisation. Should you want more information on this, there is plenty on our website under the investor section.

One final comment, the Security Group LTV only moved up from 50.5% at 31 March to 53.4% at 30 September, despite the sharp declines in property values. This was partly because we had a reduction in net debt over the period but more importantly because we were able to contribute to the security pool additional assets which we hadn't secured in the past. We still have the potential to move further assets into the Security Group.

Finally, let me now turn to our debt maturity profile and financing position.

Slide 15 – Financing

Over the last six months we have extended existing facilities or signed new agreements totalling over £1.2bn for group companies and a further £296m for joint ventures. No mean feat in the circumstances and testament to the strength of our treasury team and the quality of our assets.

As at 30 September, we had £106m of facilities which mature before 31 March 2010. These were loan notes, related to the acquisition of Tops Estates, which have now been repaid.

The graph here shows how our debt facilities are expected to expire over the years. As you can see, apart from the loan notes, we have no facilities expiring until after 31 March 2010 and all of these facilities have at least one year term out options.

At 10.7 years, our weighted average debt maturity is reasonably long and our weighted average cost of debt at 5.4% is still very attractive. We are around 81% hedged on our debt so we do have some exposure to falling interest rates. A 1% decline in LIBOR would deliver an annual saving of £11.4m. Finally, we have undrawn committed facilities of £874m, of which £200m relates to a specific development. On top, we have an additional £100m of cash and money market facilities.

Let me put those facilities into the context of one of our largest cash flow items, namely development capex. Our total future capital expenditure to which we are committed on all our developments over the next 30 months or so, is approximately £700m.

I must stress that the above is a static view and our facilities and cash management are dynamic as can been seen from the changes over the last six months. We will continue to manage our banking facilities and cash flows most carefully so that we are able to capitalise on attractive opportunities which will arise in due course from the growing spread between property yields and funding costs.

Let me now hand you back to Francis.

Speaker: Francis Salway, Chief Executive

Slide 16 – Business review

Thank you, Martin. I will now cover the results of the half year revaluation and activities across the business.

Slide 17 – Investment portfolio valuation results

As Martin said earlier, the first half saw a 12.7% valuation deficit.

There is no great variance between sectors – other than for our central London retail holdings which showed extreme resilience. This reflected ongoing retail sales growth in Central London and also successful asset management initiatives by our team.

You will see from the differential between the two right hand bars that our total portfolio performed better than the like-for-like investment assets. There are two reasons for this: firstly, the recently completed and ongoing developments benefited from the release of profit allowances for schemes we de-risked, whether through practical completion or leasing progress – or both, as at Bristol.

And, secondly, our like-for-like portfolio was impacted negatively by the fact that prospective future development sites sit within this category. So, without the development pipeline properties which include 20 Fenchurch Street, Arundel Great Court and the Trinity Centre in Leeds, the valuation change on the balance of the like-for-like portfolio would have been 0.8% better. The pre-development properties themselves showed an average valuation deficit of 27.1%. So, development sites have been sharply marked down in value, but the impact on the overall portfolio has been modest.

Slide 18 – Analysis of performance relative to IPD

After 12 months of significant out-performance relative to IPD in the year to March 2008, we saw under-performance over the last 6 months, but by a much smaller amount. This was partially explained by the sector mix of our portfolio, as you can see from the extreme right hand bar.

But the biggest contributor was greater adverse yield movement - our equivalent yields moved by 82 bps (on IPD's measurement) as compared to 69 bps for the IPD quarterly universe.

Slide 19 – Investment portfolio sales

Consistent with general market trends, we had lower levels of investment transactions over the period.

We sold £181.5m of property at an average of 1.7% above the March 2008 valuation (before disposal costs). The yield on properties sold was 5.6%. The most significant disposal was the half interest in Empress State building put into a joint venture with liberty who own the adjoining Earls Court land.

Other smaller sales included an Aparthotel in Holborn which we sold to the operator.

Slide 20 – Reversionary potential

With the settling of rent reviews over the last six months and the slight reduction in rental values, the net reversionary potential of our investment portfolio has decreased slightly, but still stands at 10.5%. Encouragingly, rent review settlements over the six months were 3.9% above valuers' ERV.

Slide 21 – Voids

Headline void levels across the whole portfolio moved up from 3.9% in March to 6.3% in September. But, these figures are distorted by development pipeline properties where leases have been expiring to allow for redevelopment. The diagonally hatched bars show voids on development pipeline properties. Excluding these, and focusing on the solid bars, you can see that on this basis, our normalised voids only moved from 3.4% to 4.0%.

Within the retail sector, voids actually fell because our retail warehouses voids came down significantly from 2.6% to an incredibly low 1.0%. Adjusted shopping centre voids are running at a slightly higher level at 5.2%, up from 4.3% in March.

Excluded from our void figures are units in insolvency where the lease is still held by the Administrator. Such units represent 1.8% of our total portfolio. Within that figure, and looking specifically at our retail assets, units in insolvency still held by the Administrator represented 2.9% of retail income. Of these, over a quarter are still trading and paying rent.

And, as an aside, our statistics on rent collection within five and 10 days from the September quarter day were better than June 2008 and better than September 2007.

Slide 22 – Investment portfolio

Our average lease length is now 8.6 years on the like-for-like portfolio and 9.5 years if you include acquisitions and completed developments.

In truth, what really matters is not whether average unexpired lease terms are 10 or 15 years, but what the exposure is in the next two or three years.

And our exposure to breaks and expiries over the next three years is less than implied by simply spreading an average nine years unexpired lease term. The reason is because we actively manage the pattern of expiries and breaks, and I will give you an example of this later.

In terms of near term security of income, this bar chart shows the proportion of income subject to expiries or breaks over each of the next three years. The diagonal hatching relates to tenancies which we want back to accommodate development. Excluding the diagonal hatching, the annual average expiries and breaks over each of the next three years represents 4.3% of total portfolio income per annum. And some of these are absolutely rock solid such as lease expiries at Piccadilly Circus Lights two years before the Olympics.

Slide 23 – Profile of cash rents / ERV

Now this slide comes with a health warning. It is good for our shareholders, but bad for your eyes. Do not attempt to read the figures on the screen, but do absorb them in print form afterwards.

As I said, I am a great believer that, in times of downturn, it is income which ultimately provides support to values. So I think it is right for us to provide as much detail as possible on the income profile of our investment portfolio and its growth potential. The information shown on this slide and in your packs is new in terms of disclosure and, I hope, will be helpful to you.

Slide 24 – Retail Portfolio

Turning to our Retail Portfolio, and covering just like-for-like investment properties, the valuation deficit was 14.3%. Rental value change moved from low positive to low negative, although almost half of our shopping centres and three quarters of our retail parks saw flat or even low positive rental value change.

Our High Street shops saw positive growth in rental values because of the shops in Bristol outside the Cabot Circus development which have benefited enormously from its opening.

Slide 25 – Retail development

Of our major retail development projects, the 2007 openings at Exeter, Corby and Cambridge are now 97% let.

Our two major retail developments for the current year are Cabot Circus in Bristol, developed with Hammerson, and the extension at Livingston. Both are now open with Livingston being 82% let or in solicitors hands and Bristol 91%.

The bar chart in the lower half of the slide shows the pattern of shopping centre development completions across the whole of the UK. Despite a peak of completions in 2008, these schemes across the country have generally been letting up well.

Looking forward to 2009, completions are at a quarter of the 2008 level. The largest national completion in 2009 is the St David's 2 scheme in Cardiff, which we are developing in partnership with Liberty. It is currently 47% let or in solicitors hands by area, or 33% by income. Our marketing was specifically planned to avoid competing with the 2008 completions, and the leasing team is now making a real push on lettings.

Slide 26 – Retail – delivering developments

It is worth saying a few words about our Cabot Circus scheme in Bristol. It has been an outstanding success, confounding commentators' pessimism about the challenges of opening a new scheme in 2008. 70% of the retailers are new to Bristol and we delivered over one million shoppers past their doors in the first 10 days. Even with recent outward yield movement, the scheme has delivered a profit on cost of 14.2%.

Slide 27 – Retail – tenant diversification

At a time when national newspapers are providing extensive coverage of retailer insolvencies, it is important to recognise the degree of tenant diversification which we have across our portfolio.

You will see from this pie chart that our largest single retail tenant, Arcadia Group, represents only 1.7% of our total investment portfolio income.

Slide 28 – London Portfolio

Turning now to our London Portfolio, and the like-for-like properties, capital values were down 20.2% in the City, but only 10.8% in the West End. So we benefited from having 38% of our London Portfolio in West End offices.

The performance of our West End offices was supported by Queen Anne's Gate, which is our third largest asset and benefits from a long lease to the Government with fixed increases in rent - and so suffered a fall in value of only 3.5%.

Excluding development pipeline properties, the average gross income yield on our like-for-like London offices now stands at 6.3% or, in valuation terms, this is a net initial yield of some 5.9%.

By far the most resilient performance across our portfolio came from central London retail, where values fell by only 1.9% and rental values were up 3.8%. The growth in rental values was driven largely by asset management initiatives at the east end of Oxford Street and on the Piccadilly Circus lights block.

Slide 29 – London Portfolio – timing of development completions

This bar chart shows the profile of completions of our London developments with the bars sized according to the total development cost for each scheme. You will see that the peaks and troughs of the profile of our developments are broadly matched to what are likely to be the peaks and troughs of the cycle.

In terms of the near term, we have the 160,000 sq ft scheme at Dashwood House which we completed last month. As we are letting on a floor-by-floor basis, we have only just started marketing and we have early occupier interest in around five floors.

Our next major completion is at One New Change in the City in Autumn 2010. By income, the scheme is 37% retail and 63% offices. The offices are 38% pre-let. The unique location and views make us confident of securing office lettings, albeit that we will be exposed to general market pricing trends.

Beyond 2010, we have flexibility as to when we deliver projects. We are prepared to delay starts, where appropriate. This will have a short term impact on revenue profit as we sit on sites without income and without capitalisation of interest. However, it can be the right answer to ensure that we deliver the best total return for shareholders - as we evidenced with great success in the early and middle years of this decade, for example at New Street Square.

Slide 30 – London Portfolio – planning for the next cycle

Whilst we have to be cautious about the short term, we continue to plan for the longer term - to ensure that we are in a position to deliver developments as the market recovers. In Septemer and October, we submitted planning applications for a total of 1.9 m sq ft at Victoria Transport Interchange, Selborne House and Wellington House in Victoria together with Arundel Great Court in Mid-Town. These schemes can be delivered from late 2012.

Slide 31 – London Portfolio – asset management

In terms of asset management within the London Portfolio, we are pleased to have agreed terms with News International for a short-term letting of 191,000 sq ft at Thomas More Square, which we own jointly with Cadillac Fairview.

In Victoria, we have continued to work with various government departments to meet their changing accommodation needs. Following completion of the refurbishment of Queen Anne's Gate for the Ministry of Justice, we have agreed the removal of a 2010 break clause from DCLG's eland house with a rent roll of £12.4m and, in return, given them more flexibility on the smaller Ashdown House.

Slide 32 – London offices – tenant diversification

Within London offices, we do have a high exposure to one tenant, but that is the Government. So it is a strong positive. Beyond that, we are not overly exposed to the financial services sector with their contribution being very similar to that of professional services.

Slide 33 – Trillium

Trillium again demonstrated the operational strengths of its business.

DVLA is on its fourth contract extension and three of the projects have now been completed on programme and within budget.

And, as Martin has described, the Trillium Investment Partners fund structure is working well for our PPP business with a further £103m of contracts transferred into the fund.

On the new business front, we were delighted that we closed the Kent Building Schools for the Future contract, the largest BSF project to reach financial close so far in the UK. The project relates to 10 schools in the first phase and potentially a total of 35 schools. The construction cost for the first phase is £180m and our equity investment is £6m.

Slide 34 – Trillium – revaluation of investment properties

On this slide we show the six month movement in valuation for the investment properties within Trillium. Overall, the valuation deficit was less than on our main investment portfolio, because of the support provided by income growth, particularly on the Accor portfolio.

Accor showed a 7.7% reduction in values, but performance was supported by the fact that turnover for the nine months calendar year-to-date was up 3.7% - and it is the turnover growth for the full calendar year which sets our rental income for next year.

You will see a large positive increase in valuation for the DWP investment properties. This is attributable to the surplus upon transfer of properties from the occupational estate. These properties were previously held at depreciated cost and are now reported in the investment category at a revalued amount. On the former DWP properties classified as investments over the full period, the average valuation decline was 10.7%

Slide 35 – DWP contract

Whilst Trillium benefits from having a high proportion of its income index-linked, it does still have a material exposure to the real estate market through surplus accommodation. The surplus leasehold space creates an exposure to the commercial letting market and surplus freehold space tends to give an exposure to the residential land market in that many of the surplus freeholds have hitherto been sold for residential development or conversion.

You can see from this slide that we have disposed of an impressive 820,000 sq ft of accommodation in the six months including Trillium's largest ever single letting. We have also shed a further 350,000 sq ft through lease expiries and break clauses. This more than offsets the ongoing rate of vacation by our client at 750,000 sq ft. However, we do still have 2.2 million sq ft of vacant space under the DWP contract.

Not on this slide, but in the context of surplus space, I should also mention the Royal Mail portfolio. This contract started in March 2007 with 740,000 sq ft of surplus leaseholds. We have now reduced this to 490,000 sq ft and, of this, 120,000 sq ft is under offer.

Slide 36 – Outlook

In terms of the current environment and outlook, I have heard the CEO of one company wisely state that he could "add little to the long trail of negative economic and market assessments". It is tempting to stop at that. But, we do need a view on outlook to run our business effectively.

It is evident that investment property pricing has continued to deteriorate as we have moved through our half year end date of 30 September.

The industry will have to look to equity capital for investment inflows into the direct property market, and I am confident this will come. But the arrival of equity capital will not immediately reverse the supply-demand imbalance for property investments because of ongoing deleveraging.

As and when financial markets do attract net positive flows of capital, they have the potential to turn quite quickly. But, in our occupational markets, we will need to be patient as, in terms of occupier demand, property is a late cycle play. So, we expect a material time lag between turning points in the property investment and occupational markets.

Slide 37 – Maintain competitive advantage in a challenging market

Turning to Land Securities, our portfolio gives us good defensive qualities. And we work hard to create competitive advantage throughout the cycle. In this market, we benefit from a management team with experience of navigating cycles and with specialist expertise in their sectors. We have a flexible debt structure with progressive regimes rather than aggressive covenants, and we have taken action to increase our funding headroom over the last six months. We also have strong leasing teams with an unrivalled track record of securing lettings in both the retail and London office markets. And, as I said, the peaks and troughs of our development activity are broadly aligned to the cycle in occupational markets.

We are managing our business with a cautious outlook and with the flexibility required in these times. Our immediate priorities are around leasing and balance sheet management. Our medium term priority is to ensure that we have a development pipeline to capture recovering occupational markets.

I will now ask my colleagues to join me on the platform to take your questions. If you do want to ask a question, please raise your hand and a microphone will be brought to you. Please then give your name and company name.

For those of you watching via our live webcast, do click on “Ask the board a question” link to raise a question.