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Financial performance



Graham Roberts
Finance Director

Total return

British Land has delivered a total return of 34.6% in the year, before refinancing charges, compared with 18.8% (restated for IFRS) in the previous year. The valuation gains from active management and positive market conditions were amplified by our gearing levels, which went up during the year as a result of the Pillar acquisition and reduced through revaluation surpluses and disposals later in the year.

	March 2006	March 2005 ³	% increase
NAV per share ¹	1486p	1128p	31.7%
Dividends paid per share	16.1p	14.87p	8.3%
Total return ¹ per share	378p	161p	134.8%
Total return ^{1,2}	34.6%	18.8%	

¹ EPRA basis (note 2)

² excludes refinancing charges (note 2)

³ restated for IFRS

The principal drivers of total return were valuation uplifts on properties and investments in the Group and Joint Ventures which added £1,771 million or 337 pence to NAV. Our capital structure proved its worth during a period of high asset value growth as this increase represents 30% of the NAV at the beginning of the year.

Sales of properties added a further £182 million, 35 pence per share, as we sold properties into the strong investment market, reducing the higher level of debt created by our acquisition of Pillar.

Underlying profits added a further £228 million, 44 pence per share before tax, £185 million after tax.

Valuation movements and capital profits

The revaluation surplus for the year was £1,771 million, £1,316 million arising from wholly owned properties, £363 million from our share of Funds and Joint Ventures and £92 million from investments (principally Songbird Estates PLC). Our Songbird investment is now valued at £233 million.

The reasons for the valuation gains and the gains in property disposals against the March 2005 values are fully set out earlier in this review. Underlying profits, the refinancing charges and goodwill are explained further below.

Underlying profits

Underlying profits have increased from £181 million in 2005 to £228 million. The £47 million increase is summarised below:

	£m
New lettings and rent reviews (net of lease expiries)	15
Songbird dividend	16
Pillar (8 months) ¹	(3)
Debenhams and Spirit purchases	14
Effect of other purchases and sales	7
Broadgate & Sainsbury's refinancings	13
Non-recurring items ²	(7)
Other	(8)
Increase	47

¹ Net of £6 million management and £20 million performance fees

² Closure of Pillar offices, several small business units, redundancies and pension costs, net of new approach to rent review recognition and realignment of JV year ends

The Group has prepared a proportionally consolidated income statement and balance sheet (which are included on page 108) for the benefit of stakeholders who wish to see the results of the Group's interest in Funds and Joint Ventures on a look through basis. The following commentary refers to financial information of the Group as reported under IFRS where the after tax results of Funds and Joint Ventures are shown as a single line on the income statement.

Revenue returns

Gross rental and related income for the year is up 14.2% to £690 million and net rental income increased 13.9% to £589 million. The substantial acquisition and disposal programme over the last two years being the key drivers of change, as follows:

	£m
Gross rental and related income	£m
Year ended 31 March 2005 (restated for IFRS)	604
Purchases	69
Sales	(14)
New lettings and rent reviews	29
Lease expiries	(12)
Other	14
Year ended 31 March 2006	690

The growth principally arises from the benefit of a full year of acquisitions made in 2005 and new lettings net of the impact of sales. Significant sales were made late in the year (e.g. the residential portfolio and our investment in Plantation Place) and so had a relatively small impact on this year's rents. Their full year impact will be visible in 2007. The impact of the purchases of the Spirit and Debenhams portfolios (purchased in 2005) includes the effect of the minimum guaranteed rent increases of 2.5%. Accounting standards require these increases to be spread over the lease term resulting in earlier recognition of the income in the initial years of the lease.

Net rental income is 85.4% of gross rental and related income, after development costs and individual asset management initiatives charged to property income. The growth in rental income on a like for like basis (including our share of Joint Ventures and Unit Trusts) – that is excluding purchases, sales, developments and adjusting for asset management initiatives – was 2.7%, ahead of the market overall (IPD at 2.1%). The 2.7% reflects 1.1% on offices and 4.0% on retail properties.

The accounting policy for the recognition of rent reviews has been changed in the year to recognise the benefit of rent reviews from the date of review. This has increased rents by £4 million.

Funds and Joint Ventures

The contribution to underlying profit from Funds and Joint Ventures is £39 million, an increase of 25.8% from £31 million reflecting the purchase of the Fund interests as part of the Pillar acquisition in July 2005. To make the timing of reporting of Joint Ventures consistent with the Group, the results of December year end ventures have been included for a 15-month period to March resulting in a one-off increase of £4 million to underlying profit. As required by IFRS the reported results for Funds and Joint Ventures are included on a post tax basis as a single line with profits totalling £311 million, an increase of 96.8% on the prior year. This profit includes financing costs (£67 million), profits on sale and valuation gains (£378 million) and a taxation charge (£106 million).

Other income

Our fees and other income are up by £42 million to £50 million comprising dividends from our investment in Songbird and performance and management fees from the newly acquired Fund Management business.

In November 2005 we received our first dividend of £16 million in respect of our holdings of A & B shares in Songbird, which owns 60.8% of Canary Wharf Group PLC.

The fees comprise £20 million of performance fees and £6 million of management fees. The management fees are based on a percentage of the portfolio value. The performance fees are earned by exceeding stretching targets in the calendar year measured against a benchmark. The third party element only of the fee earned is recognised.

Half of the performance fee earned is recognised immediately while the balance is released over a vesting period provided there is not significant underperformance against the benchmark in later years. The vesting period runs to the end of the Trust's life. Fees of £14 million are deferred.

Administration expenses

Administration expenses are £81 million, some £32 million more than the prior year. The increase reflects increased staff numbers, primarily due to the acquisition of Pillar and recruitment of additional property professionals to support our intensified asset management and portfolio reshaping activities. £18 million of costs represent performance-related compensation from bonus and share-related plans. Administration costs include one-off costs of £13 million, including the costs of the closure of the Pillar head office, redundancies and changes to actuarial assumptions in the Pension Scheme. Our administration costs, representing 0.4% of Funds under management, continue to demonstrate efficient management of the portfolio.

Financing

Net interest payable (before refinancing charges) is some 13.2% higher at £369 million, representing the increase in debt due to the Pillar acquisition earlier in the year, net of the savings made from refinancing Broadgate in 2005. The level of interest expense is expected to reduce as a result of the sales programme reducing the level of debt in the second half of the year. As announced on 28 February 2006, the Group has restructured the financing of the Sainsbury's portfolio and this has given rise to an exceptional charge. In addition, as a result of the sales programme and consequent reduction in debt, certain derivatives have been closed out in accordance with our financial risk management policies. These two items give rise to a charge in the year of £122 million. The interest charge in future is estimated to reduce by £11 million as a result of the cheaper finance available under the new securitisation from BL Superstores Finance PLC. Interest cover remains stable with underlying profit before interest and tax representing 1.5 times the net interest charge.

Net valuation gains

The most significant contribution to IFRS profits are net valuation gains amounting to £1,462 million, reflecting revaluation surpluses on the Group's properties and investments of £1,295 million and profits on disposals of £167 million. This compares to total revaluation gains in 2005 of £610 million. The increase is due to the strong revaluation performance due to continued yield shift and the profitable disposals made in the year. This amount ignores revaluation gains of £378 million included within the results of Funds and Joint Ventures (see above) and on developments of £102 million, which are shown in the consolidated statement of changes in equity.

Intangible assets and goodwill

IFRS require the Group to recognise an intangible asset of £75 million upon acquisition of Pillar representing the estimated fair value of anticipated future income from Fund Management contracts. In accordance with IFRS this intangible asset is being amortised over the life of the contracts. Consequently a non-cash charge of £10 million relating to this amortisation has been released.

A non-cash impairment charge of £240 million has been recognised in respect of goodwill arising from the acquisitions of Pillar and the Spirit and Debenhams portfolios. Accounting Standards require us to provide in full for deferred tax on corporate acquisitions and not the fair value of the contingent tax liability absorbed on acquisition, and this inflates the value of goodwill on the balance sheet. This charge eliminates the goodwill that has arisen on these acquisitions.

Taxation

The **underlying tax rate** this year is 18.8% (2005: 23.2%). This low rate arises principally through the effect of non-taxable dividends, capital allowances and capitalised interest. The actual corporation tax liability is lower than 18.8% due to the cost of refinancing of our Sainsbury's portfolio which has been used to relieve taxable profits in the current year. The rate of tax on disposals is low because the Group's pool of capital losses and the Sainsbury's refinancing costs have been used to relieve gains in the current year.

Earnings per share

Diluted **earnings per share** rose to 240 pence from 126 pence in 2005. Underlying earnings per share have increased from 27 pence to 36 pence, as a result of strong growth in underlying profits and the reduced underlying tax rate.

Our proposed final dividend of **11.8 pence per share** continues our progressive dividend policy growing the level of distribution by 8.3%. Total dividends per share declared for the year are 17 pence (2005: 15.7 pence). Underlying profits after tax twice cover dividends. As required by IFRS final dividends are only reflected in the financial statements once approved by shareholders and as such the final 2006 dividend is not included in these results.

Net assets

Net assets rose significantly as a result of the geared impact of revaluation gains and retained earnings for the year.

	March 2006	March 2005 (restated for IFRS)	% increase
NAV per share ¹	1486p	1128p	31.7%
EPRA net assets ¹	£7,802m	£5,913m	31.9%
Net assets	£6,016m	£4,783m	25.8%

¹ EPRA basis (note 2)

Cash flows

Net cash flow from operating activities is broadly unchanged. An increased level of interest expense following the acquisition of Pillar has led to the decrease in pre-investment and financing cash flows. The Group has been a net seller of property during the year leading to the £1 billion net investment cash inflow following net investment outflow of £527 million in the prior year. These net proceeds have been used to repay £1 billion of debt.

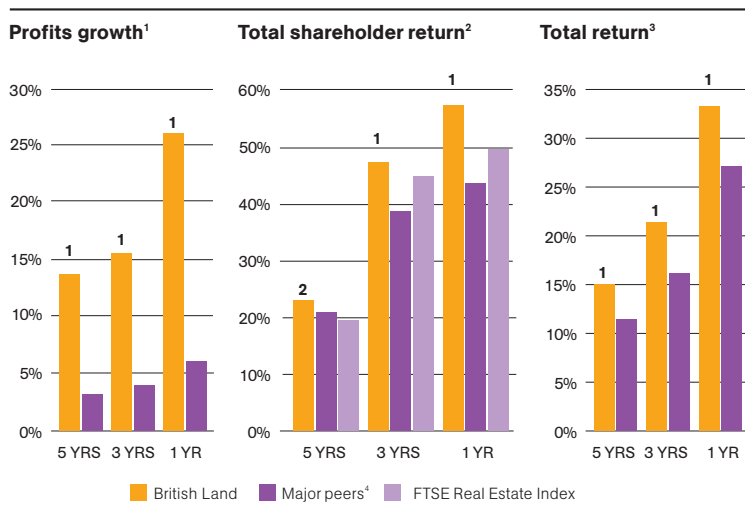
	March 2006 £m	March 2005 £m (restated for IFRS)
Net cash flow from operating activities	455	464
Net cash flow after JV dividends, Unit Trust distributions, interest, tax and working capital movements	104	126
Net investment cash flows	986	(527)
Financing	(1,025)	459
Dividends	(84)	(77)

Key performance indicators

Property is a long-term business. Decisions taken to create value over time frequently affect current year's earnings and so the Board measures performance over a range of time periods. Our management judgements over asset selection, sector views, redevelopments, financial structure, corporate and community responsibility all combine to deliver a single set of financial returns and these should be judged against the risk profile adopted.

In measuring and benchmarking performance the Group uses a number of key performance indicators to indicate the impact of management actions. At the 'total company' level, the three most visible indicators are 'profits growth', 'total shareholder return' and 'total return' over one, three and five year periods reflecting the geared performance of the whole business. Benchmarking is undertaken against our major quoted peers (Land Securities, Hammerson, Liberty and Slough) and the FTSE Real Estate Index. We believe that the total returns of the Company to be most important as these represent the returns our Shareholders experience. The low risk nature of our portfolio, focused on prime properties (with long leases and strong tenant covenants) and with a modest proportion of development activity, enables the Group to finance itself at a higher level of gearing than its peer group.

The key performance indicators demonstrate British Land's strong track record in relative and absolute value creation over the last one, three and five years.



¹ Growth in underlying profits excluding exceptional items, profits on disposals and revaluation gains
² Growth in share price plus dividends per share
³ Growth in adjusted, diluted net asset value per share plus dividends per share
⁴ Average of major peers – Land Securities, Hammerson, Liberty and Slough (some differences in year ends)
 One year, IFRS, others based on UK GAAP
 Number represents British Land's ranking compared to its major peers

International accounting standards

First time implementation

This is the first year the Group reports its results under International Accounting Standards (IFRS) which were adopted on 1 April 2005. This change to the accounting basis arises from legislation requiring all EU listed companies to apply these standards to their financial statements. Comparative figures for 2005 have been restated in accordance with IFRS. The principal impacts of adopting IFRS, along with comparatives for the year ended 31 March 2005 contained within this report, were published in a press release on 14 July 2005. Further details and reconciliations explaining the transition to IFRS are available on the Group's website, www.britishland.com. As permitted by IFRS the Group has adopted material exemptions from full retrospective application of IFRS accounting policies in respect of 'Business Combinations', where combinations that took place before 1 April 2004 have not been restated, and 'Employee Benefits' (where the accumulated actuarial gains and losses in respect of employee defined benefit plans have been recognised in full through reserves).

EPRA

To assist stakeholders, British Land has worked closely with other major European property companies and the European Public Real Estate Association to publish guidelines on a standard net asset value and earnings per share calculation, designed to aid comparability between companies following implementation of IFRS and to assist in understanding the reported figures compared to previous accounting practices. The EPRA calculations are set out in note 2 as well as a reconciliation to our underlying earnings per share, which reflects company only adjustments.

Accounting judgements

Significant accounting policy judgements are highlighted in our accounting policy note. The most important judgement affecting comparability with other property companies is our approach to deferred tax. Many (but not all) have adopted our policy of calculating deferred tax consistent with the principle of an ultimate sale of investment properties capturing all available tax reliefs. Some others assume no sale. Both methods are appropriate under IFRS dependent on company specific strategies and practices.

Finance and capital structure

British Land is managed on an integrated basis to produce secure and attractive risk adjusted returns to shareholders. Risk management is a distinctive skill at British Land where the mix of assets, leases, developments and debt are managed together to ensure the most effective result. Overall, the Group's prime assets and their secure rental income present lower risks than many other property portfolios, enabling the returns to be enhanced using financial leverage. A 45-55% loan to value ratio is currently targeted, subject to the Board's view of the market, the prospects of the portfolio and the recurring cash flows of the business. The financing policy, outlined below, is set out in more detail later in this report, together with our principal debt instruments.

Since we seek to maximise shareholder returns, we prefer to avoid equity issuance, except where the commercial opportunity clearly merits it. We also would expect to return capital to shareholders if a surplus arises over what we believe can be attractively deployed in the business.

Debt is raised from a variety of sources with a spread of maturity dates. Longer term debt is raised principally through securitisations and debentures. Securitisations have a range of benefits, including long maturities at competitive rates with no recourse to other companies or assets in the Group, and without financial covenants by British Land. Debentures also have long maturities and no amortisation.

Unsecured revolving and committed bank facilities tend to be for terms of five to seven years. We aim to spread the maturities of the different facilities from a wide range of banks.

The Group borrows at fixed and floating rates and uses derivatives to achieve the desired interest rate profile; currently the policy is to maintain around 85% (subject to 5% tolerance) of debt at fixed or capped rates. This interest rate profile is closely monitored as part of our management of the overall financial effects of transactions in the Group. The year end position of 95% fixed/capped reflects our expectation of increasing floating rate debt as we fund our committed development projects.

The Joint Ventures are separately financed, and have their own interest rate derivatives, all with no recourse to British Land.

Financing statistics	31 March 2005	
	31 March 2006	(restated for IFRS)
Group:		
Net debt	£5,593m	£6,061m
Weighted average debt maturity	15.0 yrs	14.3 yrs
Weighted average interest rate	5.71%	6.00%
% of net debt at fixed/capped interest rates	95%	90%
Interest cover ¹	1.51	1.46
Loan to value (debt to property & investments)	42%	50%
Unsecured debt to unencumbered assets	26%	42%
Undrawn committed facilities and cash	£2,415m	£969m
Group and share of Funds and Joint Ventures:		
Net debt	£6,684m	£6,538m
Weighted average debt maturity	13.4 yrs	13.5 yrs
Interest cover ¹	1.52	1.50
Loan to value (debt to property & investments)	46%	52%

¹ Underlying profit before interest and tax/net interest excluding refinancing charges

Gearing increased on the acquisition of Pillar and then decreased over the year to 46% (loan to value, including share of Funds and Joint Ventures) as a result of asset value growth and repayment of debt following property disposals.

During the year we have been active in both the banking and debt capital markets to arrange financing of the business. We raised over £1.5 billion of new or renewed bank lines, including £790 million arranged in a successful, oversubscribed syndicated facility with 25 banks, taking advantage of favourable market pricing. In addition, more than £700 million resulted from a number of bilateral agreements with banks on similar (or improved) terms.

In February 2006 we completed the refinancing of the Superstores portfolio. BL Superstores Finance PLC issued £753 million of bonds at an average interest rate of 4.96%, with an average life of 13.4 years.

The weighted average cost of debt has been reduced as at 31 March 2006 to 5.7% (2005: 6.0%) and the weighted average debt maturity has increased to 15 years (2005: 14.3 years).

At 31 March 2006, the market value of the Group's net debt was £384 million more than book values (£386 million including shares of Joint Ventures). This reflects the higher historical cost of debt compared to levels at which it might be available today. Tax relief currently available for the higher interest would not be available if British Land were to become a REIT.

Within unit trusts the most notable financing activity was the restructuring of the debt in HUT, completed in September 2005, reducing its average cost of debt. Three bank loan facilities, with combined debt of £758 million, were repaid or reduced with the proceeds of a new £1 billion securitisation. The seven year issue, secured against 16 retail parks, incorporated significant asset management flexibility.

The Scottish Retail Property Partnership (a Joint Venture with Land Securities PLC) was refinanced in April 2005 by a seven year securitisation, raising £430 million, most of which was returned to the partners.

Risks and rewards

The Company generates returns to shareholders through long-term investment decisions relating to both income and capital growth. These decisions require us to evaluate opportunities arising in the following core areas:

- demand for space from occupiers against available supply (including new developments);
- differential pricing for premium locations and buildings;
- alternative use for buildings (particularly redevelopment);
- demand for returns from investors in property, compared to other asset classes;
- price differentials for capital to finance the business;
- legislative initiatives, including planning consents and taxation;
- economic cycles, including their impact on tenant covenant quality, interest rates and inflation; and
- mis-pricing of property assets by the equity markets (for example, share buy-backs or opportunistic investments).

These opportunities can also represent risks. Demand for property and ability of tenants to pay rent can be affected by general economic conditions at both a macro and local level. Excessive levels of supply of property can also lead to falling rental levels. Rising interest rates may impact the security of the tenant base, lower development margins significantly and reduce investment appetite. Property values are also affected by changes in planning, taxes, technology and lease structures. Interest rates, bond yields and the relative attractions of other asset classes also impact property values. These risks in the UK property sector can be amplified by development exposure and gearing.

Operating and financial review

In preparing this OFR we have had regard to the recommendations in Reporting Standard 1: Operating and Financial Review issued by the ASB in 2005 insofar as we consider they are relevant to our business model and industry. We have provided herein a detailed management commentary on our markets, activities and prospects. Users will understand that where we make forward looking statements they reflect our current views; the future depends on many factors and interactions which may cause outcomes to differ from those anticipated in this assessment.