REPORT & ACCOUNTS 2002

# DERWENT VALLEY HOLDINGS PLC

# Contents

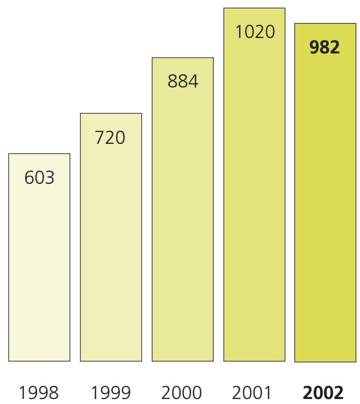
Derwent Valley is a commercial property investor focused on Central London. The group has a portfolio balanced between income generation and refurbishment and development opportunities. Its strategy is to add value to its buildings through creative planning, quality of design, innovative refurbishment and enterprising lease management. Through this approach, the group aims to deliver, over time, high total returns to shareholders.

# Financial highlights

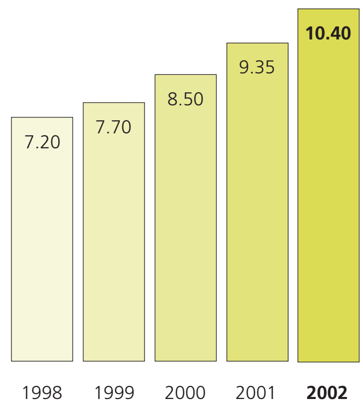
| | | 2002 | 2001 | % Increase/ (decrease) |
|---|---|---|---|---|
| **Net revenue from properties** | | **£41.9m** | £43.0m | (2.6) |
| **Profit before taxation** | Adjusted | **£17.4m** | £17.9m | (2.8) |
| | FRS3 | **£15.4m** | £21.7m | (29.0) |
| **Earnings per share** | Adjusted | **25.50p** | 27.73p | (8.0) |
| | FRS3 | **21.68p** | 31.68p | (31.6) |
| **Dividend per share** | | **10.40p** | 9.35p | 11.2 |
| **Net assets per share** | Adjusted | **982p** | 1020p | (3.7) |
| | Basic | **963p** | 1004p | (4.1) |
| **Total return** | | **(2.7%)** | 16.4% | |
| **Gearing** | Balance sheet | **58.0%** | 50.8% | |
| | Profit and loss | **1.96** | 1.95 | |

# Five year review

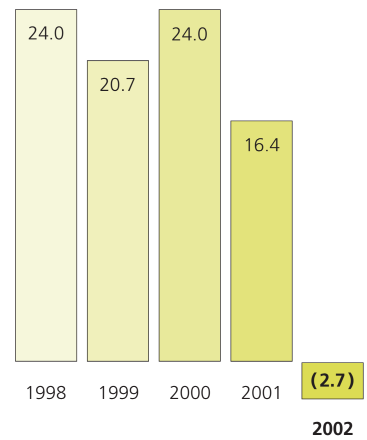
Adjusted net assets per share (pence)



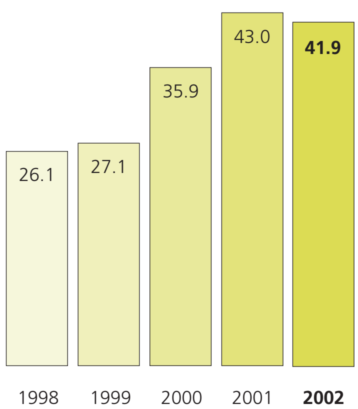

Dividend per share (pence)



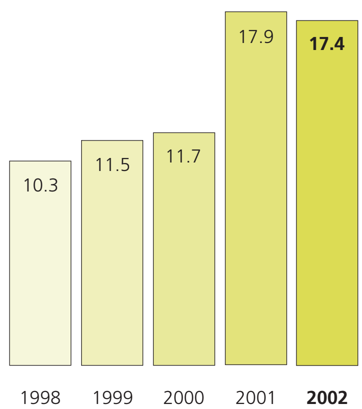

Total return (%)



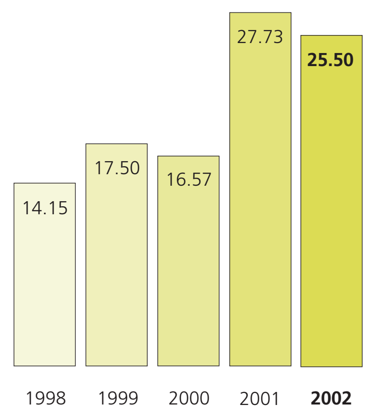

Net revenue from properties (£m)




Adjusted profit before taxation (£m)




Adjusted earnings per share (pence)



# Chairman's statement

**Results**

Market conditions during the second half of the year proved more difficult than anticipated as business confidence was undermined further by increased economic uncertainty. This led to reduced occupational demand and falling rents in the group's main operational area of Central London. Consequently, following 9 years of uninterrupted growth, net asset value per share, adjusted for the effect of FRS19 – Deferred Tax, declined 3.7% from 1020p at 31st December 2001 to 982p at the year end. Over this ten year period from 1993, the group's total return has been 321% and, despite the slowdown in the current year, it remains in excellent shape with future growth prospects being supported by strong finances and a reversionary portfolio which contains a number of redevelopment and refurbishment opportunities.

Profit before tax, excluding the results from the disposal of investments, was £17.4 million, marginally down from the £17.9 million reported for 2001. Last year, the result included the net receipt of a surrender premium of £2.3 million and, adjusting for this, profits increased by £1.8 million in 2002. FRS3 profits, which include the results from the disposal of investments, decreased to £15.4 million from £21.7 million in 2001.

**Dividend**

The directors propose a final dividend of 7.35p per share, which would give a total for the year of 10.40p, an increase of 11.2% from that paid last year. The final dividend will be paid on 9th June 2003 to shareholders on the register on 16th May 2003.

**Valuation overview**

At the year end, the group's investment portfolio was revalued at £832 million, a deficit of £29 million over the year, after adjusting for acquisitions and disposals. The scheme at Tower House, Covent Garden, WC2 was completed in the period and showed a valuation surplus of £2.2 million. The adjoining development property at Southampton Street, WC2, which has been completed since the year end, was included in development properties held at a cost of £24.7 million. Investment properties that were held throughout the year fell in value by 3.5% against an increase of 9.9% in the previous year.

The decline in the demand for space had a significant influence on the valuation as lower estimated rents and longer void periods were attributed to space that was either currently or imminently vacant. Consequently, values of such buildings fell. Those with longer lease profiles generally maintained their value as investment demand remained firm.

Overall, the group's West End properties, which represented 74% of the portfolio, declined by 1.7% in the year. Within this figure, the performance of the individual London villages varied considerably. The group's core business is focused on the middle market of the West End and surrounding areas. This is characterised by rents between £30 and £50 per sq ft. (£320 and £540 per $m^2$), and continued to prove relatively resilient. The group's holdings in Paddington, Victoria and Soho/Covent Garden, where such rents prevail, make up 36% of the portfolio and made slight gains. Those in the higher rental areas of Belgravia and Mayfair, which constitute 18% of the portfolio, fell back.

Tower House, reception

Of the remainder of the portfolio, those properties located in the City and its borders, 26% of the portfolio, were hardest hit with values falling by 8.2%. Much of this fall was attributable to the group's buildings at Hatton Garden, EC1, where leases are coming to an end, and Shoreditch, E1, which was vacant. However, both are potential major refurbishment schemes and, in the medium term, should offer opportunities for substantial capital uplift.

**Operations review**

In what has been a quiet year for acquisitions and disposals, management has concentrated on completing existing schemes and evaluating future projects so that these can be undertaken swiftly once conditions improve. However, the search for profitable transactions arising from changes in economic and market circumstances has continued. Since the year end, we have identified and acquired one such opportunity, a portfolio of investment properties from the London Borough of Islington for £38 million. This transaction brings to the group under-managed properties with numerous lease management and marriage value angles that will undoubtedly benefit from the hands-on approach in which we specialise. Our initial strategy will be to dispose of the smaller properties and concentrate on those buildings with greater potential, a number of which are located in the regeneration area of Kings Cross which we believe will become another important London village.

The maintenance of the group's robust operating cash flow by continual and diligent lease management was, as always, important. Lettings with an annualised income in excess of £4.9 million were achieved over the year, of which £2.3 million was from space that was vacant a year ago. In addition, an annualised uplift of £1.2 million was achieved from rent reviews.

Although prevailing market conditions determined that some schemes should be deferred and others reduced in scope, refurbishment and redevelopment remained a significant part of the group's activities. During the year, £35 million was spent on schemes, including those at Tower House and Southampton Street, WC2, Charing Cross Road, WC2, Oliver's Yard, EC2 and Greencoat House, SW1. As a result of the trimmed development programme, only £16 million is budgeted for the current year.

**Prospects**

Despite a substantial increase in available space in Central London during the year, planning regulations, particularly in the West End, are likely to restrict the returns that can be achieved from new development. We believe that existing buildings, which are not fettered by the need to include residential space, offer more expedient opportunities to enhance capital values. A number of such properties within the group's portfolio are being appraised for refurbishment when market conditions improve. However, until signs of such an improvement are evident, our priorities are to complete the current schemes, minimise the level of vacant space and manage our capital expenditure programme accordingly.

Although Central London office rents remain depressed there will be a turning point as demand for space, especially in the West End, recovers. Assets, as described above, that have latent potential that can be exploited when sentiment improves, are not easy to acquire. The group is fortunate to own such properties and to have the resources which enable enterprising and creative management to ensure that the portfolio's full potential is realised.

**Directors**

Finally, the board looks forward to Robert Farnes, who recently retired as Chairman of CB Hillier Parker, joining the board as a non-executive director on 1st April 2003.

J. C. Ivey 11th March 2003

Gordon House, reception

# Property review

**Introduction**

The group has over 400 tenancies with an average lease length, after adjusting for breaks, of 8 years. The average lease length in the West End is 9.2 years whilst in the City and its borders it is 4.8 years. These levels characterise a portfolio that can be actively managed. Where properties have been refurbished and re-let on longer leases, they are selectively sold and replaced with new acquisitions.

The group has established a reputation for delivering well designed contemporary offices. By working closely with talented architects, innovative design solutions are found and adaptable space provided, which suits the diverse occupational requirements in Central London. This approach, especially in these more difficult letting markets, increases the likelihood of attracting tenants.

An important aspect of the business is the planning process and area regeneration. In order to assimilate the current regulations, Derwent Valley works closely with The Westminster Property Owners Association in ongoing discussions with Westminster City Council's planning department. In addition, the group is represented on the board of the New West End Company where, together with other major landlords, it seeks to preserve and enhance the dynamics and reputation of the West End.

**Portfolio management**

The portfolio continues to be actively managed and during the year 41 rent reviews, with a passing rental of approximately £3.8 million per annum, were triggered. Twenty three of these were settled by year end, increasing £1.8 million of annualised income to £3 million, an uplift of 67%.

Tenant demand is considerably lower than experienced for a number of years and, as a consequence, vacancy rates in Central London increased over the year from 6.2% to 8.0% and in the West End from 5.0% to 6.1%. Against this background it was inevitable that lettings would be difficult. However, 44 lettings were concluded on 11,700m² of space and 19 lease renewals completed.

Whilst office demand was weak, the retail letting market remained buoyant. The letting of one unit at Tower House, WC2, to sports retailer Ellis Brigham followed an earlier letting to Sainsbury's of the adjacent 5 Southampton Street, whilst at The Courtyard, Charing Cross Road, WC2, two of the four new retail units have been let.

As active property managers, the group will always have vacant space for both letting and refurbishment. At year end, there was 56,700m² vacant which represents 22.4% of the portfolio's estimated rental value, compared to 15.2% last year. Of this, 23,100m² or 11.1% of the rental value was available for letting. This included the balance of recently completed schemes at Tower House (3,400m²), The Courtyard (2,800m²) and 1 Oliver's Yard, EC2 (10,800m²). A further 33,600m² is under refurbishment or identified for potential refurbishment, with Centric House, E1 (20,300m²) the principal element. Whilst this is a substantial building in floor space terms, it only represents about 3% of the investment portfolio's value.

Although rental values declined during the year, the portfolio still has a significant reversionary element. At year end, the contracted rental income of the investment portfolio, after deduction of ground rents, was £44.8 million, which has an estimated rental value of £70.1 million. This is a potential £25.3 million uplift of which £15.7 million is from vacant space and £9.6 million from rent reviews and lease reversions due over the next few years.

**Refurbishment and development**

Three principal refurbishment schemes were completed during the year, all in the second half. Firstly, in September, Tower House, the refurbishment element of the group's Covent Garden scheme, was completed to provide 3,400m² of offices, a 1,300m² retail unit and 300m² of residential space. Both the retail and residential have been let and the offices are available. In October, The Courtyard project was completed. The 2,400m² of refurbished offices have been given a new identity and the 800m² retail units, which front Charing Cross Road, were redesigned. Additional works are to be undertaken this year to provide further

The Courtyard, reception

retail space. Finally, at 1 Oliver's Yard, following the lease restructure in April with Globix, the sole occupier of this 17,400m$^2$ office building, 11,000m$^2$ of space was brought back under the group's control. The property has been re-branded and fitted out at a cost of £6.8 million, funded from the £11.3 million payment received from the tenant.

Since the year end, the redevelopment of 5 Southampton Street has been completed. A 1,100m$^2$ retail unit and 3,000m$^2$ of impressive offices have been created behind a retained facade.

Centric House, which was acquired in 2001, is the group's largest holding by floor area, and was income producing until June 2002. This prominent building, located on the northern edge of the City, offers long-term potential either through extensive refurbishment or redevelopment. In the interim, to reflect the change in market conditions, an economic but innovative refurbishment is being implemented to create workshop/office units which will be offered on flexible lease terms. The first phase of 5,900m$^2$ will be available shortly with additional space refurbished upon demand.

At the group's 11,700m$^2$ office complex in Hatton Garden, EC1, rental income of £2.4 million per annum expires in September this year. The existing buildings occupy an under utilised site and a planning decision is awaited for a major refurbishment of the main building and the development of approximately 4,000m$^2$ of new space in the existing courtyard. A 3,000m$^2$ income producing building, which will not be affected by the proposals, is included in this holding. Any decision to proceed with the scheme will be dependent on both the planning outcome and the economic environment. The earliest the space would be available is late 2005.

Although the commencement of new schemes has slowed, the group continues to appraise the long-term strategy for each building. Planning studies are underway on the group's two important Paddington holdings. Both let, they are located in strategic positions in this highly successful regeneration area and have medium term redevelopment potential. Early indications show that the existing 16,100m$^2$ floor space can be increased substantially.

**Acquisitions and disposals**

Whilst the group remains acquisitive, suitable and interesting acquisitions are still not easy to find. The low interest rate environment continued to support the investment market during the year, despite the downward movement of rental levels. Only two purchases were made in the year. In April, 12 Roger Street, WC1, a 1,660m$^2$ office building, which offers an opportunity to create additional space, was acquired for £5.2 million. In August, 28-29 Dover Street, W1 was acquired for £9.8 million. Although not in the group's principal operating area, this 1,400m$^2$ building is one of the few non-period buildings in the vicinity and has medium term opportunities to enhance value through refurbishment.

Following disposals in 2001 of £104.5 million, 2002 was a much quieter year, with three properties sold realising £16.9 million.

The following 9 pages provide more detail on the portfolio, its performance and forthcoming projects.

J. D. Burns 11th March 2003

# Principal properties

| | | Approximate net area $m^2$ |
|---|---|---|
| **£30 million and over – 48% of portfolio** | | |
| O R | 135-155 Charing Cross Road, WC2 | 6,100 |
| O R | Covent Garden Estate: 19-26 and 19A Floral Street, 26 and 27-32 King Street and 34 Rose Street, WC2 | 6,800 |
| O | Greencoat and Gordon House, Francis Street, SW1 | 11,100 |
| O | 1-3 Grosvenor Place, SW1 | 7,700 |
| O | 4 Grosvenor Place, SW1 | 7,300 |
| O R | Holden and Dumbarton House, 54-68 Oxford Street, W1 | 8,200 |
| O | New Garden House, 78-83 Hatton Garden, EC1 | 11,700 |
| O R | 1 Oliver's Yard, EC2 | 17,400 |
| O | Telstar House, Eastbourne Terrace, W2 | 8,300 |
| **£20 - £30 million – 26% of portfolio** | | |
| O | Centric House, Shoreditch High Street, E1 | 20,300 |
| O | Gresse Street Estate: Birkbeck College and 16-19 Gresse Street and 7-8 Rathbone Place, W1 | 8,300 |
| O | Harcourt House, 19-19A Cavendish Square, W1 | 5,500 |
| O R | Heron House, 319-325 High Holborn, WC1 | 6,100 |
| O | Middlesex House, 34-42 Cleveland Street, W1 | 6,000 |
| O | 55-65 North Wharf Road, W2 | 7,800 |
| O | Premier House, 10 Greycoat Place, SW1 | 5,900 |
| O R | 25 Savile Row, W1 | 3,800 |
| O R | Tower House, 10 Southampton Street, WC2 | 5,000 |

| | | Approximate net area $m^2$ |
|---|---|---|
| **£10 - £20 million – 17% of portfolio** | | |
| O | Argosy House, 215-227 Great Portland Street, W1 | 2,800 |
| O | Berkshire House, 168-173 High Holborn, WC1 | 4,900 |
| O | 40-43 Chancery Lane, WC2 and 20-21 Tooks Court, EC4 | 5,700 |
| O R | Exmouth House, Exmouth Market, EC1 | 5,000 |
| O | 6 Greencoat Place, SW1 | 3,100 |
| O R | Jaeger House, 57 Broadwick Street, W1 | 2,300 |
| O R | Morelands Buildings, 5-27 Old Street, EC1 | 7,400 |
| O R | Morley House, 314-322 Regent Street, W1 | 3,600 |
| O R | Panton House, 25-27 Haymarket, SW1 | 2,700 |
| **Under £10 million – 6% of portfolio** | | |
| O R | Broadmead and Westcombe House, 19-23 Panton Street, SW1 | 1,500 |
| O R | 28-29 Dover Street, W1 | 1,400 |
| O | 27-32 Old Jewry, EC2 | 2,100 |
| O R | 78 St Martin's Lane, WC2 | 1,500 |
| **Development properties – 3% of portfolio** | | |
| O R | 5 Southampton Street, WC2 | 4,100 |
| O | 20 Leonard Street, EC2 | Site |

O Offices
R Retail/Restaurant

# Portfolio statistics and performance

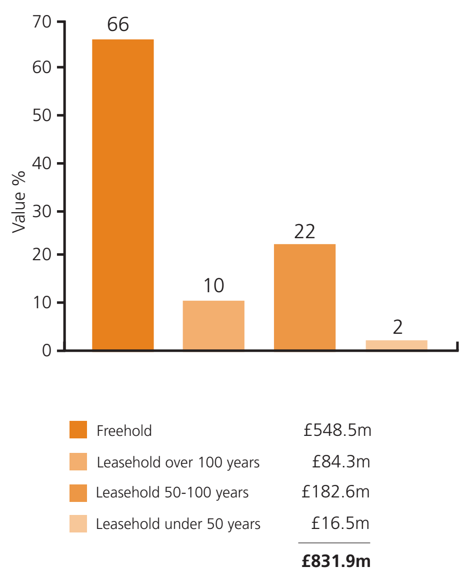
| | Valuation £m | Weighting % | Valuation performance[1] % | Number of properties | Floor area m² | Vacant accommodation m² |
|---|---|---|---|---|---|---|
| WEST END | | | | | | |
| Central | 555.3 | 67 | (2.2) | 31 | 117,000 | 19,700 |
| Outer | 60.2 | 7 | 2.2 | 4 | 18,300 | 1,200 |
| | 615.5 | 74 | (1.7) | 35 | 135,300 | 20,900 |
| CITY | | | | | | |
| Central | 5.5 | 1 | (11.4) | 1 | 2,100 | 600 |
| Outer | 210.9 | 25 | (8.1) | 12 | 82,800 | 35,200 |
| | 216.4 | 26 | (8.2) | 13 | 84,900 | 35,800 |
| **TOTAL PORTFOLIO 2002** | **831.9** | **100** | **(3.5)** | **48** | **220,200** | **56,700** |
| 2001 | 833.5 | 100 | 9.9 | 48 | 232,800 | 25,000 |

[1] properties held throughout the year and excluding development properties of £24.7 million.

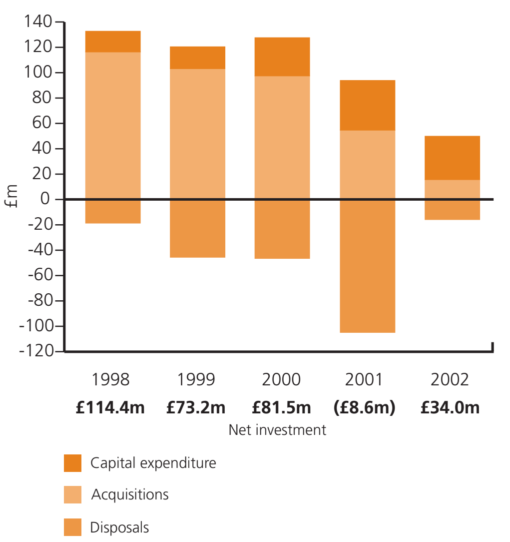
West End - Central: Belgravia, Mayfair, Soho, Covent Garden, Victoria, Noho, King's Cross
- Outer: Camden, Islington, Paddington

City - Central: Core
- Outer: Clerkenwell, Holborn, Shoreditch and borders

**Value of portfolio by tenure**




**Net investment 1998-2002**



| | Contractual rental income per annum £m | Average rental income £ per m² | Vacant accommodation rental value per annum £m | Rent review and lease reversions per annum £m | Portfolio estimated rental value per annum £m | Average unexpired lease length[2] Years |
|---|---|---|---|---|---|---|
| WEST END | | | | | | |
| Central | 29.0 | 305 | 8.0 | 7.0 | 44.0 | 8.9 |
| Outer | 3.4 | 210 | 0.3 | 1.2 | 4.9 | 11.7 |
| | 32.4 | 290 | 8.3 | 8.2 | 48.9 | 9.2 |
| CITY | | | | | | |
| Central | 0.4 | 285 | 0.2 | (0.1) | 0.5 | 5.3 |
| Outer | 12.0 | 260 | 7.2 | 1.5 | 20.7 | 4.7 |
| | 12.4 | 260 | 7.4 | 1.4 | 21.2 | 4.8 |
| **TOTAL PORTFOLIO 2002** | **44.8** | **280** | **15.7** | **9.6** | **70.1** | **8.0** |
| 2001 | 44.0 | 220 | 11.4 | 19.4 | 74.8 | 8.2 |

[2] lease length weighted by rental income and assuming tenants' break at first opportunity.

**Portfolio yields**

| | Rental uplift per annum £m | Rental per annum £m | Yield[3] % |
|---|---|---|---|
| Year end contractual rental income, net of ground rents | | 44.8 | 5.4 |
| Letting 23,100m² vacant accommodation available at year end | 7.8 | | 6.3 |
| Completion and letting 33,600m² of existing schemes and developments | 7.9 | | 7.2 |
| Anticipated rent review and lease renewal reversions | 9.6 | | 8.3 |
| Portfolio reversion | | 25.3 | |
| Potential portfolio rental value | | 70.1 | 8.3 |

[3] based upon the year end valuation of £831.9 million and adjusted for costs to complete commenced projects.

# Refurbishment and development

| Property | Proposed net area $m^2$ | Expected completion date | Estimated cost to complete including fees £m | Comments |
| --- | --- | --- | --- | --- |
| **DEVELOPMENT PROPERTIES** | | | | |
| **Covent Garden** | | | | |
| 5 Southampton Street, WC2 | 4,100 | March 2003 | 1.4 | Office/retail redevelopment behind a retained facade, with the retail unit let to Sainsbury's. |
| **City borders** | | | | |
| 20 Leonard Street, EC2 | 4,500 | – | – | Site with planning permission for office development. |
| | **8,600** | | **1.4** | |
| **CURRENT REFURBISHMENTS** | | | | |
| **City borders** | | | | |
| Centric House, Shoreditch High Street, E1 | 20,300 | April 2003 | 3.2 | Initial phase of refurbishment to provide 5,900$m^2$ of workshop/office and storage units. Potential for additional space to be refurbished as required. |
| **Holborn** | | | | |
| Berkshire House, 168-173 Holborn, WC1 | 2,600 | August 2003 | 2.4 | Six floors of air conditioned offices. |
| **Victoria** | | | | |
| 6 Greencoat Place, SW1 | 1,100 | August 2003 | 1.8 | Final phase to complete this office refurbishment. |
| **Soho** | | | | |
| 135-155 Charing Cross Road, WC2 | 1,000 | November 2003 | 1.8 | Reconfiguration of retail units and the creation of additional space. |
| **Mayfair** | | | | |
| 25 Savile Row, W1 | 1,400 | May 2003 | 1.1 | Two floors of air conditioned offices. |
| | **26,400** | | **10.3** | |

| Property | Existing area $m^2$ | Comments |
|---|---|---|
| **FUTURE PROJECTS** | | |
| **Holborn** | | |
| New Garden House, 78-83 Hatton Garden, EC1 | 8,700 | Lease expiry on main building in September 2003. Planning application submitted for refurbishment and additional office space. |
| **Paddington** | | |
| 55-65 North Wharf Road, W2 | 7,800 | Medium term redevelopment potential. Planning studies underway. |
| **Holborn** | | |
| 40-43 Chancery Lane, WC2 and 20-21 Tooks Court, EC4 | 5,700 | Medium term redevelopment or refurbishment opportunity. |
| **Noho** | | |
| Birkbeck College, 7-15 Gresse Street, W1 | 4,100 | Refurbishment under consideration of this educational use building, where the lease expires in December 2003. |
| **Noho** | | |
| 16-19 Gresse Street, W1 | 3,100 | Lease expiry in September 2003. Planning application to be submitted for new office development. |
| **Noho** | | |
| Holden and Dumbarton House, 54-68 Oxford Street, W1 | 2,300 | Final phase to include Dumbarton House office refurbishment and connection with Holden House entrance. In addition, possible retail extension. |
| | **31,700** | |

# Acquisitions and disposals

**ACQUISITIONS**

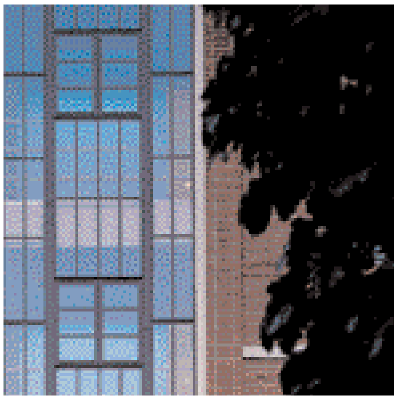
- Two Central London acquisitions totalling £15.0 million and reflecting a net initial yield of 6.4%.

**12 Roger Street, Holborn, WC1 – £5.2 million**
*1,660m² – Freehold*
- Office building let to a single tenant at £225 per m².
- Possibility to add further floor space.

**28-29 Dover Street, Mayfair, W1 – £9.8 million**
*1,400m² – Freehold*
- Multi-let office building.
- Lease management and refurbishment opportunities.

**DISPOSALS**

- Three properties sold for a net £16.9 million at an exit yield of 7.0%.
- Caledonia House, 223 Pentonville Road, N1.
- Dragon Court, 27-29 Macklin Street, WC2.
- 6-7 Queen Street, EC4.



# Portfolio activity

| Property | Approximate net area $m^2$ | Rental per annum £m | Headline rental £ per $m^2$ | Comments |
|---|---|---|---|---|
| **PRINCIPAL LETTINGS** | | | | |
| 21 Grosvenor Place, SW1 | 1,640 | 0.89 | 540 | Two floors let to Hicks Muse Tate & Furst on a ten year lease. |
| 21 Grosvenor Place, SW1 | 1,470 | 0.74 | 505 | Two floors let to Citywest Homes. |
| Tower House, 10 Southampton Street, WC2 | 1,300 | 0.50 | 390 | Following extensive refurbishment, retail unit let to Ellis Brigham on a twenty five year lease. |
| 55-65 North Wharf Road, W2 | 1,100 | 0.38 | 350 | A lease surrendered and the space re-let to St Mary's National Health Service Trust. |
| Panton House, 25-27 Haymarket, SW1 | 760 | 0.40 | 540 | Letting of the first floor to Fortum Energy and the fourth floor to Xstrata Services. |
| 6-7 St Cross Street, EC1 | 600 | 0.17 | 295 | Two floors refurbished and let to Video Arts. |
| 135-155 Charing Cross Road, WC2 | 335 | 0.24 | 710 | Following refurbishment, retail units let to Benjys and Office Shoes. |
| **PRINCIPAL RENT REVIEWS** | | | | |
| Heron House, 319-325 High Holborn, WC1 | 4,180 | 1.64 | 375 | Four reviews concluded, resulting in a rental uplift of 66%. |
| 40-43 Chancery Lane, WC2 | 1,380 | 0.39 | 290 | Five reviews settled. |
| Middlesex House, 34-42 Cleveland Street, W1 | 1,290 | 0.21 | 165 | Car park lease reviewed. |
| Exmouth House, Exmouth Market, EC1 | 960 | 0.26 | 270 | Three office and one retail review concluded. |
| Greencoat and Gordon House, Francis Street, SW1 | 760 | 0.28 | 370 | Four reviews settled in this multi-let building. |

# Retail and restaurant holdings

- Retail and restaurants are an important element of the portfolio, comprising over 14,400m² and contributing approximately 11% of the rental income.

- Retail space enhances a building's amenities and its provision in schemes is encouraged. For example, at 1 Oliver's Yard, 500m² of the ground floor office space has recently been converted to provide two retail units, one of which has been let to Pret a Manger.

- Principal retail holdings include:

- **The Covent Garden Estate, WC2.**
  This has frontage on to King Street, one of the retail routes leading into the Piazza, and also onto Floral Street which is a specialist fashion retail location. There are five retail units, comprising 1,500m². Tenants include Hackett and Moss Bros.

- **Tower House and 5 Southampton Street, WC2.**
  Following re-configuration, two large retail units totalling 2,400m² have been created and let to Sainsbury's and Ellis Brigham.

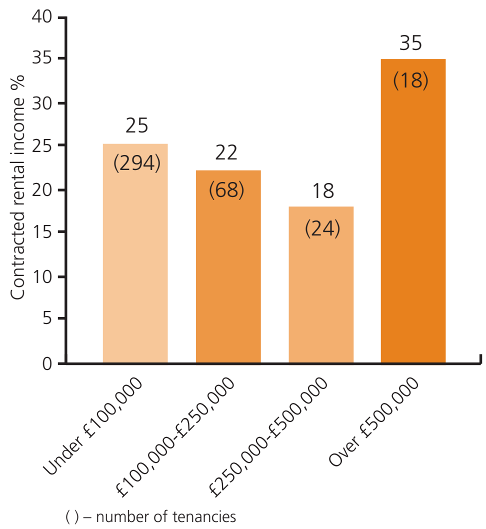
- **Holden and Dumbarton House, W1.**
  There are five retail units with frontage on to Oxford Street, one of London's premier retail locations, and five units on Rathbone Place. The retail space totals 2,000m² and tenants include The Body Shop, Halifax Building Society and Pret a Manger.

- **Heron House, 319-325 High Holborn, WC1.**
  Four retail units totalling 590m² with tenants including A Jones & Sons and Holland & Barrett.

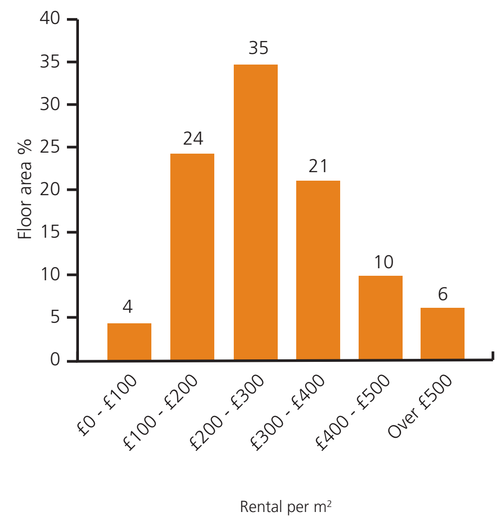
- **135-155 Charing Cross Road, WC2.**
  Four retail units recently re-configured with two let, one to Benjys. Following a further phase of works this year, the building will provide 1,600m² of retail space.


# Rental income analysis

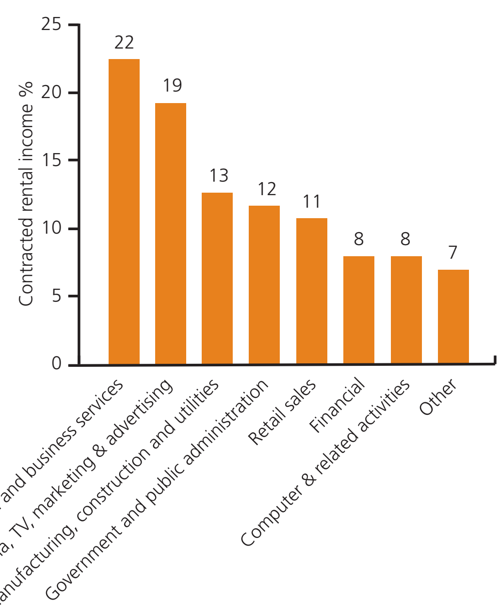
## Profile of rental income bands



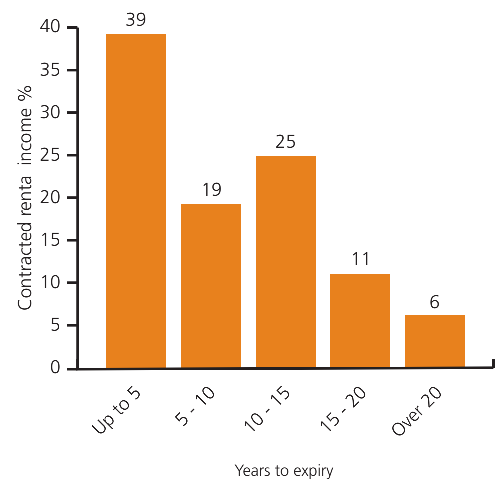

## Profile of occupied floor area




## Profile of tenant business sector




## Profile of rental income expiry



# Financial review

### Results

To understand the underlying trend in these results, the 2001 figures must be adjusted for the surrender premium received that year in respect of Old Jewry, EC2. The effect of this, which was explained in last year's annual report, was to increase gross rental income by £2.8 million and net rental income and profits by £2.3 million.

Therefore, adjusting for this, profit before taxation, excluding the results from the disposal of investments, rose £1.8 million from £15.6 million to £17.4 million. On reduced disposal activity, investment profits were down from £4.6 million to £0.2 million. This was turned into a loss of £2.0 million by a provision for the permanent diminution in value of 21 Grosvenor Place, SW1 consequent upon its disposal in March 2003, despite the fact that the price obtained exceeded the year end valuation. This resulted in an underlying reduction in FRS3 profit of £4.0 million to £15.4 million.

The increase in gross rental income of £2.4 million came from net lettings and rent reviews, which added £1.4 million and £1.8 million respectively, and the release of premiums, including part of that received in respect of Oliver's Yard, of £1.3 million. This was offset by rent foregone on void space of £1.9 million and a small reduction from the combined effect of acquisitions and disposals. Voids created an increased service charge liability for the group which held back the increase in net rental income to £1.2 million. Despite higher average borrowings in 2002 than in the previous year, interest payable was reduced by £0.8 million due to lower interest rates. This reduction more than compensated for the rise in non-utilisation fees that followed the increase in committed bank facilities negotiated in 2001.

Net assets at 31st December 2002 were £512.0 million which gave a basic net asset value per share of 963p. However, the headline net asset value is calculated by adding back to net assets the deferred tax, provided under FRS19, that it is considered will not become payable. This amounted to £10.2 million and gave an adjusted net asset value of 982p per share.

### Taxation

The total tax chargeable in 2002 was £4.5 million compared with £14.5 million in the previous year. The profit and loss account bore £3.9 million of this while £0.6 million was passed through the statement of total recognised gains and losses. The lower tax charge in 2002 was due to the reduced capital gains tax charge on investment property disposals.

In accordance with FRS19, the group has provided a further £1.4 million of deferred tax, bringing this to £10.2 million at the end of 2002. It remains the belief that this is unlikely ever to be paid and that it is difficult to justify making this provision which negates the benefit the group has generated in claiming capital allowances to reduce its tax bill. Capital allowances claimed now total £65 million and a further £2.5 million of tax, and cash, was saved in 2002.

The group does not have to provide for the capital gains tax that it would have to pay if its land and buildings were sold at their year end values. This amounts to £62.8 million (2001: £74.3 million), equivalent to 118p per share (2001: 140p).

### Cash flow and debt

The group's cash outflow in 2002 amounted to £25.8 million compared with an inflow the previous year of £12.5 million. The turnaround was due mainly to a reduction in receipts from property disposals of £88 million, offset by reduced expenditure on acquisitions of £41 million. Capital expenditure was £35 million, close to the £39 million spent in 2001, so that net investment in 2002 of £34 million compared with a net divestment in 2001 of £9 million. The operating cash inflow was £14 million (2001: £9 million) of which £5 million was paid to shareholders as dividends.

The cash outflow increased the company's debt to £297 million at the year end compared with £271 million the previous year. Gearing rose from 51% to 58% at the end of 2002 as a result of an increase in debt and a fall in the value of net assets. However, interest cover remained at last year's level of 1.96 which demonstrates the strength of the group's profit and loss account.

Suncourt House, fourth floor

Gordon House, reception

**Financing**

During 2002, the opportunity was taken to renew one of the company's bank facilities that was not due to expire until 2004. This followed the pattern of 2001 with both an extension of the term of this debt and a reduction in the cost of borrowing. There are now no facilities due for renewal until 2006 and the company's committed, unutilised facilities continue to exceed £150 million. Since the year end, the company has concluded its first unsecured loan to provide finance for the purchase of The Islington Estate.

**Interest rate hedging**

Interest rate hedging is used to protect the group from the risk of adverse interest rate movements. The policy of varying the total of fixed rate debt and that fixed using derivatives within a range of 40% to 75% of borrowings, depending on the perceived risk to the group, remains unchanged. At the year end, 52% of debt was either at fixed rates or hedged. At the same date, the weighted average cost of borrowing was 6.3%. The fair value adjustment figure, arising from the valuation of fixed rate debt and interest rate hedging instruments as required by the relevant financial reporting standard, was a negative £17.0 million (31st December 2001: negative £12.5 million), equivalent to a reduction of 22p per share after tax (31st December 2001: 17p). There is no obligation or present intention to redeem the debenture or any of the hedging instruments other than at normal maturity and therefore this amount is unlikely to be realised.

# Group profit and loss account

for the year ended 31st December 2002

| | Note | 2002 £m | 2001 £m |
|---|---|---|---|
| Gross rental income | | | |
| Group and share of joint ventures | | **46.8** | 47.3 |
| Less share of joint ventures | | **0.3** | 0.4 |
| Group gross rental income | | **46.5** | 46.9 |
| Property outgoings net of recoveries | 2 | **4.6** | 3.9 |
| Net revenue from properties | | **41.9** | 43.0 |
| Administrative costs | | **6.3** | 6.2 |
| Operating profit | | **35.6** | 36.8 |
| Share of operating results of joint ventures | | **0.3** | 0.3 |
| (Loss)/profit on disposal of investments | 3 | **(2.0)** | 3.8 |
| | | **33.9** | 40.9 |
| Interest receivable | | **–** | 0.1 |
| Interest payable | 4 | **18.5** | 19.3 |
| Profit on ordinary activities before taxation | 5 | **15.4** | 21.7 |
| Taxation on profit on ordinary activities | 8 | **3.9** | 4.8 |
| Profit on ordinary activities after taxation | 9 | **11.5** | 16.9 |
| Dividend | 10 | **5.5** | 5.0 |
| Retained profit | 22 | **6.0** | 11.9 |

All amounts relate to continuing activities.

| | Note | 2002 | 2001 |
|---|---|---|---|
| Adjusted earnings per share | 11 | **25.50p** | 27.73p |
| Adjustment for disposal of investments | | **(3.82p)** | 3.95p |
| Basic earnings per share | 11 | **21.68p** | 31.68p |
| Adjustment for dilutive share options | | **(0.04p)** | (0.07p) |
| Diluted earnings per share | 11 | **21.64p** | 31.61p |
| Dividend per share | 10 | **10.40p** | 9.35p |
| Total return | 12 | **(2.7%)** | 16.4% |

The notes on pages 28 to 41 form part of these accounts.

# Balance sheets

at 31st December 2002

| | Note | Group 2002 £m | 2001 £m | Company 2002 £m | 2001 £m |
|---|---|---|---|---|---|
| Fixed assets | | | | | |
| Tangible assets | 13 | **832.7** | 834.1 | **0.8** | 0.6 |
| Investments | 14 | **–** | – | **185.5** | 185.4 |
| Investments in joint ventures | | | | | |
| Share of gross assets | | **3.1** | 3.1 | **–** | – |
| Share of gross liabilities | | **(2.9)** | (2.9) | **–** | – |
| | | **0.2** | 0.2 | **–** | – |
| Current assets | | | | | |
| Properties held for resale | | **6.6** | 5.4 | **–** | – |
| Debtors | 15 | **14.1** | 10.0 | **340.8** | 317.7 |
| | | **20.7** | 15.4 | **340.8** | 317.7 |
| Creditors falling due within one year | 16 | **33.4** | 37.0 | **29.3** | 35.1 |
| Net current (liabilities)/assets | | **(12.7)** | (21.6) | **311.5** | 282.6 |
| Total assets less current liabilities | | **820.2** | 812.7 | **497.8** | 468.6 |
| Creditors falling due after more than one year | 17 | **297.0** | 269.4 | **295.4** | 269.4 |
| Provisions for liabilities and charges | | | | | |
| Deferred tax | 19 | **10.2** | 8.8 | **–** | – |
| Other provisions | 20 | **1.0** | 0.8 | **1.0** | 0.8 |
| | | **512.0** | 533.7 | **201.4** | 198.4 |
| Capital and reserves – equity | | | | | |
| Called up share capital | 21 | **2.6** | 2.6 | **2.6** | 2.6 |
| Share premium account | 22 | **153.7** | 153.7 | **153.7** | 153.7 |
| Revaluation reserve | 22 | **262.9** | 294.0 | **–** | – |
| Profit and loss account | 22 | **92.8** | 83.4 | **45.1** | 42.1 |
| | | **512.0** | 533.7 | **201.4** | 198.4 |
| Net asset value per share | 23 | **963p** | 1004p | | |
| Adjusted net asset value per share | 23 | **982p** | 1020p | | |

J. D. Burns, Director    C. J. Odom, Director    11th March 2003

The notes on pages 28 to 41 form part of these accounts.

# Other primary statements

for the year ended 31st December 2002

| **Statement of total recognised gains and losses** | Note | **2002 £m** | 2001 £m |
|---|---|---|---|
| Profit for financial year | | **11.5** | 16.9 |
| Unrealised (deficit)/surplus on revaluation of investment properties | | **(27.1)** | 69.2 |
| Taxation on realisation of property revaluation gains of previous years | 8 | **(0.6)** | (9.7) |
| Total recognised gains and losses relating to the year | | **(16.2)** | 76.4 |

| **Note of historical cost profit and loss** | **2002 £m** | 2001 £m |
|---|---|---|
| Reported profit on ordinary activities before taxation | **15.4** | 21.7 |
| Realisation of property revaluation surplus of previous years | **4.0** | 35.5 |
| Historical cost profit on ordinary activities before taxation | **19.4** | 57.2 |
| Historical cost profit retained after taxation and dividends | **9.4** | 37.7 |

| **Reconciliation of movements in shareholders' funds** | **2002 £m** | 2001 £m |
|---|---|---|
| Profit for financial year | **11.5** | 16.9 |
| Other gains and losses relating to the year | **(27.7)** | 59.5 |
| | **(16.2)** | 76.4 |
| Dividend | **(5.5)** | (5.0) |
| | **(21.7)** | 71.4 |
| Opening shareholders' funds | **533.7** | 462.3 |
| Closing shareholders' funds | **512.0** | 533.7 |

The notes on pages 28 to 41 form part of these accounts.

# Group cash flow statement

for the year ended 31st December 2002

| | Note | £m | 2002 £m | £m | 2001 £m |
|---|---|---|---|---|---|
| Net cash inflow from operating activities | 24 | | **41.6** | | 34.9 |
| Return on investments and servicing of finance | | | | | |
| Interest received | | **–** | | 0.1 | |
| Interest paid | | **(18.1)** | | (19.8) | |
| Net cash outflow from return on investments and servicing of finance | | | **(18.1)** | | (19.7) |
| Taxation | | | | | |
| Corporation tax paid | | | **(9.8)** | | (6.5) |
| Capital expenditure and financial investment | | | | | |
| Additions to properties | | **(50.9)** | | (95.9) | |
| Disposal of properties | | **16.9** | | 73.3 | |
| Disposal of subsidiary undertaking | | **–** | | 31.2 | |
| Purchase of other fixed assets | | **(0.3)** | | (0.2) | |
| Net cash (outflow)/inflow from capital expenditure and financial investment | | | **(34.3)** | | 8.4 |
| Equity dividends paid | | | **(5.2)** | | (4.6) |
| Cash (outflow)/inflow before management of liquid resources and financing | | | **(25.8)** | | 12.5 |
| Financing | | | | | |
| Movement in bank loans | 27 | | **26.0** | | (14.0) |
| Increase/(decrease) in cash in the year | | | **0.2** | | (1.5) |

The notes on pages 28 to 41 form part of these accounts.

# Notes

**1. Accounting policies**

Basis of accounting

The financial statements have been prepared under the historical cost convention, as modified by the revaluation of certain assets, and in accordance with applicable financial reporting standards. Compliance with SSAP19 "Accounting for Investment Properties" requires a departure from the requirements of the Companies Act 1985 relating to depreciation and amortisation and an explanation of this departure can be found under the heading for depreciation. The principal accounting policies are described below.

Basis of consolidation

The group accounts incorporate the accounts of Derwent Valley Holdings plc and all of its subsidiary undertakings made up to 31st December, together with the group's share of the results of its joint ventures, incorporating such adjustments as are appropriate, made up to a date no earlier than six months before 31st December. As permitted by section 230(3) of the Companies Act 1985, no profit and loss account is presented for the holding company.

Net revenue from properties

Gross rental income arises from operating leases. Rent receivable under the terms of the leases is adjusted, in accordance with UITF28, for the effect of any incentives given, which are spread on a straight line basis up to the time when the prevailing market rent will be payable. Void costs associated with major refurbishment schemes together with the initial letting costs of a development are capitalised in accordance with FRS15. All other costs incurred under operating leases are charged to the profit and loss account as they become payable.

Disposal of properties

The disposal of both investment and trading properties is accounted for on completion of contract. On disposal, any gain or loss is calculated by reference to the valuation at the last year end plus subsequent additions in the year.

Surrender premiums

Reverse premiums, after having first allocated an appropriate part of the premium to reinstate the premises to a lettable condition, are recognised in net revenue from properties at a rate equal to the gross rental income under the surrendered lease together with any associated void costs whilst the surrendered space remains vacant. Following reletting, or subject to there being no further significant costs as a result of the surrender, any residual premium is immediately released to the profit and loss account. Premiums paid are capitalised.

Properties

(i) Investment properties

Investment properties, as defined by SSAP19, are revalued annually by independent valuers in accordance with the Statements of Asset Valuation Practice and Guidance Notes issued by the Royal Institution of Chartered Surveyors and are included in the balance sheet on the basis of open market value. The aggregate surplus or deficit arising from such revaluation is transferred to the revaluation reserve. However, if on an individual property, a deficit arising from a valuation below cost is expected to be permanent, it is charged to the profit and loss account with any subsequent reversal being credited to the same.

**1. Accounting policies (continued)**

A property in the course of development is stated at its value at the time it was so designated, plus subsequent development costs less any permanent diminution in value. All outgoings, excluding interest, which can be fairly attributed to a development are considered development costs. The property is revalued once the certificate of practical completion has been issued.

(ii) Properties held for resale

Properties held for resale, including those under development, are stated at the lower of cost and net realisable value.

Investments

Investments in joint ventures are included in the group balance sheet at cost together with the appropriate share of post acquisition reserves and are presented in accordance with FRS9 "Associates and Joint Ventures".

Depreciation

No depreciation is provided in respect of freehold investment properties or leasehold investment properties with over 20 years of the lease remaining. This is a departure from the Companies Act 1985 but the directors consider that this accounting policy results in the financial statements giving a true and fair view. Depreciation and amortisation are only one of the many factors reflected in the annual valuation and the amount which might otherwise have been shown cannot be separately identified or quantified.

Leasehold investment properties with under 20 years of the lease remaining and leasehold improvements are amortised over the outstanding term of the lease. Other tangible fixed assets are depreciated at a rate between 10% and 25% per annum which is calculated to write off the cost, less estimated residual value of the assets, over their expected useful life.

Financial instruments

Financial instruments are used to manage the interest rate risk associated with the group's business and the financing thereof. No trading in financial instruments is undertaken. Short term debtors and creditors are excluded from the analysis of financial instruments given in note 18.

Deferred tax

Deferred tax balances are recognised in respect of all timing differences that have originated but not reversed by the balance sheet date except that deferred tax is not recognised on timing differences arising on revalued properties unless these are subject to a binding sale agreement. Deferred tax balances are not discounted.

# Notes

| 2. Property outgoings net of recoveries | 2002 £m | 2001 £m |
|---|---|---|
| Ground rents | 1.1 | 1.4 |
| Other property outgoings net of recoveries | 3.5 | 2.5 |
| | 4.6 | 3.9 |

| 3. (Loss)/profit on disposal of investments | 2002 £m | 2001 £m |
|---|---|---|
| Investment properties | | |
| Disposals | 16.9 | 73.3 |
| Cost/valuation | (16.7) | (71.8) |
| Profit on disposal of investment properties | 0.2 | 1.5 |
| Permanent diminution in value of investment properties | (2.2) | (0.8) |
| | (2.0) | 0.7 |
| Subsidiary undertaking | | |
| Disposal | – | 31.2 |
| Net assets on disposal | – | (28.1) |
| Profit on disposal of subsidiary undertaking | – | 3.1 |
| Total (loss)/profit on disposal of investments | (2.0) | 3.8 |

Profit on the sale of investments is calculated by reference to the valuation at the previous year end plus subsequent additions in the year. The permanent diminution in value in 2002 related to a valuation deficit realised on the disposal of an investment property in 2003. The profit on disposal of the subsidiary undertaking in 2001 related to the sale of Broadwick House through the disposal of Apexzone Limited.

| 4. Interest payable | 2002 £m | 2001 £m |
|---|---|---|
| Bank loans and overdraft wholly repayable within five years | 8.3 | 15.0 |
| Bank loans not wholly repayable within five years | 6.3 | 0.4 |
| Debenture stock | 3.6 | 3.6 |
| Group interest payable | 18.2 | 19.0 |
| Share of joint ventures' interest payable | 0.3 | 0.3 |
| | 18.5 | 19.3 |

| 5. Profit on ordinary activities before taxation | 2002 £m | 2001 £m |
|---|---|---|
| This is arrived at after crediting or charging: | | |
| Exceptional item - surrender premium received | – | 2.3 |
| Depreciation and amortisation | 0.1 | 0.1 |
| Rent payable under property leases | 1.1 | 1.4 |
| Auditors' remuneration | | |
| Audit | 0.1 | 0.1 |
| Other services | 0.1 | 0.1 |

The exceptional item in 2001 related to the surrender of a lease that resulted in a premium of £2,790,000 being received, which was included in gross rental income. Under the terms of the headlease, the freeholder of the property received a payment of £446,000. This was charged as ground rent in property outgoings net of recoveries.

| 6. Directors' emoluments | 2002 £m | 2001 £m |
|---|---|---|
| Remuneration for management services | 1.5 | 1.7 |
| Non-executive directors' remuneration | 0.1 | 0.1 |
| Pension contributions | 0.3 | 0.3 |
| Total emoluments | 1.9 | 2.1 |

Details of the directors' remuneration and of options granted to the directors under the group share option schemes are given in the report on directors' remuneration on pages 48 to 51.

Messrs. J. D. Burns and S. P. Silver are partners in Pilcher Hershman and Partners, estate agents, who have received fees at a commercial rate, in respect of the management, letting, acquisition and disposal of certain properties owned by the company's subsidiary undertakings amounting to £0.7m (2001 – £1.6m), excluding value added tax. This amount included management fees which were rechargeable to tenants of £0.5m (2001 – £0.5m). Pilcher Hershman and Partners occupy offices owned by the group for which they paid a commercial rent in the year of £0.1m (2001 – £0.1m).

| 7. Employees | 2002 £m | 2001 £m |
|---|---|---|
| Staff costs, including those of directors: | | |
| Wages and salaries | 2.3 | 2.5 |
| Social security costs | 0.3 | 0.4 |
| Pension costs | 0.5 | 0.4 |
| | 3.1 | 3.3 |

The average number of employees during the year, excluding directors, was 23 (2001 – 22), all of whom were employed in administrative roles.

# Notes

| **8. Taxation on profit on ordinary activities** | **2002 £m** | 2001 £m |
|---|---|---|
| UK corporation tax on profit, adjusted for the disposal of investments, at 30% (2001 – 30%) | **5.2** | 4.5 |
| Capital allowances | **(2.5)** | (2.3) |
| Tax on disposal of investments | **0.6** | 11.4 |
| Other reconciling items | **0.1** | – |
| Corporation tax payable on current year's profit | **3.4** | 13.6 |
| Less amount allocated to the statement of total recognised gains and losses | **(0.6)** | (9.7) |
| Corporation tax charge in respect of current year's profit | **2.8** | 3.9 |
| Adjustment in respect of prior years' corporation tax | **(0.3)** | (0.2) |
| Corporation tax charge | **2.5** | 3.7 |
| Deferred tax charge | **1.4** | 1.1 |
| | **3.9** | 4.8 |

**9. Profit for year attributable to members of Derwent Valley Holdings plc**

Profit on ordinary activities after taxation includes £8.5m (2001 – £17.2m) which has been dealt with in the accounts of the holding company.

| **10. Dividend** | **2002 £m** | 2001 £m |
|---|---|---|
| Ordinary shares of 5p each: | | |
| Paid – interim dividend of 3.05p (2001 – 2.75p) per share | **1.6** | 1.4 |
| Proposed – final dividend of 7.35p (2001 – 6.60p) per share | **3.9** | 3.6 |
| | **5.5** | 5.0 |

**11. Earnings per share**

Earnings per ordinary share have been computed on the basis of a profit after taxation of £11,525,000 (2001 – £16,841,000) and the weighted average number of ordinary shares in issue during the year of 53,158,000 (2001 – 53,157,000).
An adjusted earnings per share has been calculated using a profit of £13,557,000 (2001 – £14,740,000). This figure excludes the profit after tax arising from the disposal of investments in order to show the recurring element of the group's profit. The diluted earnings per share has been calculated using 53,268,000 (2001 – 53,285,000) ordinary shares which includes the number of dilutive share options outstanding at the year end.

**12. Total return**

Total return is defined as the increase in adjusted net asset value per share plus dividend per share expressed as a percentage of the adjusted net asset value per share at the beginning of the year.

| 13. Tangible assets | Group | | | | Company |
|---|---|---|---|---|---|
| | Freehold land and buildings £m | Leasehold property £m | Other fixed assets £m | Total £m | Other fixed assets £m |
| Cost or valuation: | | | | | |
| At 1st January 2002 | 540.6 | 292.9 | 1.0 | 834.5 | 1.0 |
| Additions | 40.0 | 4.4 | 0.3 | 44.7 | 0.3 |
| Disposals | (14.3) | (2.4) | (0.1) | (16.8) | (0.1) |
| Revaluation | (17.8) | (11.5) | – | (29.3) | – |
| At 31st December 2002 | 548.5 | 283.4 | 1.2 | 833.1 | 1.2 |
| Amortisation and depreciation: | | | | | |
| At 1st January 2002 | – | – | 0.4 | 0.4 | 0.4 |
| Disposals | – | – | (0.1) | (0.1) | (0.1) |
| Provision for year | – | – | 0.1 | 0.1 | 0.1 |
| At 31st December 2002 | – | – | 0.4 | 0.4 | 0.4 |
| Net book value: | | | | | |
| **At 31st December 2002** | **548.5** | **283.4** | **0.8** | **832.7** | **0.8** |
| At 31st December 2001 | 540.6 | 292.9 | 0.6 | 834.1 | 0.6 |
| Assets stated at cost or valuation: | | | | | |
| 31st December 2002 valuation | 523.8 | 283.4 | – | 807.2 | – |
| Prior years' valuation plus subsequent costs | 24.7 | – | – | 24.7 | – |
| Cost | – | – | 0.8 | 0.8 | 0.8 |
| | 548.5 | 283.4 | 0.8 | 832.7 | 0.8 |

Short leasehold property with a value of £16.5m (2001 – £16.7m) is included in leasehold property above. Investment property in the course of development with a carrying value of £24.7m (2001 – £34.4m) is included in freehold land and buildings above.

The freehold land and buildings and leasehold property, other than those in the course of development, were revalued by either Keith Cardale Groves (Commercial) Limited or CB Hillier Parker Limited, chartered surveyors, at open market value on 31st December 2002. At 31st December 2002 the historical cost of the freehold land and buildings and leasehold property owned by the group was £572.0m (2001 – £540.6m).

# Notes

| **14. Investments** | Company Subsidiary undertakings £m | Company Joint ventures £m | Company Total £m |
|---|---|---|---|
| Shares in subsidiary undertakings: | | | |
| At 1st January 2002 and 31st December 2002 | 185.4 | – | 185.4 |
| Loans: | | | |
| At 1st January 2002 | – | – | – |
| Movement in provisions | – | 0.1 | 0.1 |
| At 31st December 2002 | – | 0.1 | 0.1 |
| **Total at 31st December 2002** | **185.4** | **0.1** | **185.5** |
| Total at 31st December 2001 | 185.4 | – | 185.4 |

| **15. Debtors** | **Group 2002 £m** | Group 2001 £m | **Company 2002 £m** | Company 2001 £m |
|---|---|---|---|---|
| Trade debtors | **9.1** | 6.7 | **–** | – |
| Amounts owed by subsidiary undertakings | **–** | – | **338.1** | 316.2 |
| Other debtors | **0.4** | 0.5 | **0.1** | 0.1 |
| Prepayments and accrued income | **4.6** | 2.8 | **0.8** | 0.7 |
| Corporation tax | **–** | – | **1.8** | 0.7 |
| | **14.1** | 10.0 | **340.8** | 317.7 |

Group prepayments and accrued income includes £2.2m (2001 – £1.3m) which falls due for payment after more than one year.

| **16. Creditors falling due within one year** | **Group 2002 £m** | Group 2001 £m | **Company 2002 £m** | Company 2001 £m |
|---|---|---|---|---|
| Bank loans and overdraft | **1.4** | 1.6 | **0.8** | 1.9 |
| Amounts owed to subsidiary undertakings | **–** | – | **18.9** | 23.5 |
| Corporation tax | **2.4** | 9.1 | **–** | – |
| Other taxation and social security | **0.7** | 0.7 | **0.1** | 0.1 |
| Other creditors | **7.7** | 2.6 | **0.3** | 0.4 |
| Dividend payable | **3.9** | 3.6 | **3.9** | 3.6 |
| Accruals and deferred income | **17.3** | 19.4 | **5.3** | 5.6 |
| | **33.4** | 37.0 | **29.3** | 35.1 |

Other creditors includes an amount of £4.0m (2001 – £nil) in respect of the balance of an assignment inducement of £11.3m net of VAT received during the year. The payment relates to the assignment of a lease and has been accounted for in accordance with the group's accounting policy on reverse premiums.

| **17. Creditors falling due after more than one year** | **Group 2002 £m** | 2001 £m | **Company 2002 £m** | 2001 £m |
|---|---|---|---|---|
| Accruals and deferred income | **1.6** | – | **–** | – |
| Bank loans | **261.0** | 235.0 | **261.0** | 235.0 |
| 10⅛% First Mortgage Debenture Stock 2019 | **34.4** | 34.4 | **34.4** | 34.4 |
| | **297.0** | 269.4 | **295.4** | 269.4 |

In accordance with FRS4, "Capital Instruments", the £35,000,000 10⅛% First Mortgage Debenture Stock 2019 is shown net of the unamortised discount and costs on issue of £0.6m (2001 – £0.6m).

| **18. Borrowings** | **Group 2002 £m** | 2001 £m | **Company 2002 £m** | 2001 £m |
|---|---|---|---|---|
| Bank loans and overdraft wholly repayable: | | | | |
| less than 1 year | **1.4** | 1.6 | **0.8** | 1.9 |
| between 1-2 years | **–** | 10.0 | **–** | 10.0 |
| between 2-5 years | **30.0** | 140.0 | **30.0** | 140.0 |
| more than 5 years | **231.0** | 85.0 | **231.0** | 85.0 |
| 10⅛% First Mortgage Debenture Stock 2019 | **34.4** | 34.4 | **34.4** | 34.4 |
| | **296.8** | 271.0 | **296.2** | 271.3 |

The bank loans and overdraft are secured by charges on certain of the group's properties.

| | **Group 2002 £m** | 2001 £m | **Company 2002 £m** | 2001 £m |
|---|---|---|---|---|
| Undrawn committed bank facilities were: | | | | |
| expiring in less than 1 year | **3.6** | 20.9 | **3.6** | 20.9 |
| expiring between 1-2 years | **–** | 7.5 | **–** | 7.5 |
| expiring between 2-5 years | **70.0** | 50.0 | **70.0** | 50.0 |
| expiring beyond 5 years | **94.0** | 115.0 | **94.0** | 115.0 |
| | **167.6** | 193.4 | **167.6** | 193.4 |

# Notes

**18. Borrowings (continued)**

After taking into account the various interest rate hedging instruments entered into by the group, the interest rate exposure of the group's borrowings was:

| | Floating rate borrowings £m | Hedged borrowings £m | Fixed rate borrowings £m | Total £m | Weighted average cost of borrowing % | Weighted average life Years |
|---|---|---|---|---|---|---|
| **At 31st December 2002** | **142.4** | **120.0** | **34.4** | **296.8** | **6.33** | **7.44** |
| At 31st December 2001 | 126.6 | 110.0 | 34.4 | 271.0 | 6.70 | 6.44 |

Details of the group's fixed rate borrowings, which comprise the Debenture Stock 2019, and the instruments used to hedge its floating rate borrowings are summarised below:

| Instrument | Principal £m | Weighted average interest rate % | Weighted average life Years | Fair value £m | Fair value adjustment £m |
|---|---|---|---|---|---|
| 10⅛% First Mortgage Debenture Stock 2019 | 35.0 | 10.125 | 16.59 | 46.3 | (11.3) |
| Interest rate swaps | 120.0 | 6.05 | 3.31 | 5.7 | (5.7) |
| **At 31st December 2002** | | | | **52.0** | **(17.0)** |
| 10⅛% First Mortgage Debenture Stock 2019 | 35.0 | 10.125 | 17.59 | 45.1 | (10.1) |
| Interest rate swaps | 105.0 | 6.27 | 3.96 | 2.4 | (2.4) |
| Interest rate collars | 5.0 | cap 8.000<br>floor 6.500 | 0.04 | – | – |
| At 31st December 2001 | | | | 47.5 | (12.5) |

10⅛% First Mortgage Debenture Stock 2019

The market price for the debenture at 31st December 2002 was £132.375 (2001 – £128.875) which gave rise to a value of £46,331,000 (2001 – £45,106,000). At this price, the gross redemption yield on the debenture was 6.83% (2001 – 7.20%) implying a margin of 2.4% (2001 – 2.15%) over the 8% Treasury 2015 gilt. The fair value adjustment effectively represents the net present value of the difference between the contracted fixed rate of the debenture and the gross redemption yield on the benchmark gilt at 31st December 2002.

Interest rate swaps

The fair values represent the net present value of the difference between the contracted fixed rates and the fixed rates payable if the swaps were to be replaced on 31st December 2002 for the period to the contracted expiry dates.

Interest rate collars

Interest rate collars comprised interest rate caps purchased and interest rate floors sold. These expired in 2002. The fair values at 31st December 2001 represented the net cost of replacement on identical terms at prices prevailing at that date.

Further details on financial instruments are given in the financial review on page 23.

| 19. Deferred tax | Group £m |
|---|---|
| At 1st January 2002 | 8.8 |
| Provided during the year | 1.4 |
| **At 31st December 2002** | **10.2** |

The provision for deferred tax relates to timing differences on accelerated capital allowances and other reversing timing differences. No such liability exists for the company (2001 – £nil).

A taxation liability of approximately £62.8m (2001 – £74.3m) would arise on the disposal of land and buildings at the valuation shown in the balance sheet. This is equivalent to 118p per share (2001 – 140p). In accordance with FRS19 no provision has been made for this. No such liability exists for the company (2001 – £nil).

| 20. Other provisions | Group and company £m |
|---|---|
| At 1st January 2002 | 0.8 |
| Released during the year | (0.2) |
| Provided during the year | 0.4 |
| **At 31st December 2002** | **1.0** |

The provision relates to an onerous lease which expires in 2014 and reflects the discounted present value of future net payments under that lease.

| 21. Share capital | Authorised £m | Issued and fully paid £m |
|---|---|---|
| At 1st January 2002 and 31st December 2002 | 3.55 | **2.6** |

The number of shares in issue at the year end was 53,160,972 (2001 – 53,156,972). During the year, 4,000 shares were issued as a result of the exercise of share options.

# Notes

| 22. Reserves | Share premium account £m | Revaluation reserve £m | Profit and loss account £m |
|---|---|---|---|
| Group | | | |
| At 1st January 2002 | 153.7 | 294.0 | 83.4 |
| Deficit on property revaluation | – | (27.1) | – |
| Profit realised on disposal of investments | – | (4.0) | 4.0 |
| Tax attributable to profit realised on disposal of investments | – | – | (0.6) |
| Retained profit for the year | – | – | 6.0 |
| **At 31st December 2002** | **153.7** | **262.9** | **92.8** |
| Company | | | |
| At 1st January 2002 | 153.7 | – | 42.1 |
| Retained profit for the year | – | – | 3.0 |
| **At 31st December 2002** | **153.7** | **–** | **45.1** |

**23. Net asset value per share**

Net asset value per share has been calculated on the basis of net assets at 31st December 2002 of £512,003,000 (2001 – £533,657,000) and the number of ordinary shares in issue at the year end of 53,161,000 (2001 – 53,157,000).

An adjusted net asset value per share has been calculated using net assets of £522,138,000 (2001 – £542,415,000). This figure excludes the deferred tax provided in accordance with FRS19 on the basis that it is unlikely that this liability will crystallise.

| **24. Net cash inflow from operating activities** | **2002 £m** | 2001 £m |
|---|---|---|
| Cash received from: | | |
| Tenants | **53.8** | 47.5 |
| Cash payments in respect of: | | |
| Direct property expenses | **(4.7)** | (3.8) |
| Wages and salaries | **(3.6)** | (3.3) |
| Administrative costs | **(2.8)** | (2.7) |
| Properties held for resale | **(1.1)** | (2.8) |
| | **41.6** | 34.9 |

| **25. Reconciliation of operating profit to net cash inflow from operating activities** | **2002 £m** | 2001 £m |
|---|---|---|
| Operating profit | **35.6** | 36.8 |
| Depreciation charge | **0.1** | 0.1 |
| Increase in debtors | **(4.1)** | (0.2) |
| Increase/(decrease) in creditors | **4.8** | (1.3) |
| Increase in properties held for resale | **(1.2)** | (2.8) |
| Effect of other deferrals and accruals on operating activity cash flow | **6.4** | 2.3 |
| Net cash inflow from operating activities | **41.6** | 34.9 |

| **26. Reconciliation of net cash flow to movement in net debt** | **2002 £m** | 2001 £m |
|---|---|---|
| (Increase)/decrease in cash in the year | **(0.2)** | 1.5 |
| Cash inflow/(outflow) from movement in bank loans | **26.0** | (14.0) |
| Amortisation of discount and costs on issue of debenture | **–** | 0.1 |
| Movement in net debt in the year | **25.8** | (12.4) |
| Opening net debt | **271.0** | 283.4 |
| Closing net debt | **296.8** | 271.0 |

# Notes

| 27. Movement in net debt | 1st January 2002 £m | Cash flow £m | Other £m | **31st December 2002 £m** |
|---|---|---|---|---|
| Overdraft | 1.6 | (0.2) | – | **1.4** |
| Bank loans wholly repayable: | | | | |
| between 1 – 2 years | 10.0 | – | (10.0) | **–** |
| between 2 – 5 years | 140.0 | (20.0) | (90.0) | **30.0** |
| more than 5 years | 85.0 | 46.0 | 100.0 | **231.0** |
| | 235.0 | 26.0 | – | **261.0** |
| 10⅛% First Mortgage Debenture Stock 2019 | 34.4 | – | – | **34.4** |
| Total | 271.0 | 25.8 | – | **296.8** |

**28. Principal operating companies**

The principal operating companies within the group are as follows:

| | Class of shares | Principal activity |
|---|---|---|
| Subsidiary undertakings | | |
| Derwent Valley Central Limited (previously Colebrook Estates Limited) | Ordinary | Property investment |
| Derwent Valley London Limited (previously Wilmar Estates Limited) | Ordinary | Property investment |
| Derwent Valley Property Investments Limited | Ordinary | Property investment |
| Derwent Valley Property Developments Limited | Ordinary | Property investment |
| Derwent Valley Property Trading Limited | Ordinary | Property trading |

Each of the above companies' share capital is wholly owned by the group.

| | Class of shares | Principal activity |
|---|---|---|
| Joint ventures | | |
| Primister Limited | Ordinary | Property investment |
| Dorrington Derwent Holdings Limited | Ordinary | Holding company |

The company owns 50% of the ordinary shares of each of the joint ventures which are accounted for and disclosed in accordance with FRS9, "Associates and Joint Ventures". All of the above companies are registered and operate in England and Wales.

**29. Capital commitments**

Contracts for capital expenditure entered into by the group at 31st December 2002 and not provided for in the accounts amounted to £6.4m (2001 – £21.3m).

**30. Lease commitments**

At 31st December 2002, annual commitments under property leases expiring in more than 5 years were £1.4m (2001 – £1.1m).

**31. Pension commitments**

The company operates a defined contribution pension scheme. The contributions payable to the pension scheme are charged to the profit and loss account in the accounting period to which they relate.

**32. Post balance sheet events**

On 3rd March 2003, the group purchased a portfolio of properties for a consideration of £37.8m before costs and on 7th March 2003 sold a property for an effective consideration of £32.2m before costs.

**33. Contingent liabilities**

The company and its subsidiary undertakings are party to cross guarantees securing the overdraft and certain bank loans. At 31st December 2002 the maximum liability that could arise for the company from the cross guarantees amounted to £0.6m (2001 – £nil). The company has guaranteed its share of a loan to Primister Limited, the contingent liability for which at 31st December 2002 amounted to £2.8m (2001 – £2.8m). In addition, the company guarantees its share of interest payable on this loan which amounts to £0.3m per annum (2001 – £0.3m).

# Directors' report

The directors present their report and the financial statements for the year ended 31st December 2002.

**Results and dividend**

Profit before taxation from ordinary activities was £15.4m (2001 – £21.7m) and profit after taxation amounted to £11.5m (2001 – £16.9m). The directors recommend a final dividend of 7.35p per ordinary share. This, when taken with the interim dividend of 3.05p per share, paid on 4th November 2002, gives a total dividend of 10.40p (2001 – 9.35p) per ordinary share for the year ended 31st December 2002, amounting to £5.5m. After ordinary dividends, £6.0m (2001 – £11.9m) was transferred to revenue reserves.

**Principal activities, trading review and future developments**

The principal activities of the group are those of property investment, refurbishment and redevelopment, and trading. A review of the business and comments on the future outlook for the group can be found within the chairman's statement, property review and financial review on pages 4 to 23.

**Directors**

The directors of the company during the year and their interests in the share capital of the company, including shares over which options have been granted, are shown below. All of these interests are held beneficially.

| | Ordinary shares of 5p each | | Options | |
|---|---|---|---|---|
| | **31st December 2002** | 31st December 2001 | **31st December 2002** | 31st December 2001 |
| J. C. Ivey | **79,072** | 79,072 | **–** | – |
| J. D. Burns | **686,998** | 679,013 | **161,257** | 137,257 |
| S. P. Silver | **272,675** | 269,589 | **136,181** | 115,931 |
| C. J. Odom | **12,650** | 12,650 | **105,521** | 90,521 |
| N. Q. George | **–** | – | **82,951** | 72,201 |
| P. M. Williams | **2,000** | 2,000 | **89,110** | 76,860 |
| I. Yeatman | **–** | – | **–** | – |
| S. J. Neathercoat | **1,000** | – | **–** | – |

There have been no changes in directors' shareholdings between the year end and 11th March 2003.
During the year, options over 82,250 shares were granted to the directors at an exercise price of £6.725. No director exercised options during the year. Full details of the directors' options are given in the report on directors' remuneration which commences on page 48.
In accordance with the articles of association, Messrs. J. C. Ivey, J. D. Burns and C. J. Odom, who retire by rotation, and Mr R. Farnes, who has been appointed since the last annual general meeting, being eligible, offer themselves for re-election. Biographies of all the directors are given on page 47.
Other than as disclosed in note 6, the directors have no interest in any material contracts of the company.

**Fixed assets**

The group's freehold and leasehold investment properties were professionally revalued at 31st December 2002, resulting in a deficit of £29.3m. The freehold and leasehold investment properties are included in the group balance sheet at a total value of £831.9m.

**Charitable donations**

During the year, the group made charitable donations amounting to £77,000.

**Substantial shareholders**

In addition to those of the directors disclosed above, the company has been notified of the following interests in the issued ordinary share capital as at 11th March 2003:

| | Number of shares | Percentage of issued share capital |
|---|---|---|
| Royal & SunAlliance Investments | 3,352,127 | 6.31 |
| Stichting Pensioenfonds ABP | 3,050,818 | 5.74 |
| Standard Life Assurance Company | 2,590,766 | 4.87 |
| Scottish Widows Investment Partnership | 2,211,008 | 4.16 |
| Aegon Asset Management UK plc | 2,119,116 | 3.99 |
| Morley Fund Management Limited | 2,074,736 | 3.90 |
| Threadneedle Asset Management Limited | 1,657,425 | 3.12 |
| Legal and General Investment Management | 1,601,229 | 3.01 |

**Creditor payment policy**

It is the group's policy to agree terms of business with suppliers prior to the supply of goods or services. In the absence of any dispute, the group pays in accordance with these agreed terms. For the year ended 31st December 2002, the average payment period for trade creditors was 18 days (2001 – 18 days).

**Corporate governance**

The company is required to comply with "The Combined Code – Principles of Good Governance and Code of Best Practice" ("the Combined Code") which is appended to the Listing Rules of the Financial Services Authority. The board believes that the company has complied with the Combined Code throughout the period and has set out below how the 14 principles of good governance in the Combined Code have been applied.

The board

Throughout 2002, the board comprised Mr. Ivey, the non-executive chairman, five executive directors, Messrs. Burns, Silver, Odom, George and Williams and two independent non-executive directors, Messrs. Yeatman and Neathercoat.
Mr. Yeatman was the senior non-executive director throughout the year. Biographies of the directors are given on page 47.
Five meetings of the full board are scheduled each year and a formal list of matters is reserved for its approval. The board is provided with comprehensive papers in a timely manner to ensure that the directors are fully briefed on matters to be discussed by the board. Additional meetings are arranged when necessary.
Since 1993, the board has maintained a number of board committees. Set out below are details of the membership and duties of the three principal committees.

• Remuneration committee

Throughout 2002, the committee consisted of Mr. Yeatman as chairman and Mr. Neathercoat. The committee is responsible for establishing the company's remuneration policy and individual remuneration packages for the executive directors.
The report on directors' remuneration is set out on pages 48 to 51.

• Audit committee

Messrs. Yeatman, Ivey and Neathercoat served on this committee throughout the year under the chairmanship of Mr. Yeatman. The committee is responsible for the appointment of the external auditors, reviewing the scope of the audit, discussing the results thereof and any control issues arising therefrom, and reviewing the interim and annual financial statements. The committee also considers the adequacy of the statement of independence issued by the group's auditors having particular regard to the extent of non-audit services.

# Directors' report

• Nominations committee
Mr. Ivey is chairman of this committee which, during the year, consisted of the non-executive directors and Mr. Burns. The committee is responsible for identifying external candidates for appointment as directors and, subsequently, recommending their appointment to the board. The committee may also be requested by the board to make a recommendation concerning the appointment to the board from within the company.

Directors
Appointment of a director from outside the company is on the recommendation of the nominations committee, whilst internal promotion is a matter decided by the board unless it is considered appropriate for a recommendation to be requested from the nominations committee. All new directors must stand for election at the first annual general meeting following their appointment. Existing directors must submit themselves for re-election at least once every three years.
If considered appropriate, new directors are sent on an external training course addressing their role and duties as a director of a quoted public company.
Any director may instigate an agreed procedure whereby independent professional advice may be sought at the company's expense.

Communication with shareholders
The company has always recognised the importance of clear communication with shareholders and has maintained a regular dialogue with institutional shareholders and fund managers. The annual report, which is sent to all shareholders, reinforces this communication. The annual general meeting provides an opportunity for shareholders to question the directors and, in particular, the chairman of each of the board committees.

Internal control
The directors recognise that they have overall responsibility for ensuring that the group maintains a sound system of internal control that provides the board with reasonable assurance regarding effective and efficient operations, internal financial control and compliance with laws and regulations.
Such a system can only manage business risk, not eliminate it, and cannot provide absolute assurance against material misstatement or loss. Accordingly, the system is designed to provide reasonable assurance that material risks and problems are identified and appropriate remedial measures taken on a timely basis.
The board performs an annual review of the effectiveness of the group's system of internal control and believes that an ongoing process for identifying, evaluating and managing the significant risks faced by the group has been in place from 1st January 2002 to 11th March 2003. During the period, the board has monitored the operation of the system with a view to further integrating it into the business processes where possible and to address any areas for improvement as they are identified.
The board has considered the need for an internal audit function but continues to believe that this would not be appropriate.

Going concern
Having made due enquiries, the directors have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future. Therefore, the board continues to adopt the going concern basis in preparing the accounts.

Corporate social responsibility
The board recognizes the importance of the group's relationship with the economy, community and environment within which it operates and considers matters relating thereto to be the responsibility of the whole board. However, the group's business of managing, refurbishing and redeveloping a portfolio of London properties is conducted by 29 employees all located in one Central London office. Consequently, when the board considered its approach to the many matters encapsulated by corporate social responsibility it concluded that, given the nature and location of the group's activities and the centralised staffing, formal policies were required for only two issues – the environment and health and safety.

Details of the measures taken by the group in these areas, together with the informal policies adopted in other areas, are given below.

Environmental policy
The board commissioned and adopted an environmental policy document and this is issued to all appropriate professional advisers and members of staff.
During the year, an environmental action plan was prepared which set objectives for the group's performance concerning timber, ozone depleters, energy, waste and water usage. The initial result of this has been to establish base levels of achievement which has enabled targets to be set for the future. The action plan also set objectives concerning the environmental aspects of property acquisition and general procurement.
Additionally, the group undertook an audit of all its properties in order to ascertain the amount of asbestos and ozone depleters present in the portfolio. The audit did not reveal any significant amounts of contaminant and measures are now being implemented to appropriately manage and, if possible, replace these materials.
A copy of the group's environmental policy is available to the public on request and a summary can be found on the group's website.

Health and safety
A formal health and safety policy has been adopted by the board and this has been embedded in the management regime for the group's development sites. To ensure compliance with the policy, an executive is assigned to each scheme to monitor performance. The board receives regular reports from each site together with notification of any accidents that require reporting under the Health and Safety regulations.
The policy is reviewed at regular intervals and revised as necessary.

Community/society
Whilst no formal policy has been adopted concerning this aspect of corporate responsibility, the board is aware of the benefits to the group of London's status as a centre of business. The board is also aware that through sensitive planning and involvement with local initiatives it can contribute to preserving and enhancing this status. Accordingly, the company is represented in both the New West End Company and The Westminster Property Owners Association, both of which address some of the key problems facing London, namely security, planning and transport.
On a wider social perspective, the group has continued to sponsor the Royal Academy's annual architectural lecture and architectural forums. During 2002, a major fund raising event was sponsored on behalf of Teenage Cancer Trust and the group coordinated advice for the trust's development programme.

**Annual general meeting**
The notice of meeting includes three resolutions to be considered as special business.

Resolution 9 renews the authority under Section 80 of the Companies Act 1985 for the directors to allot shares up to an aggregate nominal amount of £886,016.20 representing about one third of the issued share capital at the date of the notice of meeting. The directors have no present intention of issuing shares except on the exercise of options under the company's share option schemes. The authority will expire at the conclusion of the next annual general meeting after the passing of the resolution.

Resolution 10 is a special resolution proposed annually, renewing the directors' authority under Section 95 of the Companies Act 1985. The resolution empowers the directors to allot shares for cash in connection with pre-emptive offers with modifications to the requirements set out in Section 89 of the Companies Act 1985. The resolution further empowers the directors to allot shares for cash, otherwise than on a pre-emptive basis, up to an aggregate nominal value of £132,902.40 which is equivalent to 5% of the issued share capital at the date of the notice of meeting. The authority will expire at the conclusion of the next annual general meeting after the passing of the resolution.

# Directors' report

Resolution 11 is proposed to renew the authority enabling the company to purchase its own shares. This authority enables the directors to act quickly if, having taken account of all major factors such as the effect on earnings and net asset value per share, gearing levels and alternative investment opportunities, such purchases are considered to be in the company's and shareholders' best interest while maintaining an efficient capital structure. The resolution gives the directors authority to purchase up to 10% of the company's ordinary shares and specifies the maximum and minimum prices at which shares may be bought. The total number of options to subscribe for ordinary shares outstanding at 11th March 2003 was 621,270, which represented 1.17% of the issued share capital at that date. If the company was to purchase the maximum number of ordinary shares permitted by this resolution, the options outstanding at 11th March 2003 would represent 1.30% of the issued share capital.

**Auditors**
BDO Stoy Hayward have expressed their willingness to continue in office and a resolution to re-appoint them will be proposed at the annual general meeting.

By order of the board
T. J. Kite, ACA
Secretary

11th March 2003

# Statement of directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and group and of the profit or loss of the group for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Financial statements are published on the group's website in accordance with legislation in the United Kingdom governing the preparation and dissemination of financial statements, which may vary from legislation in other jurisdictions. The maintenance and integrity of the group's website is the responsibility of the directors. The directors' responsibility also extends to the ongoing integrity of the financial statements contained therein.

# Directors

**J. C. Ivey**
Non-executive chairman
A chartered accountant, Mr Ivey, 61, is chief executive of The Davis Service Group plc. He chairs the nominations committee and is a member of the audit committee.

**J. D. Burns**
Managing director
Mr Burns is 58 years old and has overall responsibility for group strategy, business development and day to day operations. He is a non-executive director of The Davis Service Group plc and a consultant partner at Pilcher Hershman & Partners, estate agents. A member of the nominations committee.

**S. P. Silver**
Aged 52, Mr Silver has overall responsibility for acquisitions, design and development projects. He is also a consultant partner in Pilcher Hershman & Partners.

**C. J. Odom**
Mr Odom, 52, is a chartered accountant and has overall responsibility for financial strategy, treasury, taxation and financial reporting.

**N. Q. George**
A chartered surveyor, Mr George was appointed to the board in 1998. Aged 39, he has responsibility for acquisitions and investment analysis.

**P. M. Williams**
Mr Williams is a chartered surveyor. He is 43 years old and was appointed to the board in 1998. His responsibilities include asset management and supervision of refurbishment and development projects.

**I. Yeatman**
Senior non-executive director
Mr Yeatman is 65 years old and a chartered surveyor. He joined the board in 1995 and is chairman of both the audit and remuneration committees. He is also a member of the nominations committee.

**S. J. Neathercoat**
Non-executive director
Mr Neathercoat, 54, is a chartered accountant. He joined the board in March 1999 and is a member of the audit, remuneration and nominations committees.

**R. Farnes**
Non-executive director
Mr Farnes, 57, is a chartered surveyor. He recently retired as chairman of CB Hillier Parker and joined the board on 1st April 2003.

# Report on directors' remuneration

**Remuneration committee**

The committee consisted of Mr. Yeatman and Mr. Neathercoat. Neither member has any personal interest in the matters decided by the committee, nor any day to day involvement in the running of the business and, therefore, are considered to be independent. The committee meets at least 3 times a year to consider the terms and conditions of employment of the executive directors, to set remuneration levels and to operate the group's performance related bonus and share option schemes.

During the year, New Bridge Street Consultants provided the performance statistics required to operate the share option scheme and the committee appointed Watson Wyatt to provide remuneration data on a group of comparable companies. Neither firm of consultants provide any other services to the company. No director had any involvement in determining his own remuneration although some of the matters considered by the committee were discussed with Mr. Burns.

**Policy**

The committee's objective in formulating the remuneration policy for the executive directors is to ensure that the company attracts, employs and motivates executives with the skills and experience necessary to make a significant contribution to the delivery of the group's objectives.

When setting the level of remuneration, the committee aims to achieve broad comparability with other FTSE 250 companies that have delivered similar long term returns to shareholders whilst having particular regard to the levels of remuneration prevailing in the property sector.

The committee recognises the importance of aligning, as far as possible, the interests of the directors with those of the shareholders. To this end, a combination of basic salary, annual bonus and share options is used, by which the committee aims to provide a significant proportion of the directors' total remuneration through performance related elements.

**Service contracts**

The service contracts of Messrs. Burns, Silver and Odom are dated 20th May 1997 whilst those of Messrs. George and Williams are dated 31st March 1999. The contracts have no stated termination date but require 12 months' notice of termination and include provision for the company to pay, by way of liquidated damages, a cash amount equivalent to 12 months salary and benefits in kind plus a pension contribution of at least 20% of basic salary. The remuneration committee reviews the service contracts periodically. The non-executive directors do not have service contracts and are appointed for three year terms which expire as follows: Mr. Ivey, 12th December 2005; Mr. Yeatman, 30th November 2004 and Mr. Neathercoat, 28th February 2005.

**Basic salary and benefits**

Basic salaries for executive directors are reviewed annually by the remuneration committee having regard to the remuneration policy set out above. Pension contributions for the five executive directors are based solely on basic salaries and paid into a defined contribution scheme. The principal benefits in kind comprise a company car and medical insurance.

The remuneration for non-executive directors, which consists of fees for their services in connection with board and board committee meetings and, where relevant, for additional services such as chairing a board committee, is set by the whole board. Non-executive directors are not eligible for pension scheme membership and do not participate in the company's bonus or share option schemes.

Details of directors' remuneration are given in table 1 below:

**Table 1**

| | Salary and fees £'000 | Estimated bonus £'000 | Benefits in kind £'000 | **2002 Total £'000** | **2002 Pension £'000** | Under provision of 2001 bonus £'000 | Revised 2001 Total £'000 | 2001 Pension £'000 |
|---|---|---|---|---|---|---|---|---|
| Executive | | | | | | | | |
| J. D. Burns | 335 | 34 | 36 | **405** | **103** | 28 | 531 | 94 |
| S. P. Silver | 282 | 28 | 26 | **336** | **99** | 25 | 444 | 93 |
| C. J. Odom | 212 | 21 | 9 | **242** | **62** | 15 | 302 | 59 |
| N. Q. George | 160 | 16 | 9 | **185** | **37** | 13 | 236 | 33 |
| P. M. Williams | 175 | 17 | 11 | **203** | **42** | 15 | 268 | 39 |
| Non-executive | | | | | | | | |
| J. C. Ivey | 25 | – | – | **25** | **–** | – | 25 | – |
| I. Yeatman | 20 | – | – | **20** | **–** | – | 20 | – |
| S. J. Neathercoat | 20 | – | – | **20** | **–** | – | 20 | – |
| | 1,229 | 116 | 91 | **1,436** | **343** | 96 | 1,846 | 318 |

The under provision of the 2001 bonus, which has been charged in the 2002 results, is the amount by which the final award under the bonus scheme, which could only be ascertained once the results of all the comparator companies had been announced, exceeded the estimated amount included in the 2001 results. The total remuneration for 2001, which was previously disclosed as £1,750,000, has been revised to allow a correct comparison to be made between the two years.

**Bonus scheme**

The company operates an all employee, performance related, bonus scheme under which entitlements are calculated by reference to the group's performance relative to a group of UK quoted companies with similar characteristics to those of the group. Performance is measured in terms of net asset value per share and the directors' maximum entitlement of 34% of basic pay is payable if the group is ranked in the upper quartile of the comparator group. Second quartile performance results in an entitlement of 15% whilst a 5% bonus is payable for third quartile performance. No bonus is due for lower quartile results.

Additional amounts, the total of which cannot exceed the total of the performance related entitlement, may be awarded by the remuneration committee to individuals, based on an assessment of both the individual's performance and that of the group.

**Share option schemes**

The Derwent Valley Holdings 1997 Executive Share Option Scheme was approved by shareholders on 3rd June 1997. The purpose of the scheme is to incentivise the participants on a medium to long term basis and to recognise, to the extent appropriate, the linkage between management performance and shareholder returns.

Performance criteria apply to both the grant and exercise of options. Options are granted annually, at a price equal to the market price of the company's shares on a day not more than 30 days prior to the date of grant, subject to there being sufficient capacity within the overall scheme rules. The market value of shares over which options are granted each year is limited to an individual's basic salary.

# Report on directors' remuneration

This maximum entitlement is then adjusted to reflect the group's ranking, measured by total shareholder return, within a comparator group consisting of the following companies:

| | | |
|---|---|---|
| NHP plc | Daejan Holdings plc | Capital and Regional plc |
| Ashtenne Holdings plc | St Modwen Properties plc | Pillar Property plc |
| Helical Bar plc | Shaftesbury plc | Chelsfield plc |
| Brixton Estate plc | Freeport plc | Quintain Estates & Development plc |
| Benchmark Group plc | Minerva plc | |

Upper quartile performance means that no reduction is made to the award. A second quartile ranking reduces the award by 25% while third and fourth quartile performance results in the award being reduced by 50%. Total shareholder return is used as the performance indicator because the committee believes that, over the medium to long term, this measure reflects most closely the success of the directors in delivering value to the shareholders. When measuring the return, the first and last months are averaged to avoid undue fluctuations. The value of shares over which options can be granted in any ten year period may not exceed four times an individual's basic salary.

Details of the options held by directors and employees under the group's share option schemes at 31st December 2002 are given in table 2 below:

**Table 2**

| Exercise price £ | Date from which exercisable | Expiry date | Directors J.D. Burns | S.P. Silver | C.J. Odom | N.Q. George | P.M. Williams | Employees | Total number of shares |
|---|---|---|---|---|---|---|---|---|---|
| 1.910 | 5/5/96 | 4/5/03 | – | – | – | 2,556 | 3,622 | – | 6,178 |
| 2.370 | 12/4/98 | 11/4/05 | – | – | – | 18,450 | 14,350 | – | 32,800 |
| 3.450 | 26/4/99 | 25/4/06 | 8,507 | 7,431 | 7,021 | 5,945 | 3,638 | – | 32,542 |
| 5.690 | 15/4/01* | 14/4/08 | 31,500 | 27,000 | 21,500 | 10,500 | 13,500 | 8,500 | 112,500 |
| 5.530 | 16/4/02* | 15/4/09 | 25,250 | 21,500 | 16,500 | 8,750 | 10,750 | 10,750 | 93,500 |
| 5.015 | 14/4/03* | 13/4/10 | 30,000 | 25,000 | 19,000 | 11,000 | 13,000 | 13,000 | 111,000 |
| 7.235 | 12/4/04* | 11/4/11 | 42,000 | 35,000 | 26,500 | 15,000 | 18,000 | 18,500 | 155,000 |
| Outstanding at 1st January 2002 | | | 137,257 | 115,931 | 90,521 | 72,201 | 76,860 | 50,750 | 543,520 |
| Options granted during the year | | | | | | | | | |
| 6.725 | 15/4/05* | 14/4/12 | 24,000 | 20,250 | 15,000 | 10,750 | 12,250 | 15,500 | 97,750 |
| Options exercised or lapsed during the year | | | | | | | | | |
| Exercise price £ | | Market price at date of exercise £ | | | | | | | |
| 5.530 | | 6.40 | – | – | – | – | – | (4,000) | (4,000) |
| 5.015 | | – | – | – | – | – | – | (5,000) | (5,000) |
| 7.235 | | – | – | – | – | – | – | (6,000) | (6,000) |
| 6.725 | | – | – | – | – | – | – | (5,000) | (5,000) |
| Outstanding at 31st December 2002 | | | 161,257 | 136,181 | 105,521 | 82,951 | 89,110 | 46,250 | 621,270 |

*These options were granted under the 1997 Executive Share Option Scheme.

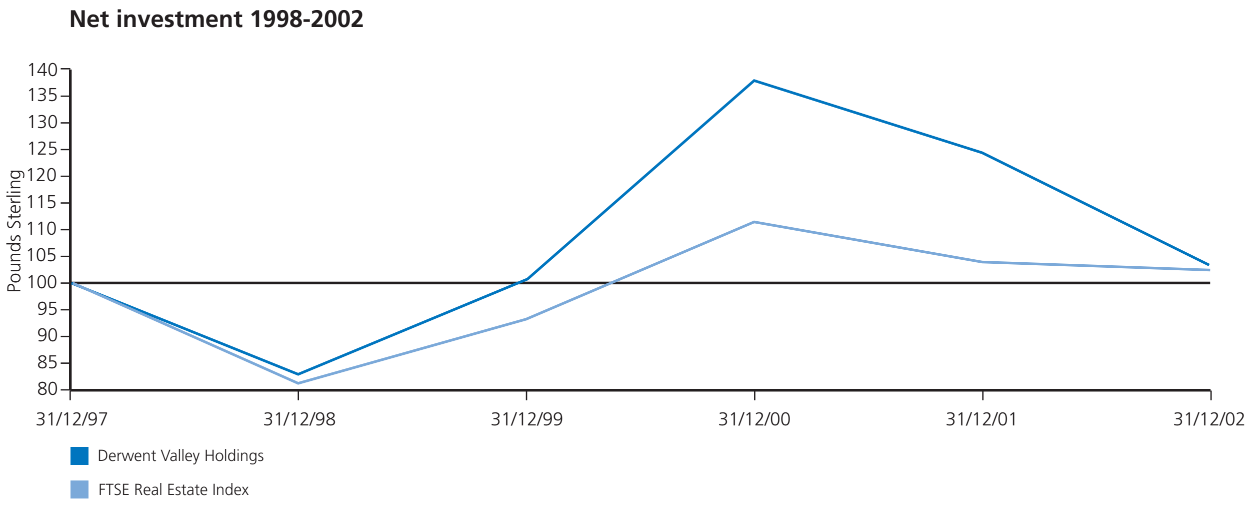
The exercise of options granted under the 1997 Executive Share Option Scheme is subject to a three year performance criteria. This states that a year's options can only be exercised once the growth of the group's net asset value per share over a subsequent three year period exceeds the increase of the IPD Central London Office Capital Growth Index over the same period by 6% or more. Those exercisable on 15th April 2001 and 16th April 2002 have met this criteria. Subsequent options have yet to be tested.

The market price of the 5p ordinary shares at 31st December 2002 was £5.41. During the year, they traded in a range between £5.35 and £8.42.

The company does not operate a long term incentive plan.

**Performance graph**

Total shareholder return compared to the FTSE Real Estate Index




This graph shows the value, by the end of 2002, of £100 invested in Derwent Valley Holdings on 31st December 1997 compared to that of £100 invested in the FTSE Real Estate Index. This index has been chosen by the committee as it is considered the most appropriate benchmark against which to assess the relative performance of the company. To produce a 'fair value', each point is a 30 day average of the return.

The disclosure on directors' remuneration included in tables 1 and 2 above has been audited as required by Part 3 of Schedule 7A of the Companies Act 1985.

On behalf of the board
I. Yeatman
Chairman of the remuneration committee

11th March 2003

# Report of the independent auditors

To the shareholders of Derwent Valley Holdings plc

We have audited the financial statements of Derwent Valley Holdings plc for the year ended 31st December 2002 on pages 24 to 41. These financial statements have been prepared under the accounting policies set out on pages 28 and 29. We have also audited the information in the report on the directors' remuneration that is described as having been audited.

**Respective responsibilities of directors and auditors**
The directors' responsibilities for preparing the annual report, the report on directors' remuneration and the financial statements in accordance with applicable law and United Kingdom Accounting Standards are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements and the part of the report on directors' remuneration to be audited in accordance with relevant legal and regulatory requirements, United Kingdom Auditing Standards and the Listing Rules of the Financial Services Authority.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the report on directors' remuneration to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or the Listing Rules regarding directors' remuneration and transactions with the company and other members of the group is not disclosed.

We review whether the corporate governance statement reflects the group's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the group's corporate governance procedures or its risk and control procedures.

We read other information contained in the annual report and consider whether it is consistent with the audited financial statements. This other information comprises only the directors' report, the chairman's statement, the property review, the financial review and the unaudited part of the report on directors' remuneration. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Our report has been prepared pursuant to the requirements of the Companies Act 1985 and for no other purpose. No person is entitled to rely on this report unless such a person is a person entitled to rely upon this report by virtue of and for the purpose of the Companies Act 1985 or has been expressly authorised to do so by our prior written consent. Save as above, we do not accept responsibility for this report to any other person or for any other purpose and we hereby expressly disclaim any and all such liability.

**Basis of audit opinion**

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the report on directors' remuneration to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the report on directors' remuneration to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the report on directors' remuneration to be audited.

**Opinion**

In our opinion:

- the financial statements give a true and fair view of the group's and company's affairs as at 31st December 2002 and of the group's profit for the year then ended; and
- the financial statements and the part of the report on directors' remuneration to be audited have been properly prepared in accordance with the Companies Act 1985.

BDO Stoy Hayward
Chartered Accountants and Registered Auditors,
London.

11th March 2003

# Notice of annual general meeting

Notice is hereby given that the nineteenth annual general meeting of Derwent Valley Holdings plc will be held at The Westbury Hotel, Bond Street, London, W1A 4UH on 14th May 2003 at 10.30 a.m. for the following purposes:

**Ordinary business**

**1.** To receive the report of the directors and the accounts for the year ended 31st December 2002 and the auditors' report thereon;

**2.** To declare a final dividend of 7.35p per ordinary share for the year ended 31st December 2002;

**3.** To approve the report of the remuneration committee for the year ended 31st December 2002;

**4.** To re-elect Mr. J. C. Ivey as a director;

**5.** To re-elect Mr. J. D. Burns as a director;

**6.** To re-elect Mr C. J. Odom as a director;

**7.** To re-elect Mr. R. Farnes as a director;

**8.** To re-appoint BDO Stoy Hayward as auditors of the company to hold office from the conclusion of this meeting until the conclusion of the next general meeting at which accounts are laid before the company and to authorise the directors to determine their remuneration.

**Special business**

To consider and, if thought fit, pass the following resolutions, resolution 9 as an ordinary resolution and resolutions 10 and 11 as special resolutions.

**9.** That the directors be and they are hereby generally and unconditionally authorised to exercise all the powers of the company to allot relevant securities (within the meaning of Section 80 of the Companies Act 1985) up to an aggregate nominal amount of £886,016.20 provided that this authority shall expire at the conclusion of the next annual general meeting of the company after the passing of this resolution except that the company may before such expiry make an offer or agreement which would or might require relevant securities to be allotted after such expiry and the directors may allot relevant securities in pursuance of any such offer or agreement as if the authority conferred hereby had not expired;

**10.** That the directors be and they are hereby empowered pursuant to Section 95 of the Companies Act 1985 to allot equity securities (as defined in Section 94 of the said Act) for cash pursuant to the authority conferred upon them by the previous resolution as if Section 89(1) of the said Act did not apply to such allotment provided that the power conferred by this resolution shall be limited to:

**(i)** the allotment of equity securities in connection with a rights issue, open offer or any other pre-emptive offer in favour of ordinary shareholders where the equity securities respectively attributable to the interests of all such shareholders on a fixed record date are proportionate (as nearly as may be) to the respective numbers of ordinary shares held by them, subject to such exclusions or other arrangements as the directors may consider necessary or expedient to deal with fractional entitlements or legal or practical difficulties arising in any overseas territory, or by virtue of the requirements of any regulatory body or stock exchange or any other matter whatsoever; and

**(ii)** the allotment (otherwise than pursuant to sub-paragraph (i) above) of equity securities up to an aggregate nominal amount of £132,902.40,

and shall expire at the conclusion of the next annual general meeting of the company after the passing of this resolution except that the company may before the expiry of the power conferred by this resolution make an offer or agreement which would or might require equity securities to be allotted after such expiry and the directors may allot equity securities in pursuance of such offer or agreement as if the power conferred hereby had not expired;

**11.** That the company be and is hereby generally and unconditionally authorised to make market purchases (within the meaning of Section 163 (3) of the Companies Act 1985) of ordinary shares of 5p each in the capital of the company provided that:

**(i)** the maximum number of ordinary shares hereby authorised to be purchased is 5,316,097;

**(ii)** the minimum price (exclusive of expenses) which may be paid for any such ordinary share is 5p;

**(iii)** the maximum price (exclusive of expenses) at which any such ordinary share may be purchased is an amount equal to 105% of the average of the middle market prices shown in the quotations for an ordinary share as derived from the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the share is contracted to be purchased; and

**(iv)** the authority to purchase hereby conferred shall expire at the conclusion of the next annual general meeting of the company after the passing of this resolution save that the company may before such expiry enter into a contract of purchase under which such purchase may be completed or executed wholly or partly after the expiration of this authority and a purchase of shares may be made in pursuance of any such contract.

By order of the board
T. J. Kite, ACA
Secretary

25 Savile Row
London
W1S 2ER

9th April 2003

Notes:

The company, pursuant to Regulation 41 of the Uncertificated Securities Regulations 2001, specifies that only those shareholders registered in the register of members of the company as at 6 pm on 12th May 2003 shall be entitled to attend or vote at the aforesaid general meeting in respect of the number of shares registered in their name at that time. Changes to entries on the relevant register of securities after 6 pm on 12th May 2003 shall be disregarded in determining the rights of any person to attend or vote at the meeting. Every member entitled to attend and vote at the meeting may appoint a proxy or proxies to attend and, on a poll, vote instead of him. The proxy need not himself be a member. A form of appointment of a proxy is enclosed.

Copies of contracts of service relating to Messrs. J. D. Burns, S. P. Silver, C. J. Odom, N. Q. George and P. M. Williams will be available for inspection by members at the company's registered office during usual business hours on any weekday (public holidays excluded) from the date of this notice to the date of the annual general meeting. These documents will also be available for inspection during the annual general meeting and for at least fifteen minutes prior to the meeting. The register of directors' (and their families') interests in the ordinary shares of the company will also be available for inspection during the fifteen minutes prior to the meeting and throughout the meeting.

# Five year summary

| | **2002** **£m** | 2001 £m | 2000 £m | 1999 £m | 1998 £m |
|---|---|---|---|---|---|
| Group gross rental income | **46.5** | 46.9 | 39.5 | 29.8 | 28.7 |
| Net revenue from properties | **41.9** | 43.0 | 35.9 | 27.1 | 26.1 |
| Profit from property trading | **–** | – | – | 0.2 | – |
| Net interest | **18.5** | 19.2 | 19.0 | 11.8 | 12.8 |
| Adjusted profit before taxation | **17.4** | 17.9 | 11.7 | 11.5 | 10.3 |
| (Loss)/profit on disposal of investments | **(2.0)** | 3.8 | – | 5.1 | 0.3 |
| Profit before taxation | **15.4** | 21.7 | 11.7 | 16.6 | 10.6 |
| | | | | | |
| (Deficit)/surplus on revaluation of investment properties | **(29.3)** | 68.3 | 81.9 | 53.3 | 46.7 |
| | | | | | |
| Investment property | **831.9** | 833.5 | 770.4 | 604.1 | 471.7 |
| Net borrowings | **296.8** | 271.0 | 283.4 | 209.3 | 143.3 |
| Net assets | **512.0** | 533.7 | 462.3 | 376.5 | 314.0 |
| | | | | | |
| Net cash inflow from operating activities less interest | **23.5** | 15.2 | 14.8 | 13.1 | 12.0 |
| Acquisitions | **15.9** | 57.3 | 98.3 | 101.7 | 117.4 |
| Other capital expenditure | **35.0** | 38.6 | 29.8 | 16.9 | 15.2 |
| Disposals | **16.9** | 104.5 | 46.6 | 45.4 | 18.2 |
| | | | | | |
| Adjusted earnings per share (p) | **25.50** | 27.73 | 16.57 | 17.50 | 14.15 |
| Dividend per share (p) | **10.40** | 9.35 | 8.50 | 7.70 | 7.20 |
| Net assets per share (p) | **963** | 1004 | 870 | 709 | 593 |
| Adjusted net assets per share (p) | **982** | 1020 | 884 | 720 | 603 |
| Total return (%) | **(2.7)** | 16.4 | 24.0 | 20.7 | 24.0 |
| Gearing – Balance sheet (%) | **58.0** | 50.8 | 61.3 | 55.6 | 45.6 |
| – Profit and loss | **1.96** | 1.95 | 1.63 | 1.97 | 1.83 |

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# Financial calendar

| | |
|---|---|
| Annual general meeting | 14th May 2003 |
| Payment of 2002 final dividend | 9th June 2003 |
| Announcement of 2003 interim results | September 2003 |
| Payment of 2003 interim dividend | November 2003 |
| Announcement of 2003 preliminary results | March 2004 |
| Payment of debenture interest | 31st January &<br>31st July |

# Advisers

Auditors
BDO Stoy Hayward

Solicitors
Slaughter and May

Stockbrokers
UBS Warburg

Clearing bankers
HSBC Bank plc

Registrars
Lloyds TSB Registrars

Debenture stock trustee
Royal Exchange Trust Company Limited

DERWENT VALLEY HOLDINGS PLC
Registered office
25 Savile Row
London W1S 2ER
Tel 020 7659 3000
Fax 020 7659 3100
www.derwentvalley.co.uk
Registered No 1819699