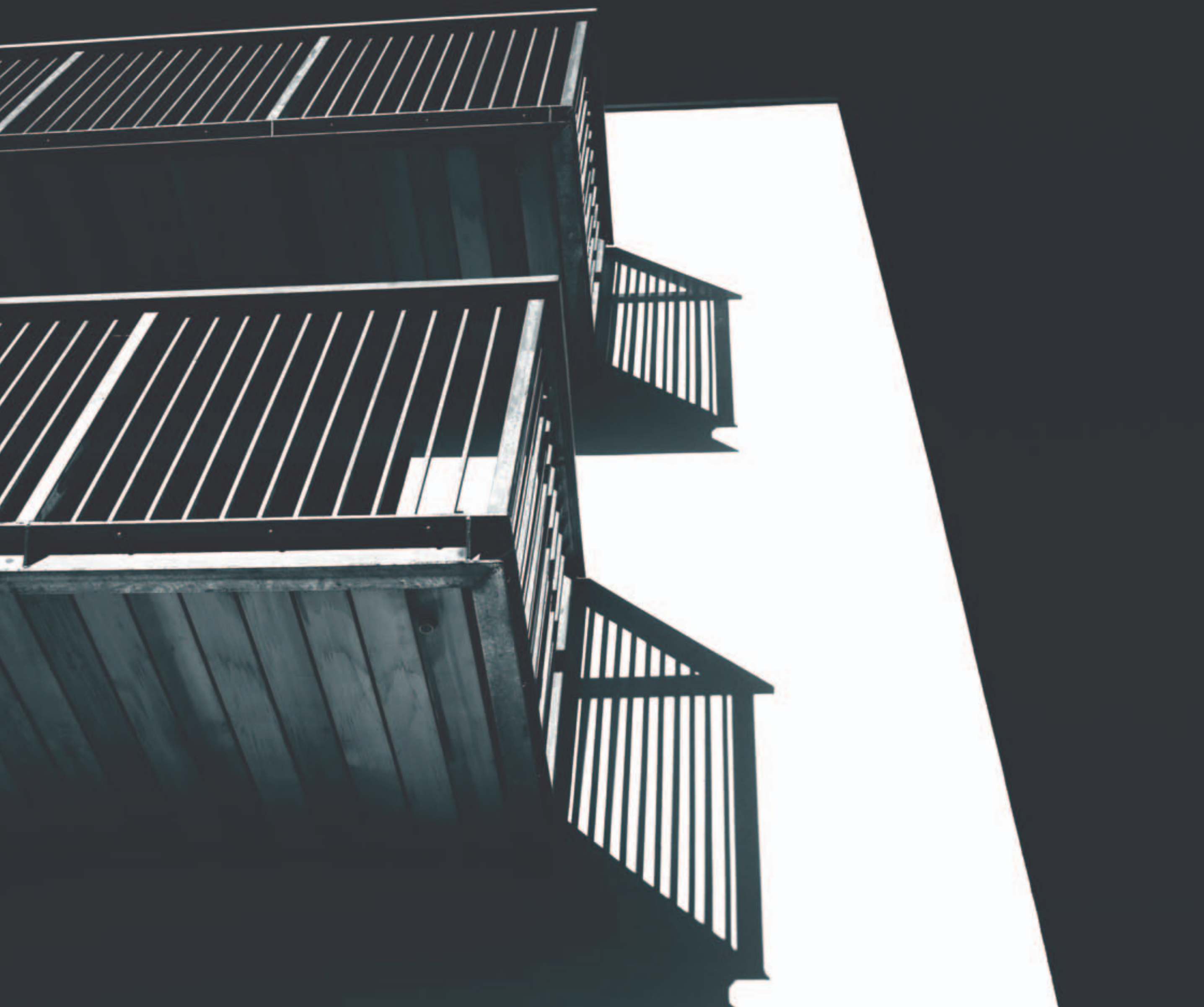
Grainger plc annual review for the year ended 30 September 2008

grainger facts



ACHIEVEMENTS OF THE YEAR

At Grainger, our dedicated management and staff have worked diligently in the very challenging conditions which existed during the year. As a result of these efforts, we are pleased to count the following amongst our achievements:

- ★ Operating profit up 19.1% to £106m (2007: £89m) before valuation and goodwill movements as a result of increased net rents and management fees
- ★ Sales from core and retirement solutions portfolios up 15% to £168m (30 September 2007: £146m)
- ★ New bank financing raised totalling circa. £228m
- ★ Cash conservation, by reducing property spend and overheads and increasing sales
- ★ Planning permission obtained for 1,550 new homes and 100,000 sq. m. of commercial space at Newlands Common, West Waterlooville
- ★ Successful tender offer for German residential company Francono Rhein-Main AG for €41.4m (£32.6m) creating critical mass in Germany

Grainger plc is the UK's largest listed residential landlord...

UNIQUE
expertise and perspective

Grainger plc is the UK's largest listed residential landlord with approximately £2.3bn of property assets and £3.0bn of assets under management. We specialise in owning, developing, managing, selling and delivering sustainable value from residential property.

We have a unique blend of expertise gained from owning and managing properties in local communities for many years. Our wealth of experience is invaluable in our task to manage the business through this challenging time.

Our strategy

Our long-term strategy remains unchanged. At our core, we have an irreplaceable portfolio of regulated properties, which generates regular cash flow through sales following natural vacancies. Our properties have continued to be desirable as they fall in an affordable price bracket and provide purchasers with refurbishment opportunities. It is also possible to sell these properties tenanted making them attractive liquid assets. We use our skills and experience of the market to ensure we sell to deliver the best possible value.

Grainger's Bridgewater business is also an industry leader in home reversion plans, which offer equity release for the elderly. Bridgewater is the first home reversion provider to be awarded the 'Best Home Reversion Provider' for three years in a row at the prestigious Mortgage Solutions Equity Release Awards. Grainger has an overall market share of some 35%. We are constantly broadening our portfolio of products and properties in this area, to include other solutions for retirement living, recognising a major area of growth over the coming years.

Our development business gives us further insight into the residential property market. We take a long-term approach where we can see strategic land opportunities. More recently we have recognised the benefits of working with partners to deliver large, mixed use schemes.

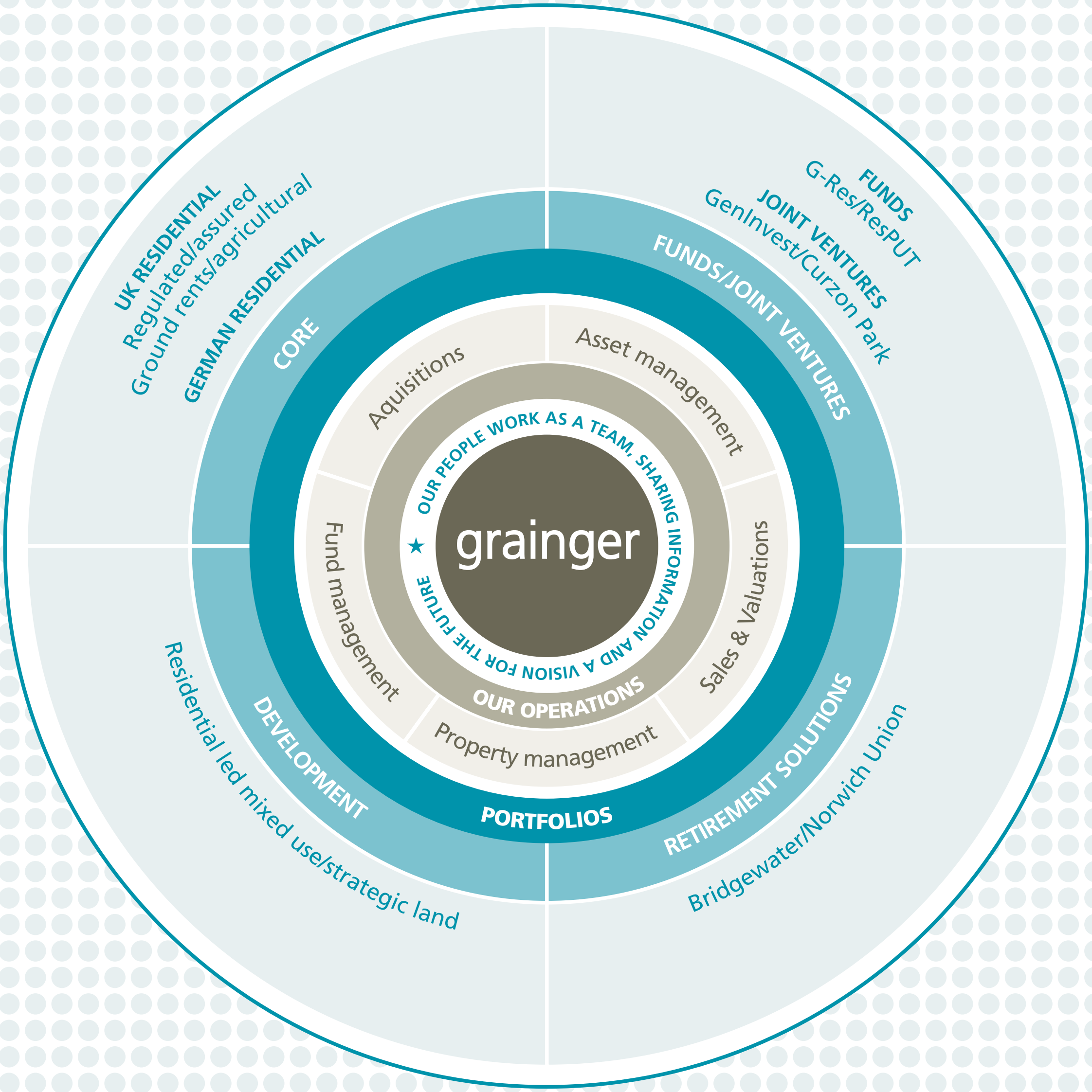
Over the last few years we have capitalised on our strengths and skills in the UK to enter the German residential market. This year we achieved critical mass of over €500m of property following the successful acquisition of Francono Rhein-Main AG. We have utilised those same abilities to launch and become fund, asset and property manager of G:res1, a residential property fund in which Grainger co-invests. These diversifications have spread our risk and reduced our dependency on the UK residential market. When appropriate opportunities arise, we will continue to leverage our capabilities.

Our aim is to maintain and consolidate our position as the UK's leading quoted residential property company. To do this we aim, over the long term to:

- provide superior risk-adjusted returns;
- maximise the efficiency of our capital structure by introducing third-party equity and debt through residential property funds;
- enter new residential sectors where we can use our management skills and resources to build large portfolios;
- diversify income streams to include fund management fees alongside co-investment growth;
- continue to build on our unique position as a long-term holder, asset manager, trader and developer of residential property;
- use our skills and property network reputation to integrate developing, managing and funding; and
- encourage and capitalise on the growing recognition of residential property as an investment class.

These aims are underpinned by our group-wide ethical way of doing business. This includes commitment to integrity in all business relationships, employee development, tenant care, environmental responsibility and community service.

In the short to medium term our plans for growth will be undoubtedly dampened by the economic climate. Our focus is fundamentally on managing the business in a prudent way, as we have done through previous downturns in the cycle. In practice this means focusing our efforts on maximising cash flow and delivering covenant compliance.



INTEGRATED
asset base and interests

CHAIRMAN'S STATEMENT

Despite the turmoil in the financial markets over the last 12 months and its inevitable overspill into the wider economy, I can report that our core business has continued to perform. In particular, sales of residential property, the heart of our activities, have shown a year-on-year increase in proceeds received of 15%.

However, Grainger is not, of course, immune from the general economic problems and this is reflected in decreased trading margins, increased funding costs and falls in net asset value from asset writedowns.

Current main objectives

In our interim management statement in August we set out our three main objectives for the anticipated difficult period ahead. These are:

- to maximise sales revenue;
- to reduce purchases of replacement stock; and
- to cut our overhead base.

Progress on these to date

- sales of residential property amounted to £168m compared to £146m in 2007;
- in the period April to September 2008 we acquired just £27m of UK property assets compared to £96m in the first half of the year and to £403m in the whole of 2007; and
- our overhead costs are 10% lower than 2007.

In addition, we will maintain an overriding focus on the protection and enhancement of our revenue, cash maximisation, financial stability and compliance with our banking covenants until market conditions improve.

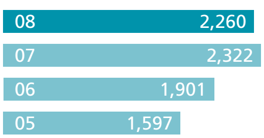
Results

As with all real estate companies our results for the year have been significantly affected by valuation movements. We have therefore analysed our income statement into trading activities and valuation and other mark-to-market adjustments in note 3 to the accounts. This analysis enables us to present more meaningful comparisons of our core operations year-on-year.

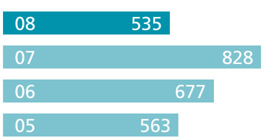
Profit before tax has decreased by £190m from a profit of £78m to a loss of £112m, of which £177m comes from valuation deficits, goodwill impairment and mark-to-market adjustments. Adjusting for these, our result for the year would be a profit before tax of £12m compared to £25m on the same basis last year, the fall resulting largely from increased funding costs.

Operating profit has increased by 19.1% from £89m to £106m (before valuation writeoffs and goodwill impairment) reflecting increases in net rents from our enlarged UK and German portfolios and in management fees from our fund management activities. Despite the market conditions our trading profits are relatively unchanged.

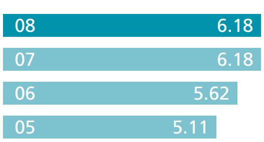
Gross property assets (£m)



Gross NAV per share (pence)



Dividends per share (pence)



Gross net asset value per share ('Gross NAV') has decreased by 35% to 535p from 828p and this fall is also reflected in our other NAV measures: triple net asset value ('NNNAV') down 37% to 385p from 613p and base case Grainger NAV down 29% to 520p from 732p. The major factors behind the decrease have been the fall in vacant possession value of our properties and an increase in the discount applied to those values to calculate market values which are then used for NAV purposes. Details of the calculation of the NAV measures are provided in the financial review.

We are maintaining our full year dividend for shareholders in Grainger plc at the same level as last year. Thus the board is recommending a final dividend of 3.91p which together with the interim dividend of 2.27p per share paid on 4 July 2008 will produce a total dividend for the year of 6.18p per share. If approved the final dividend will be paid on 16 February 2009 to shareholders on the register on 9 January 2009.

Strategy

In the short to medium term, management's entire focus is on managing the business in a prudent way, ensuring that we steer the business through this cycle by maximising cash flow and remaining covenant compliant.

In the long term, the group's strategic objective is to maintain and consolidate its position as the UK's leading quoted residential company. Underpinning this objective are these key features:

- the group has a unique, diversified portfolio built up over many years;
- supporting this portfolio is our core property management services division. This not only delivers a personal and caring service to our tenants but also enables us to expand and diversify the residential activities we are able to supply;
- in turn, in addition to our market leadership in the ownership of properties subject to regulated tenancies we are leaders in the fields of home reversions and residential fund management;
- we now have additional income streams not reliant on the direct ownership of property and at low incremental cost. We have widened our risk and return exposure by entering the German residential market and curtailing our involvement in residential development; and
- when the market bottoms out, we believe attractive new opportunities will present themselves, and our objective is to be in a position to take advantage of these.

Our core portfolio is unique and diverse in nature. We are not exposed to new build properties (particularly city centre flats which have been most adversely affected by recent price falls) and our relatively low average value, un-refurbished properties tend to maintain their demand and value better than many other sectors. This is reflected in our year end valuation which showed a 12-month fall of 7.6%, compared to national indices from the Halifax and Nationwide showing a fall of 12.4%. We also have the ability in many of our portfolios to make investment sales (i.e. sales with a tenant in possession) and this is invaluable in increasing liquidity and generating cash.

Robin Broadhurst Chairman

CHAIRMAN'S STATEMENT

Board changes

In July, we welcomed Baroness Margaret Ford of Cunninghame as a non-executive director. Currently a managing director in the Royal Bank of Canada's Capital Markets Group, her extensive experience as Chairman of English Partnerships, the Government's Regeneration Agency, and her wide ranging knowledge of housing and regeneration in both the public and private sectors will be of great assistance to the board.

I must also take this opportunity to pay tribute to Stephen Dickinson who will step down from the board at the company's Annual General Meeting on 10 February 2009. Stephen joined Grainger in 1974 and was chief executive until October 2002. During that time he was unquestionably the face of Grainger and presided over an exciting period of growth and consolidation which included flotation of the group in 1983 when it had assets of just £18m. Stephen laid the foundations that enabled the business to progress and develop and his experience of the residential market, as well as his unique style, will be greatly missed. On behalf of the board I thank him for his long service and contribution.

Outlook

It is difficult to recall a period of such economic uncertainty. The impact on the housing market in the UK has been well documented and it is inevitable that funding constraints and forecasted lack of economic growth will further depress the market over the coming 12 months.

However, the last year has demonstrated the continuing resilience of Grainger's portfolio and it is worth repeating that our sales proceeds were up 15% on last year, showing its inherent liquidity and ability to generate cash.

The coming year will present many challenges and in response we will continue to operate as we have through the latter part of 2008 – maximising sales revenue, reducing property spend and cutting back on overhead. We are under no illusions as to how difficult these tasks will be but are confident that the irreplaceable and diverse nature of our core portfolio, the range of activity and expertise within the business and our experience of managing the business through previous downturns will stand us in good stead.

I would like to take this opportunity to thank everyone at Grainger for the drive and commitment they have shown in extremely testing times.

Robin Broadhurst Chairman 16 December 2008

DIVERSE operational platform

In the UK we own:

- 7,300 regulated properties
- 6,200 retirement properties / interests, including home reversions
- £142m of development assets (including joint ventures)
- £117m co-investment shares in residential funds / investments

In continental Europe we own:

- 6,900 residential units in Germany

CHIEF EXECUTIVE'S REVIEW

Market review

This year has seen significant falls in both the value and volume of residential transactions as indicated by the fact that mortgage approvals for September 2008 were down 57% compared to September 2007.

Whilst we are seeing a correction to house prices, the market situation has been considerably worsened by the lack of appropriate funding for house buying with many of the usual sources either stopping lending altogether or offering terms which are unacceptable.

Without question, the era of high level loan to value home loans based on excessive multiples of earnings has ended. Lenders are requiring higher deposits and better earnings coverage. The market will inevitably take time to adjust to this new environment.

However, we believe that other factors must also be considered, in particular imbalances between supply and demand and levels of affordability.

The most stark example of imbalance currently exists in the oversupply of one or two-bedroom city centre apartments primarily built for the buy to let market. This sector, to which Grainger has virtually no exposure, has shown falls of as much as 50% in some areas. Overriding this, however, are the broader statistics. The Government has stated that three million new homes will be needed by 2020, two million of them by 2016. This does not sit comfortably with estimates of the current level of supply, estimated to be well below 100,000 new units in 2009. Inevitably at some point in the future this will once again produce upward pressure on prices.

To help alleviate this situation we have been strong advocates for policy action to promote and professionalise the private rented sector ('PRS'). The recent Rugg Review ('The Private Rented Sector; its contribution and potential') showed that the Government acknowledges the importance of the PRS but the review's focus was more on the regulation and potential licensing of landlords rather than on the need for further investment. Without this there will be no real contribution towards increasing housing supply and improving quality for those wishing to enter this sector.

We consider that, with suitable fiscal incentives and planning policies and practices to encourage build to let schemes, the PRS would not only help alleviate the supply problem but would also present Grainger, as the UK's largest listed residential owner, with significant business opportunities.

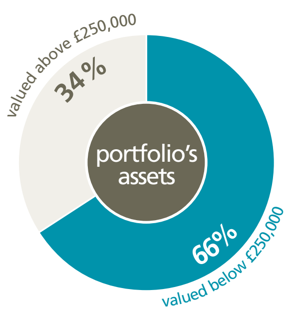
The second factor is that of affordability. Two recent significant cuts have put base rates down to 2.0%. It is too early to say whether this will act as a significant stimulus to the housing market but at the very least it will encourage potential acquirers at the margin to purchase.

We have positioned the business so that we can manage through the current difficulties by maintaining our focus on our key strategic priorities; cash generation from our portfolios, reduction in property and development spend and overhead reduction. We intend to ensure that we are in a strong position to take advantage of opportunities when the market stabilises and starts to show signs of recovery.

Rupert Dickinson Chief executive

Average vacant possession value (£)

08	190,000
07	205,000
06	188,000
05	173,000



Risk review

The major risks to Grainger's business are macroeconomic:

Housing market – A further severe and rapid downturn in UK house prices and stagnation in the market through lack of mortgage finance and/or willingness to acquire properties.

Financing – Significant increases in borrowing costs and/or a lack of or reduction in finance available to Grainger.

Housing market Our unique residential portfolio has been assembled over a significant period of time. Even after recent falls, its current market value is some £378m greater than cost. Furthermore, much of the portfolio is reversionary and the value that we will obtain by selling on vacancy currently exceeds market value by £658m (the 'reversionary surplus').

Our portfolio is inherently defensive in times of market slowdown. It is geographically diverse and not overly exposed to cluster risk. The majority of our properties are un-modernised and of relatively low average value – the average vacant possession at 30 September 2008 was £190,000 (2007: £205,000) and 66% of our portfolio's assets are valued below £250,000. This level of affordability and the opportunity to maintain or increase value through refurbishment are key elements of continued or sustained demand when they become available for sale. The nature of many of our tenancies are such that we can sell them without waiting for vacancy and still realise a profit. These 'investment' sales are a useful way to produce additional cash flows. As we have demonstrated through the 15% increase in sales during our last financial year, we are able to sell assets even in difficult market conditions.

Operationally we manage our exposure to house price inflation by constant reviews of the portfolio to ensure that we crystallise gains and maximise returns at the right time. The fact that many of our properties are acquired at a significant discount to vacant possession values provides us with an inbuilt buffer against value falls and also considerable pricing flexibility. We are also diversifying our income streams (for example, fund management income) and our geographic presence to spread risk.

Financing Our exposure to adverse interest rate movements is limited by adopting a prudent hedging policy. At 30 September 85% of group debt was hedged through being fixed or subject to caps or swaps. Debt subject to caps or which is floating can benefit from lower rates, provided they are reflected in LIBOR. The hedging instruments used and the fixed rate debt have a variety of maturity dates to give protection over the medium term.

The cost of debt is also dependent upon the lending margins charged by banks. This has increased significantly over the course of this year although this has not yet been reflected in our costs. Our blended margin is still competitive at 77 bps at 30 September.

At 30 September, the group had headroom of £370m, £303m of which was from the UK core facility. This headroom represents 76% of the first significant debt maturity we have – a facility of £400m due in June 2010. The average maturity of our debt is 4.5 years.

We guard against lack of liquidity by constantly recycling capital. The business has produced £213m of cash from operating activities, including sales of investment property, the majority of which has been generated by the core and retirement solutions businesses. This compares to a cash interest cost of £92m.

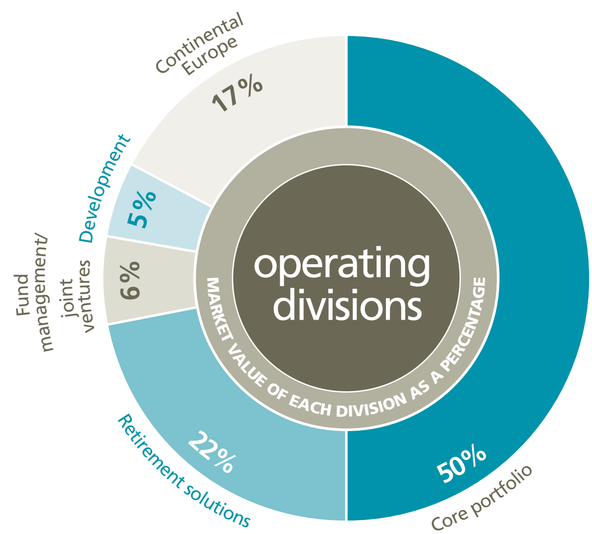
Liquidity and debt cost can also be threatened by covenant breach. Details of our covenant structure and compliance are given in the financial review. We constantly monitor current and prospective covenant compliance on all of our facilities and take pre-emptive action where necessary, for example asset sales, to ensure that no breaches occur.

CHIEF EXECUTIVE'S REVIEW

OPERATING REVIEW

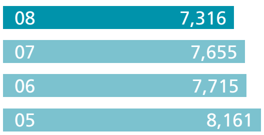
At Grainger, we pride ourselves on our integrated approach. Our skills can be used across our different divisions, bringing them together and creating a group where the whole is greater than the sum of the parts. By sharing our experiences and ideas, we can maximise the value from our assets and of our people. Our operating divisions are supported by our property management division which has over 140 staff in our seven UK and one German office.

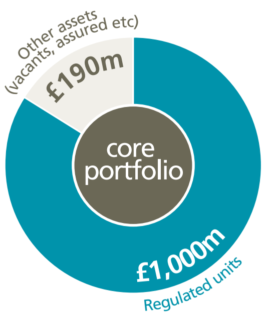
Our main operating divisions and the market value of each as a percentage of our total property and investment assets are:



Core portfolio	Primarily our portfolio of properties subject to regulated tenancies
Retirement solutions	Our interest in home reversion and retirement related assets
Fund management and investments in residential joint ventures	Investments in managed funds (G:res1 and Schroders) and in Grainger GenInvest
Development	Focused on relatively large scale residential or residential led mixed use developments
Continental Europe	Principally investment in German residential portfolios

Regulated units owned





Core portfolio

	2008	2007
Regulated units owned	**7,316**	7,655
Market value	**£1,000m**	£1,221m
Vacant possession value	**£1,399m**	£1,571m
Other assets (vacants, assured etc)	**803**	882
Market value	**£190m**	£196m
Vacant possession value	**£216m**	£220m

Despite the difficult market conditions, the liquidity of our core portfolio remained strong and sales proceeds have increased by 10.3% to £141m from £128m. This has been achieved through a concerted effort to maintain volumes and by careful selection of suitable properties for investment sales (these occur when a property is sold with a tenant in place, as opposed to normal sales which occur on vacancy). The number of units sold was 817 of which 302 were investment sales (2007: 86 investment sales out of a total of 661).

The average value achieved on normal sales has remained static at £193,000 and over the course of the whole year those sales achieved a slight fall of 0.7% from September 2007 vacant possession values, an indicator of the prudence of our valuation process and the resilience of the portfolio. Margins on normal sales have fallen from 50.7% to 45.9%.

Proceeds and profit from investment sales amounted to £41m and £17m respectively (2007: £17m and £10m).

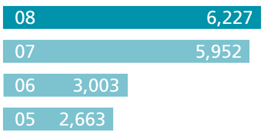
In line with our stated intentions in our interim statement in May we significantly reduced acquisitions in this portfolio in the latter part of the year. In total we acquired 403 units for £80m (2007: 863 units for £151m) of which only 72 units costing £9.5m were purchased in the second half of the year.

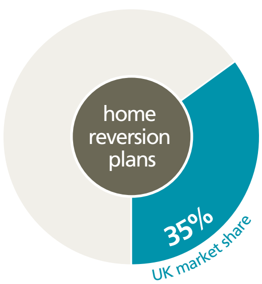
Operating contribution from this division (comprising profits on sale of trading and investment assets together with net rents and other income, after deducting divisional overheads) amounted to £83m (2007: £81m).

CHIEF EXECUTIVE'S REVIEW

OPERATING REVIEW

Interest in residential units (number)





Retirement solutions

	2008	2007
Interest in residential units (number)	**6,227**	5,952
Market value	**£521m**	£542m
Vacant possession value	**£754m**	£779m

This operating division has shown a pleasing level of profit growth during the year, reflecting the increasing maturity of the portfolio. We have sold interests in 185 assets in the retirement solutions portfolio (including CHARM) for £27.2m and recorded a profit on sale of £10.9m (2007: 146 assets, £18.5m proceeds, £7.7m profit).

As with the core portfolio, we have taken steps to reduce acquisitions although the long lead time in the home reversion process means that the results of this will not be seen fully until the financial year ending September 2009. During the year ended 30 September 2008, we acquired 460 assets for £43m, compared to 2,889 assets for £252m in 2007. The performance of the two major acquisitions made in 2007 has been in line with expectations: CHARM, where realisations have been as expected and The Capital Appreciation Trust (Isle of Man) plc ('CAT') where we have reduced vacancy rates from 25% to 6% since acquisition.

Operating contribution from this division (on the same basis as the core portfolio but excluding the CHARM revaluation) amounted to £16m (2007: £9m).

For the third consecutive year, our Bridgewater business has been named as Home Reversion Provider of the Year by Mortgage Solutions.

Grainger share (£m)

Fund management and residential investments

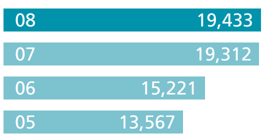
	Holding %	Gross asset value £m	Net asset value £m	Grainger share £m
Grainger GenInvest*	50.0	298	62	65
G:res1	21.6	401	159	35
Schroders	23.6	73	73	17
Total 2008		**772**	**294**	**117**
Total 2007		911	443	161

* net asset value for Grainger GenInvest is shown after adjusting for the mezzanine loan provided by Grainger of £67m

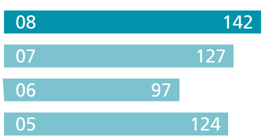
Fee income (£m)

The value of our investments in these vehicles has been hit by falls in asset values. Consequently, the contribution from this division (comprising share of profits, dividends received, fee income and share of revaluation movements) has fallen to a loss of £50m compared to a gain of £40m in 2007, largely due to our share of revaluation movements amounting to a loss of £48.3m, despite fee income for the year totalling £6.3m. All of the debt in these vehicles is non-recourse to Grainger plc.

UK residential units managed



Market value of development portfolios including share of joint ventures (£m)



Property services

This division carries out the asset and day-to-day property management of our core portfolios and those of our co-invested funds.

	2008	2007
UK residential units managed	**19,433**	19,312
Gross rent roll	**£78m**	£69m
Gross property expenditure	**£19m**	£18m

Rents have increased primarily because of the acquisition of the Tilt portfolio late in 2007.

Development

	2008	2007
Market value of development portfolios (including share of joint ventures)	**£142m**	£127m
Estimate of completed development value	**£850m**	£809m
Of this, with planning consent	**£484m**	£324m
Committed cash expenditure	**£30m**	£57m

As previously announced, we have, in the light of prevailing market conditions, curtailed the activities of this division in order to focus on cash conservation. We are, however, moving forward on public/private partnerships and achieving improved planning status for our holdings at the appropriate pace. Construction work has continued on 150 private units at Hornsey Road in Islington. The Council office building has been handed over and these apartments will become available for either sale or rent early in 2009.

Since the year end we have received a resolution to grant planning permission at our site at Wards Corner, North London for 197 residential units and a range of retail units. We have also completed the disposal of our development site in Barnsbury, North London, for £19m in early December.

CHIEF EXECUTIVE'S REVIEW

OPERATING REVIEW

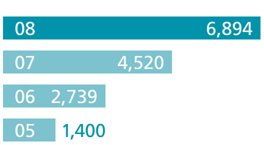
The current status of our other major projects is set out below:

Project	Description	Status
Wholly owned		
Hornsey Road, Islington	200 residential units, community building	Construction almost complete
Newlands Common	100,000 sq. m. commercial, 1,550 new homes and 1,000 reserve	Outline planning consent granted for Phase 1
Macaulay Road, Clapham	97 residential units, 30,000 sq. ft. retail	Consent granted and demolition complete. On hold
Wards Corner	197 residential units with a range of retail units, including provision for the Seven Sisters market	Development agreement with Haringey Council. Resolution to grant planning permission achieved 17 November 2008
Gateshead College	245 residential units	Planning appeal submitted end of November 2008, decision pending
Newbury	330 residential units, 50,000 sq. ft. retail	Preferred developer status, conditional development agreement expected Summer 2009
Joint ventures		
Curzon Park	400,000 sq. ft. residential, 800,000 sq. ft. office, 20,000 sq. ft. retail, 118-bed hotel	Mixed use joint venture with Development Securities. Outline planning consent granted
Hammersmith	290 residential units, 5,202 sq. m. commercial space, 11,000 sq. m. council offices, a public square, a bridge linking Hammersmith with the river, and 200 car parking spaces	Awarded Development Agreement in partnership with Helical Bar. Working up a scheme in preparation for submission of a planning application

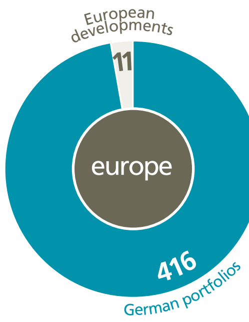
The operating loss from this business in the year (comprising trading profits/(losses), net of divisional overheads and asset writedowns) amounted to £12m (2007: profit of £4m).

Continental Europe

Residential units owned



	2008	2007
Residential units owned	**6,894**	4,520
Market value	**£417.5m**	£241.7m
Gross rent	**£21.4m**	£9.8m
Gross annual running rent	**£27.8m**	£15.0m



The major activity in the year was the acquisition of Francono Rhein-Main AG ('FRM') for £32.6m. This lifted our German portfolio to a critical mass of some 7,289 units (including 395 commercial). Our current focus is to integrate FRM with our existing business and to improve returns through rent reviews, void reductions and cost savings. In addition, in August we appointed Peter Brock formerly Head of Asset Management of listed German real estate company Vivacon AG, as managing director of Grainger Deutschland GmbH, our German advisory business.

The operating contribution from our German portfolio (comprising profits on sale of investment assets together with net rents and other income after deducting divisional overheads) in the year was £11.4m. The revaluation movement on the portfolio, however, resulted in asset writedowns of £8.6m. The net rental yield is running at 5.1% (2007: 4.5%). External debt amounts to £285m and is non-recourse to Grainger plc.

Our other European interest relates to a joint venture company in which we have a 50% stake and which owns a development site in Zizkov, Prague. Our original stake was 81.6% and we have sold this down to realise a profit in the year of £3.5m. Our investment in this joint venture, with land at market value, amounts to £10.6m and the development is going through the planning process.

Prospects

Since the year end we have continued to sell properties. As at 30 November, we had completed, exchanged contracts on or had put in solicitors hands normal sales amounting to £32.0m, 0.1% above September 2008 vacant possession values.

As well as our ongoing programme of selling properties on vacancy we have identified circa. £100m of additional properties for sale from our core and development portfolios although this is obviously dependent upon both market conditions and availability of funding. We continue to examine opportunities to bring in third-party equity through the establishment of joint ventures or other structures. Also, since the year end we have taken action to reduce our overhead running rate by a further 10%.

Our commitment is to continue to manage the business in a prudent way through these turbulent market conditions. Our portfolio is uniquely resilient, with its mix of property types, tenures and excellent liquidity.

It is held for the long term and this will help us through the short and medium-term corrections that are taking place. Real estate is a cyclical activity and we are confident that we have in place the assets, people and management platform that will ensure we are strongly positioned to take advantage of the opportunities that will undoubtedly arise.

Rupert Dickinson Chief executive 16 December 2008

LEADING market positions

- ★ Unique regulated portfolio, with market value of £1bn
- ★ 35% market share of new home reversions
- ★ Fund, asset and property manager to G:res1

FINANCIAL REVIEW

Andrew Cunningham
Deputy chief executive
and finance director

We believe it is essential to continue to be transparent in this uncertain economic climate. Inevitably, our net asset values have fallen, and we set out over the coming pages, the main factors that affected this. We are pleased to give details of the 19% increase in operating profit before valuation and goodwill adjustments, and sales from our core and retirement solutions businesses up 15%. We have also increased the detail in the disclosure of our debt covenants, including how we manage these, with a focus on LTV levels and interest cover, which can be found on page 24.

Performance overview Our key performance indicators are:

	2008	2007
Gross net asset value per share (pence)	**535p**	828p
Operating profit before valuation and goodwill adjustments	**£106.0m**	£89.0m
Return on capital employed (1)	**(11.4%)**	12.1%

	1 year	5 year	10 year
Return on shareholder equity (2)	(36.1%)	8.2%	15.3%

1 Profit before financing costs adjusted for revaluation movements as a percentage of opening gross capital

2 Growth in NNNAV plus dividends paid per share as a percentage of opening NNNAV on an annualised basis

FINANCIAL REVIEW

Most of our properties are held as trading stock and are therefore shown in the statutory balance sheet at the lower of cost and net realisable value. This does not reflect the true worth of the assets and so we set out below a summary of our net assets with the properties restated at market value.

	Statutory balance sheet £m	Adjustments to market value, deferred tax and derivatives £m	Gross NAV balance sheet £m	Contingent tax £m	Derivatives £m	Triple NAV balance sheet £m
Properties	1,883	377	2,260	–	–	2,260
Investments/other assets	145	–	145	–	–	145
Goodwill	8	–	8	–	–	8
Cash	43	–	43	–	–	43
Total assets	2,079	377	2,456	–	–	2,456
Borrowings etc	(1,663)	2	(1,661)	–	(11)	(1,672)
Other net liabilities	(107)	–	(107)	–	–	(107)
Provisions/deferred tax	(79)	79	–	(184)	3	(181)
Total liabilities	(1,849)	81	(1,768)	(184)	(8)	(1,960)
Net assets	230	458	688	(184)	(8)	496
2008 net assets per share (pence)	**178**	**357**	**535**	**(144)**	**(6)**	**385**
2007 net assets per share (pence)	251	577	828	(221)	6	613

The European Public Real Estate Association ('EPRA') Best Practices Committee has recommended the calculation and use of a diluted EPRA NAV and a diluted EPRA Net Net Net Assets Value ('NNNAV'). The definitions of these measures are consistent with Gross NAV and Triple NAV as described and shown in the table above.

This definition of Gross NAV requires us to take out any adjustments for deferred tax and changes in the fair value of derivatives as calculated under IFRS. NNNAV requires certain of these adjustments to be reinstated and, in addition, a deduction is made for contingent tax which is calculated by applying the expected rate of tax to the full inherent gains at the balance sheet date.

Market value analysis of property assets

	Shown as stock at cost £m	Market value adjustment £m	Market value £m	Investment property/ financial interest in property at value £m	Total £m
Residential	1,009	378	1,387	741	2,128
Development	133	(1)	132	–	132
Total September 2008	**1,142**	**377**	**1,519**	**741**	**2,260**
Total September 2007	1,069	643	1,712	610	2,322

Net asset value Measurements of net asset value are key performance indicators for the group. We set out three measurements to better enable shareholders to compare our performance year-on-year and with our peers, whilst reflecting the unique nature of our business:

Gross net assets per share down 35% to 535p from 828p (market value of net assets per share before deduction for deferred tax on property assets and before adjustments for fair value of derivatives).

Triple net assets per share NNNAV down 37% to 385p from 613p (gross NAV per share adjusted for deferred tax on revaluation gains and for mark-to-market adjustments).

Grainger NAV down 29% to 520p from 732p (NNNAV adjusted for the discounted and taxed reversionary surplus in our long-term regulated and home reversion portfolios).

The major movement in NAV in the year comes from the revaluation of our residential assets. Points worthy of note are:

i) Core and home reversions portfolios including CHARM (Churches Housing Assistance for Retired Ministry). The vacant possession values of these portfolios have fallen by approximately 8% over the year. This accounted for a fall of £134.0m in NAV, of which £35.5m has been taken through the income statement.

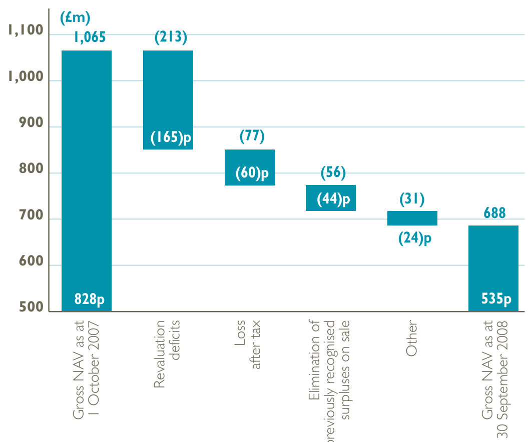
ii) Market value percentages. The market value of our UK residential portfolios is arrived at by applying a discount to vacant possession values. For our home reversion portfolios this discount is actuarially calculated based upon the age of the tenant. For the regulated and other UK residential portfolios the discount is based upon market experience. In last year's valuation, regulated assets were valued at 77.5% of vacant possession value. This year, a geographic weighting has been applied to better reflect yields and local market conditions with the overall result that these assets have been valued at 71.3% of vacant possession value. Similar discount spreads have been applied to our other residential assets (e.g. assureds) and to the assets held in our joint ventures and associates. The increase in discount on our wholly owned assets has accounted for a fall of £97.1m in NAV, of which £3.6m is through the income statement.

iii) Residential joint ventures and associates. Valuation falls in these investments account for a fall of £48.3m in NAV, all of which has been taken through the income statement.

iv) German portfolios. The German residential market has not been subject to the severe downward price pressure in the UK and our portfolio has fallen by approximately 3.4% over the year resulting in a NAV fall of £8.6m, all through the income statement.

v) Development assets. In total we have made provisions of £19.2m against the market value of our development assets including investments in development joint ventures. The largest provisions are at Curzon Park £8.6m, Gateshead £4.8m and Kylins £2.1m. £9.2m has been taken through the income statement.

Gross net assets per share



Grainger net assets per share Reconciliation of NNNAV to Grainger NAV

	£m	Pence per share
NNNAV as at 30 September 2008	496	385
Discounted reversionary surplus	241	187
Tax thereon	(68)	(52)
Grainger NAV as at 30 September 2008	**669**	**520**

FINANCIAL REVIEW

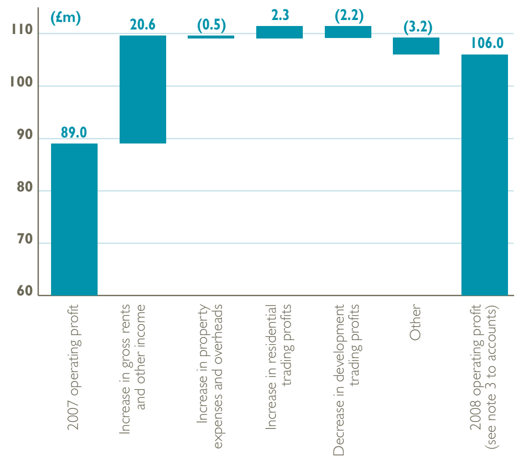
The major assumptions used in calculating the base case Grainger NAV are set out below:

- house price inflation taken as zero over the entire reversionary period;
- discount rate of 8.43% used to calculate the present value of the reversionary surplus (weighted average cost of capital +3%) (2007 discount rate: 9.38%);
- no discounting of contingent tax on the revaluation surpluses; and
- reversionary periods taken as 14 years for regulated properties and 10 years for home reversions.

Our website (www.graingerplc.co.uk) sets out how these assumptions may be varied and we show below some examples:

	No discount of deferred tax		Discounting deferred tax	
House price inflation per annum	Discount rate WACC + 3%	Discount rate WACC	Discount rate WACC +3%	Discount rate WACC
0%	520p	576p	612p	646p
4%	604p	695p	696p	766p
6%	662p	778p	754p	849p

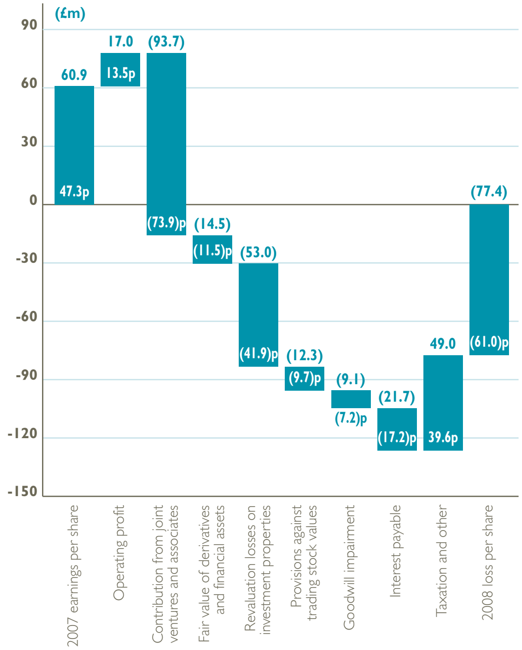
Financial performance in the year Operating profit before all revaluation movements, fair value and goodwill adjustments increased by 19.1% to £106.0m from £89.0m as shown below.



The major movement in operating profit comes from higher rents in both our UK and German residential portfolios in line with increases in the size of those portfolios. Residential portfolio profits have stayed relatively constant and, as anticipated, development profits have decreased along with the number of projects completed and/or sold in the year.

Overheads have fallen by 10.3% from £33.6m to £30.1m.

Earnings per share Basic earnings per share have decreased by 229% to a loss of 61.0p from earnings of 47.3p.



The major movements relate to revaluation and mark-to-market adjustments. In 2007, our joint ventures and associates contributed £41m, of which £39m related to revaluation gains. In 2008, these gains were reversed and a loss of £53m was recorded, of which £48m related to revaluation deficits. There is a further revaluation deficit of £43.1m (2007: gain of £9.9m) on Grainger's investment properties and net realisable value provisions on our trading stock of £12.3m. We have suffered a loss of £11.5m (2007: gain of £3.0m) on marking to market the fair value of our derivatives.

Interest and taxation Our net interest charge has increased by £24m from £65m to £89m. This reflects higher debt levels in the year (used for acquisitions in Germany and in home reversions) and higher underlying interest rate costs. On average, monthly debt levels have exceeded 2007 figures by £360m and as the majority of our debt is hedged through fixed rate loans or interest rate swaps, the high LIBOR and EURIBOR rates have not had a significant impact on the overall cost of our debt.

The income statement shows a tax credit at an effective rate of 31.0%, the major items affecting it being:

	£m
Group loss before tax	(112.1)
Tax credit at 29%	(32.5)
Adjustments:	
Permanent differences	4.7
Utilisation of capital losses	(10.6)
Other including prior period adjustments	3.7
Actual tax credit	(34.7)

FINANCIAL REVIEW

Financial resources The business has produced £213m of cash from its net rents and other income, the sales of property and other working capital movements net of overheads. The largest outflows relate to interest £92m and to residential property expenditure £178m, of which only £42m was made in the second half of the year. We spent a further £32.6m on the acquisition of FRM which had debt of £91m, and which has now been consolidated on the group balance sheet. Deterioration in the Sterling/Euro exchange rate increased overall group debt by £32m, although there is an equivalent increase in the value of Euro denominated assets.

At the year end, our net debt levels (before unamortised finance costs) stood at £1,621m (2007: £1,342m) and were 85% hedged (2007: 74%).

During the year, we increased our core borrowing facility by raising a new five-year facility of £228m. At the year end, the headroom on our core UK borrowings amounted to £303m and we had a further £30m committed facilities on our various Euro borrowings. Including cash balances and our overdraft facility amounting in total to £37m, total group headroom at 30 September 2008 was £370m. The average maturity of our debt is 4.5 years (2007: 5.4 years) and the first major repayment of £400m is due in June 2010.

Our all-in cost of debt in the year was 6.2% (2007: 6.1%) and our weighted average cost of capital was 5.43% (2007: 6.38%).

Covenants Our core facility has two covenants covering loan to value ('LTV') ratio and interest cover. Under the first, a LTV of 80% could lead to default of the agreement. At 70% LTV, purchasing restrictions apply. To a large extent the business is currently operating under the restrictions by cutting back on new acquisitions. LTV on the core facility at 30 September was 66% although this was reduced to 64% shortly after the year end by the early conversion of 78% of our convertible bond. We are able to take action to help keep the LTV ratio down, the main one being asset sales. We estimate that if we are able to maintain sales proceeds in 2009 at the same level as achieved in 2008 then UK asset values as used for covenant purposes will have to fall by circa. 24% in the year ended 30 September 2009 for us to reach 80% LTV.

Under the second covenant, our interest cost must be covered 1.25 times by net cash flow before interest. As at 30 September the ratio stood at 2.2 times (2007: 2.8 times). This covenant is calculated by reference to the previous 12 months' results and, given the cash inflows that we have already achieved to date, we are very confident that this covenant will be met at the next testing period in March 2009.

We maintain regular and constructive dialogue with our banking group and keep them fully informed of covenant status. Constant monitoring of these covenants ensures that we can take early and proactive measures, for example, asset sales, to prevent default levels being reached. This remains a key objective for the near and medium term.

Post balance sheet event Since the year end holders of £87.1m of our £112m 2014 convertible bond have accepted a cash payment of £35,000 per £100,000 nominal bond value to convert early. The effects of this early conversion have been to:

- issue 10.08m ordinary shares;
- eliminate £57m nominal of debt;
- increase net assets by £42.0m and decrease net assets per share by 1.6%; and
- reduce the LTV on our core facility to 64.1% from the figure of 66.4% at the year end.

In the year to 30 September 2009, there will be a one-off charge to the income account of £30.5m representing the cash amount paid to bondholders. Going forward, annual interest costs will be reduced by circa. £3.6m because of the overall reduction in reported debt. By converting prior to the interest payment date of 14 November we have made interest savings of £1.6m (bondholders must hold on the payment date to receive interest).

Andrew R Cunningham
Deputy chief executive and finance director

16 December 2008

CORPORATE RESPONSIBILITY

Reporting approach

For the first time this year, we are producing a comprehensive report focused specifically on our CR activities over the past year in addition to this summary of CR activity. This can be downloaded from our website: **www.graingerplc.co.uk**

The economic downturn has had a significant impact on the property sector and it would be inaccurate to suggest that this is not having an effect on Grainger's Corporate Responsibility (CR) strategy, and indeed on the approach to sustainable development of those across the property sector.

However, a strong commitment to CR is embedded in Grainger's core business strategy and our seven key objectives are still of central importance. Maintaining our commitment to CR whilst remaining focused on our responsibility to deliver profits to our shareholders will be a challenge in the years ahead. As such, the focus of our strategy is being adapted to reflect these changing conditions, with a greater focus on behavioural change of staff and tenants as opposed to substantial capital investment.

Within this context of economic change, I am particularly proud to be able to report on the success of Grainger's CR strategy in the past year. The fact that we have fully achieved 71% of our targets for 2007/08 is testament to the hard work and commitment of the Grainger team.

Rupert Dickinson Chief executive

Opportunities and risks

Real business opportunities are presented by our continued commitment to CR:

- we believe that investing in our portfolio to make it more energy and water efficient enhances its value;
- engaging with, and investing in, the community is an essential part of good property management. It gives us the opportunity to enhance the communities in which we operate and is also central to the planning process;
- managing and reducing the waste from our development and refurbishment sites can save us money;
- providing opportunities for employee involvement in local communities contributes to employee satisfaction and retention; and
- working with a network of small, local contractors stimulates the economies in which we manage assets. This also means that our tenants receive better customer care.

We are also faced with risks. The recent requirement for us to provide energy performance certificates for all properties at point of rent or sale means that for the first time, customers have an accurate picture of the efficiency of our properties. This combined with rises in energy prices means that the efficiency of our properties is of greater importance than ever before. We hope to turn this risk into an opportunity by focusing on the cost efficient measures we can take to improve the efficiency of our portfolio, thus increasing our competitiveness. We can also use this as an opportunity to further engage with customers about the actions they can take to reduce their impact on the environment and save money on fuel bills.

CORPORATE RESPONSIBILITY

KEY ISSUES OF FOCUS	OBJECTIVE
Environment	Reduce our direct adverse environmental impacts, and help and encourage our employees, suppliers, tenants and customers to do the same
Communities	Seek to understand the needs of the communities within which we operate, and positively contribute to their well-being
Tenants/Customers	Ensure that we treat our tenants and customers fairly, and that we are responsive to their needs
Employees	Encourage staff to contribute to, and share in, the success of the company through their own ideas and ongoing professional development, whilst supporting them to maintain a healthy balance between home and work commitments
Suppliers	Engage proactively with prioritised suppliers to ensure that they meet with our specified economic, social and environmental standards
Health and safety	Safeguard the health, safety and welfare of our employees, and where possible that of our tenants, contractors, visitors, clients and the general public
Investors	Maintain high standards of business conduct, and secure long-term sustainable returns for our investors

Governance

For the past three years, Grainger has had a CR committee which reports to the executive team. Grainger will be restructuring its internal management of CR in the 2008/09 period, which we believe will facilitate greater communication of CR activities across the business. The executive committee, led by CEO Rupert Dickinson will consider key CR issues on a half-yearly basis. These discussions will be informed by a series of working groups that report directly to the executive committee, and which are structured around our key areas of focus.

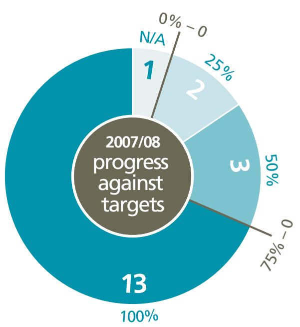
We have various policies and procedures which inform our CR strategy, these are set out in full on our website: http://www.graingercr.com/policies-procedure-guidance.asp

Performance

We have fully achieved 12 (71%) of our 17 applicable CR targets. For a full breakdown of our performance against targets, and for a full set of key performance indicators, please see our downloadable CR report.

The proportion of CR targets that were fully achieved rose from 36% in 2006/07 to 71% in 2007/08. We set targets across all of our main identified impacts. It should be noted that:

- 100% of the environmental and all of the applicable customer targets were fully achieved, representing impressive performance; and
- only one of Grainger's three community targets was 100% achieved and the other two were only 25% achieved. We will therefore ensure a renewed focus on community engagement and investment in the year ahead.



Particular successes for Grainger in the past year include the following:

- all Grainger offices have some form of recycling with 90% of staff able to recycle paper, cardboard and plastic;
- 99% of construction waste from our Newlands Common development was reused on site;
- all newly developed homes are fitted with real time display energy monitors, this will be rolled out to cover newly refurbished properties in our managed portfolio in 2009;
- in 2008, Grainger worked with the charity Emmaus to recycle and reuse 8,000kg of furniture and electrical items;
- 225 members of staff saw our environmental road show presentation; and
- the first survey of customer satisfaction with regard to repair work was undertaken and 69% of customers rated contractors as very good or excellent.

Carbon Emissions 2008/09

Source	2007/08 carbon emissions (tonnes)
Office electricity consumption (small power)	372
Office central plant (heating and cooling)	Not available
Energy use in common parts of residential portfolio	Not available
Air travel	62
Rail travel	13
Taxi travel	Not available
Car travel	Not available
Energy use at development sites (electricity and diesel consumption)	346

This is the first year that Grainger has been able to monitor its carbon emissions. The information included in the above table is based on the following:

- meter readings taken at our eight offices for a 10-month period and extrapolated up to constitute 12 months;
- diesel and electricity consumption on our development sites that is reported via our contractors; and
- business journeys recorded through our corporate travel booking service.

We are, therefore, reliant on the accuracy of data provided by our contractors and we also recognise that additional business journeys may have taken place that weren't booked through this system. These figures should therefore be judged with these limitations in mind and taken as indication of our overall impact rather than a truly accurate measure of our emissions.

CREATIVE
and ambitious approach

- Our people are not only the best in their field, but are those who consistently apply their skills and experience to benefit the group as a whole
- Our ability to innovate enables us to compete where others can't. We aim to be a high-performance team of like-minded experts who share a common vision for growth

WE ARE INTEGRATED

Teamwork across our divisions is vital to our success. By sharing our skills and experience, we can derive the best returns from our assets.

Acquisitions & Disposals

Grainger acquires all types of residential property, throughout the UK. Acquisitions are made from a wide variety of sources, ranging from single assets at auction through to portfolios sourced from long-standing trusted contacts. We have a professional team which is able to execute technically complex transactions. Equally, these expert skills apply to our disposals of assets.

★ Our knowledge of local areas teamed with an awareness of changing markets and lateral thinking allows us to capitalise effectively on growth areas, or sell at the right time to achieve the best returns.

Asset Management

Performance driven asset management is key to our strategy. We add value by minimising void periods and arrears as well as recommending and managing improvements to increase rentals or enhance capital values and marketability. Having applied these skills successfully to our own portfolio for years, we now apply them to portfolios that we manage for others.

★ The cash flows we receive for our asset management activities are an important income stream which is not wholly reliant on the UK house price inflation. We currently provide asset management for Schroders ResPUT, Grainger GenInvest (a 50:50 joint venture between Grainger and Genesis Housing Group) and the Grainger launched G:res1 residential fund.

Fund Management

Fund management is an integral part of Grainger's strategy. It adds a further layer of leverage to our operations, enabling us to generate fees from the skills of the people we employ. We believe that our perspective as a property owner and manager gives us a unique and valuable insight.

★ The additional layers of fees we can generate enhance the return on capital employed.

Property Management

Property management covers the day-to-day operational running of the properties including rent reviews and renewals, repairs and maintenance, block management, lettings and customer care. Again, we manage properties for others, enhancing our returns.

★ In total, we manage some 20,000 UK properties for ourselves and others. We are passionate about raising standards and improving the perception of residential property management in the UK. Therefore, we constantly strive to improve our processes and services.

Sales & Valuations

Our team of professionals cover all areas of the UK which ensures that we have a localised knowledge of our portfolios. This is important in determining strategic acquisitions, accurate valuations and best price on disposal.

★ Our sales team have increased sales proceeds this year by 15%.

WE HAVE TALENT

We pride ourselves on recruiting and retaining outstanding people who are individual experts and great team players. We encourage an entrepreneurial culture where everyone feels they can make a significant contribution to the business, as well as be rewarded by it.

Our people make the difference. They work together seamlessly as assets are managed through their trading cycle, from their initial purchase to their ultimate sale, creating value at each opportunity. Others build trusted relationships, leveraging our skills and those of our partners. We encourage our people, as specialists, to represent Grainger, now a recognised spokesperson in the marketplace.

Our culture supports individuals who want to perform and succeed. Autonomy levels are high, where people are given the opportunity to develop and implement their own initiatives, but with a safety net of an experienced leadership team who oversee and guide.

Learning and development During the year, we implemented a new development initiative called 'Unleash Your Potential'. Every member of staff was given the opportunity to develop themselves, where the development would be mutually beneficial to Grainger. Proposals ranged from spreadsheet skills courses to mini-business plans.

Climate and leadership At Grainger, we strive to continually create and improve an environment which attracts and retains high calibre staff. This year, we conducted a significant staff survey including employees rating how they felt about the 'climate' of Grainger, that is, the aspects of a company which best practice suggests separate high performing companies from others. We are reviewing the results and are dedicated to making more improvements over the coming year and reporting these in our next annual report.

Shared services Throughout the operating division sections of this report, we describe the work and achievements of our property, asset and fund managers. It is important to recognise the professional staff, who work behind the scenes in our support functions. These staff cover a wide variety of roles, from ensuring that we comply with all relevant laws and regulations to providing IT systems capable of handling the many thousands of transactions processed every day. Others in the team are responsible for covenant monitoring, raising finance and deal structuring. It is critical that we seek to continually improve these areas, to maintain a competitive advantage.

Involvement and reward We have high levels of participation in our share schemes and also in Workplace Giving. Many of our employees take up the benefits offered of health care for themselves and their families and travel cover. We expect the highest standards from our staff and offer them a rewarding career with attractive remuneration in return.

% of staff turnover

08	12
07	10
06	25
05	19

% of eligible employees participating in share incentive plan

08	92
07	85
06	83

1 **Feldberg Strasse**
Mannheim

2 **A typical home reversion property**

3 **Mannheim**
Germany

4 **Ashes Farmhouse**
Essex

5 **Pitmaston Court**
Birmingham

6 **Witthues**
Germany

7 **Wetherby Road**
Leeds

8 **Tait and Benson**
London

9 **Ivy Cottage**
Lawn Head, Staffordshire

10 **Rohrhofer Street**
Mannheim

WE HAVE A DIVERSE PORTFOLIO

Core At the heart of our business are 7,300 regulated properties worth £1bn. These are tenanted assets which are bought at a discount to the vacant possession value, so have an inherent 'reversion' (the difference between the tenanted value and the vacant possession value). The tenant has a right to live at the property for the rest of their life. We collect the typically sub-market rent, which is set by a rent officer, and then sell on vacancy to realise the reversion. There have been no new regulated tenancies made since 1989, so our tenants are on average getting older. We therefore have predictable rents and vacancies from these low-value, geographically spread, liquid assets, producing cash flows of over £100m per year and high trading margins. These assets are very liquid as they can be sold tenanted. This provides us with an ideal stock from which to generate additional cash as required.

Also in our core are a further £190m of other units including market let tenancies (assured shorthold tenancies), agricultural tenancies, garages and ground rents.

Retirement solutions Our retirement solutions business is worth in excess of £500m. The largest part of this portfolio, averaging £184,287 full vacant possession, is home reversion assets. Under a home reversion plan, an owner sells Grainger part or all of their home in return for a cash lump sum (or a series of payments) which is dependent upon the vacant possession value of the property, the ages of the individuals and the proportion being sold. This creates a reversion similar to a regulated tenancy, but typically with a deeper discount as there is no rent. The occupiers can then remain in the property for the rest of their lives, after which, the property is sold, to realise the reversion. Distribution, product innovation and regulation are the keys to success in this market. Grainger's equity release products are FSA (Financial Services Authority) regulated and we insist that all of our customers receive impartial professional advice from a qualified third party. Recognising that equity release is not the solution for all, this division also owns approximately 1,000 retirement units. CHARM (a financial asset with returns based on reversionary mortgages) also sits within this area.

Fund management and residential investments Grainger GenInvest LLP – is a 50:50 partnership between Grainger and Genesis Housing Group which was initially formed in June 2005 and owns some £300m of assets. Grainger provides asset management services and Genesis oversee day-to-day management of the properties.

G:res1 – was launched in November 2006 and is a Jersey-based company that invests primarily in market let properties in the UK. Grainger co-invests (current ownership 21.6%), property, asset and fund manages. Total assets are currently worth over £400m.

Schroders ResPUT – is a specialist residential fund which is ungeared. Grainger advises the fund and provides property management services. The portfolio is worth £72m and Grainger owns a 23.6% stake.

Development Our development portfolio consists of a number of key sites, details of which can be found on page 16. Our focus is on large scale, residential led, mixed use sites, where we can work effectively with partners; local authorities and communities, joint venture partners and all other relevant stakeholders. The market value of our portfolio is some £142m including joint ventures.

Continental Europe Our German residential portfolio, with some 6,900 units, is worth over £400m. The majority of the portfolio is in the more affluent south western areas of the country. We believe in time there will be a growth in demand for home ownership of quality housing. We are different from the pure financial investors who have also entered this market in recent years because of our long-term view. The relatively low cost per unit provides potential for significant future capital growth. We also have a joint venture which is developing a site in Zizkov, Prague, worth £10.6m.

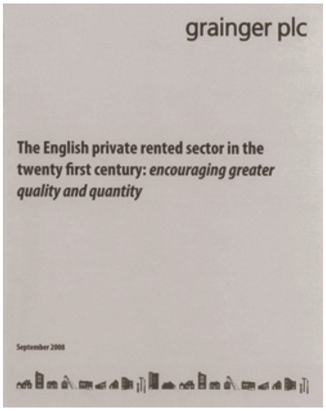
WE ARE AN INDUSTRY LEADER

Our core portfolio of primarily regulated tenancies is one of a kind. It has been built up over a significant number of years and encompasses over 7,000 units spread across the UK.

Grainger's Bridgewater business has now won 'Best Home Reversion Provider' for three consecutive years.

Our success comes from the scale of our portfolio as well as our ability to derive value from it. The regulated tenancies are valued at a discount to their vacant possession values. The total vacant possession value of our regulated tenancies is £1.4bn. This means the reversion, the difference between the vacant possession value and the value these assets are valued at in our market value balance sheet is £0.4m. When the tenants leave, the assets are sold and the reversion is realised. House price changes affects different areas of the country at different times and rates. The knowledge we gain from owning as many properties, geographically spread, means that we can and do buy and sell assets at the best time, to realise best value. We retain a majority of assets in the South East, where there is an undersupply of housing. Another key strength of our core portfolio is the average vacant possession value, which at 30 September 2008 stood at £190,000, compared to the national average of £175,143. In total, some 66% of this portfolio has a vacant possession value of under £250,000. The portfolio therefore has limited exposure to top end volatility. Many properties offer refurbishment opportunities and this keeps them in demand.

Retirement solutions has grown significantly and we expect this to continue as more people seek to release cash to supplement pensions, improve lifestyles or realise dreams. We seek to provide choice in our home reversion products – some people prefer a lump sum, others prefer a series of cash payments. Some find comfort in an early vacancy guarantee and others wish to share in the upside, should house price inflation exceed certain levels. These options are just one reason for the success of our Bridgewater business. Grainger now owns almost 5,000 home reversion assets, with an average vacant possession value (for the whole property) of £184,287. Again, we have limited exposure to top end volatility. We also appreciate that equity release is just one solution to retirement living and it is our aim to provide more options. We have over 1,000 specific retirement apartments, within retirement complexes which are very popular and as a result have high occupancy rates.



A Grainger commissioned report to contribute to the Rugg Review.

Property services within Grainger, prides itself on customer care. We appreciate that our assets are also the homes of thousands of people. We believe that it is this appreciation, combined with our owner/manager perspective that sets us apart from others. Our dedicated property management staff are based in seven offices throughout the UK, giving us national coverage as well as local knowledge. We ensure that our tenants know how to get in touch with their property manager to resolve issues or arrange for repairs to be carried out. Our property managers' knowledge of their portfolio enables them to understand the needs of the assets and the tenants. We strive to raise professionalism in the industry. All of our property managers complete our in-house training to understand how to balance the needs of our customers with expectations for financial returns. Some also study professional qualifications.

As a market leading spokesperson on landlord and tenant issues, our opinion is sought and valued. We believe that a truly professional private rented sector ('PRS') is one potential solution to the current and expected housing shortage in the UK. As the largest listed residential landlord, we are ideally placed to both assist in this change and to benefit from it. We are active in promoting the PRS, through our membership of the British Property Federation. We also have strong proactive relationships with the Chartered Institute of Housing, Association of residential Letting Agents and the Association of Residential Managing Agents. We also fundamentally believe that residential assets should be recognised as an investment class in their own right. This has been starting to happen over recent years.

WE SHARE EXPERTISE, RISK AND REWARDS

Part of our long-term strategy is to capitalise on our expertise by providing **fund management** to third parties and entering into **joint ventures**.

Kempshott Park, Basingstoke
Completed in January 2006, Grainger built to let this 25 unit scheme which now belongs to the G:res1 fund.

Funds

G:res1 is a fund which Grainger launched in November 2006. It is a Jersey-based company that invests primarily in market-let residential properties in the UK. Grainger is a co-investor in the fund, which is independently managed and controlled. Investors are currently a broad mix of UK and overseas institutions.

The fund now holds 2,149 units. 90% of the property is held in London and the south east. During the year, there were strategic sales of blocks of assets. As asset and fund manager, we also recommended and subsequently implemented, breaking up blocks for sale – where greater value could be achieved by selling each apartment individually. We have also managed some refurbishment activity, where it has added value.

As advisor and asset and property manager, we earn fees for delivering returns.
As a co-investor we benefit from dividends.

ResPUT (The Schroders Residential Property Unit Trust) is a specialist residential fund which provides investors with almost ungeared exposure to the UK residential market. The fund is managed by Schroders Property Managers (Jersey) Limited and advised by Grainger. We also manage the property on a day-to-day basis. This fund aims to combine a high quality income yield with above average prospects for capital growth. It has gross assets of £73m and Grainger currently holds a 23.6% stake. The fund is valued monthly. Capital is recycled through strategic sales and astute acquisitions.

Joint ventures

Grainger GenInvest LLP, a joint venture between Grainger plc, the UK's largest listed private landlord, and Genesis Housing Group has invested £1m into the Walworth Estate to refurbish existing homes and transform a derelict space within the estate into a community garden.

Grainger GenInvest LLP was created in June 2005, when Grainger and GenInvest Housing Association formed a 50:50 joint venture to acquire a £70m portfolio of 461 residential units from the Church Commissioners. The partnership acquired a further 1,138 units for £196m in March/June 2006.

The portfolio now consists of 1,566 units in eight blocks in central London. We stated last year that we would identify strategic opportunities to refurbish and so far we have refurbished four blocks. We are now selling from seven blocks in order to generate cash flow. Grainger provides asset management services while GenInvest handles day-to-day property management.

Curzon Park is a 10-acre site in Central Birmingham, acquired through a collaborative (50:50) joint venture with Development Securities plc in December 2006. The initial intention had been to develop this site over six to eight years. We have submitted our outline planning application, however economic conditions are such that development on the site is likely to take place over a longer period than originally anticipated.

Hammersmith is a large mixed use scheme in the heart of the town. Grainger, in a 50:50 joint venture with Helical Bar plc, was awarded preferred developer status and the Conditional Development Agreement was exchanged in March 2008.

WE ARE NOT VOLUME HOUSE BUILDERS

King Street, Hammersmith, London
The 50:50 joint venture partnership of Grainger/Helical Bar were selected as preferred developer by the London Borough of Hammersmith and Fulham in 2008 for this mixed use scheme in the heart of Hammersmith.

Wards Corner, Haringey, London
Grainger was selected by the London Borough of Haringey and the Bridge New Deals for Communities (NDC) in 2004 as the preferred development partner to regenerate the area around Seven Sisters underground station.

Longstrops, Martlesham, Ipswich
Longstrops is 130 acres of land which is designated for an extension of the existing settlement of Kesgrave in Suffolk. Grainger has made a representation to the local development framework process and Suffolk Coastal District Council is currently reviewing potential sites.

Our **core** and **retirement solutions** portfolios are geographically spread and are purchased at significant discounts to their vacant possession values.

These factors protect us to an extent from certain risks in the housing market.

Unlike a volume house builder, we do not attempt to sell many properties in one location at the same time and our properties do not suffer from cluster risk. Furthermore, due to the discounts at which we purchase our properties and the long average period we hold the assets before sale, our margins are typically 45% to 50%. This means that in the current market, we can ensure our properties are competitively priced, to keep cash flow coming into the business.

Our **development** business focuses on building residential led mixed use schemes. We promote the benefits of good design by creating schemes that take into account the way people live.

Our development activities fall into two main categories:

Residential led mixed use schemes where we work with partners to leverage our respective skills and knowledge, to deliver complex developments. Examples of this include the Curzon Park and Hammersmith joint ventures described on the previous page.

Strategic Land where we take a long-term view, setting out with an initial objective to achieve planning, then to develop, often in a number of phases. We currently own a significant 520-acre site, Newlands Common, West Waterlooville in Hampshire. During the year, we obtained planning permission for 1,550 new homes and 100,000 sq. m. of commercial space. We originally signed an option agreement for this land in 1995.

OUR SKILLS ARE TRANSFERABLE ABROAD

In **Germany** we now own or have a majority interest in almost 7,000 residential properties worth more than €500m.

We approach our investment in Germany for the long term as we believe that, at some point, an increase in home ownership will occur in this nation which lags others across Europe. Grainger is now well placed to benefit from this.

Our ownership is substantially in the more affluent areas of the country, in the south and west. Our property and asset management skills are ensuring that whilst we hold these assets, we maximise the value by minimising voids, identifying strategic refurbishment opportunities and effectively collecting rents. Our staff advise on asset management, including acquisitions and disposals. We believe we now have a critical mass and intend to seek third-party equity investment, in line with our strategy.

We have recently moved offices, from Mannheim to Frankfurt.

1 **Highbrow**
Harborne

2 **Mannheim**
Germany

3 **Dibden House**
Maida Vale, London

4 **Cottage on Ranton Estate**
Staffordshire

5 **Walworth**
London

6 **Carless Avenue**
Harborne

7 **Ravenhurst Avenue**
Harborne

8 **Homewell**
Havant, Hampshire

9 **The Lodge**
Pitmaston, Birmingham

10 **Hill Top Farm**
Staffordshire

THE BOARD

1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4


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9


1 **Robin Broadhurst** C.B.E., F.R.I.C.S. Chairman, chairman of nomination committee. Aged 62

Appointed director of the company in February 2004. Previously European chairman of Jones Lang La Salle, Trustee and non-executive director of Grosvenor, a senior advisor to Credit Suisse Group, property consultant to Sir Robert McAlpine Limited, member of the Prince's Council for the Duchy of Cornwall and non-executive director of the British Library and Invista Real Estate Investment Management plc.

2 **Rupert Dickinson** M.R.I.C.S. Chief executive. Aged 49, Chartered Surveyor

Joined the company in 1992 from Richard Ellis (now CBRE). Appointed a director of the company in 1994. Appointed chief executive in October 2002. Joined Workspace Group plc as a non-executive director in August 2006. Chairman of the residential committee and member of the policy committee of the British Property Federation, member of the International Property Federation.

3 **Andrew Cunningham** F.C.A. Deputy chief executive and finance director. Aged 52, Chartered Accountant

Joined Deloitte Haskins and Sells in London in 1978 and worked in their Nairobi and Bristol offices before being made a partner in their Newcastle office in 1989. Appointed a director of the company in December 1996. Appointed deputy chief executive in December 2002. In May 2007, was appointed non-executive director of The Local Shopping REIT plc.

4 **Stephen Dickinson*** F.C.A. Deputy chairman. Aged 74, Chartered Accountant

In practice in British Virgin Islands 1963-1974. Appointed managing director of the company in 1974. Upon retiring as managing director in October 2002, became deputy chairman. British Virgin Islands representative on United Kingdom Overseas Territories Association 1993-2004. Chairman of Deutsche Land plc since February 2006.

5 **Robert R S Hiscox*** A.C.I.I. Member of nomination and remuneration committees. Aged 65

Appointed a director of the company in March 2002. Chairman of Hiscox Limited. Deputy chairman of Lloyd's 1993-1995.

6 **John Barnsley*** F.C.A. Chairman of audit committee and member of remuneration committee. Aged 60, Chartered Accountant

Appointed a director of the company in 2002. Non-executive director of Northern Investors Company plc, American Appraisal Associates LLP and LMS Capital plc. Chairman of Westover Medical Limited. Until December 2001 was a senior partner at PricewaterhouseCoopers.

7 **Henry Pitman*** Member of audit committee. Aged 46

Appointed a director in May 2007. Currently chairman of African Century, an African investment business. Previously chief executive of Tribal Group plc. Prior to this, he was managing director of JHP Group Limited. From 1990-1995 he worked for the Property Corporation of South Africa.

8 **Bill Tudor John*** Senior independent director, chairman of remuneration committee, member of nomination committee. Aged 64

Appointed a director of the company in February 2005. Currently a managing director of Nomura International, previously a partner at Allen & Overy LLP for 29 years, serving as senior partner for six years. Also deputy chairman of the Nationwide Building Society and deputy chairman of the Bank of England Financial Markets Law Committee. An Associate Fellow of Downing College, Cambridge.

9 **Baroness Margaret Ford*** Member of audit committee. Aged 51

Managing director in the Royal Bank of Canada's Capital Markets Group. Senior independent director of Serco Group plc. Prior to this she was chairman, from 2002, of English Partnerships. Early career in a variety of housing and regeneration roles across the public and private sector.

* non-executive directors

CORPORATE GOVERNANCE REPORT

The board continues to uphold the highest standards of governance which are at the heart of the way business is conducted by Grainger. Changes made to the operation of the board by Robin Broadhurst in his early months as chairman in 2007, are now embedded in the way the board functions.

The board believes that corporate governance is fundamentally about the way a company operates and should not be an automatic response to a check list. However, it is also mindful that The Combined Code 2006 is generally accepted to describe good governance and seeks to comply as far as possible where this is in the best interests of the company. The statement of compliance refers to The Combined Code 2006, which was applicable to Grainger.

This report fulfils the requirements of the Listing Rules and should be read in conjunction with the reports of the individual committees which follow.

The directors

A company is only as good as the people who work for it and the directors are committed to ensuring that the board itself includes people who have all of the necessary skills, knowledge and experience to successfully lead the organisation. For the period 1 October 2007 until 3 July 2008, the composition of the board was, in the board's view, the chairman, deputy chairman, two executive directors and four independent non-executive directors. Baroness Margaret Ford was appointed to the board as an independent non-executive director on 3 July increasing the level of independence on the board.

The directors therefore believe that, excluding the chairman, the board consisted of at least half independent non-executive directors for the entire reporting period.

Roles

There is a written, approved statement of the separation of duties of the chairman, who reports to the board and the chief executive, who reports to the chairman. Other key differentiating factors are as follows:

The chairman
Responsible for running the board
Only the chief executive and the company secretary (for corporate governance matters) reports to him
Guardian of the board's decision making

The chief executive
Responsible for running the business
All executive management report to him, directly or indirectly
Responsible for implementing the board's decisions

Other key roles include the senior independent director and the chairmen of the committees. Bill Tudor John held the position of senior independent director for the entire period under review. The committees' compositions and work are described in detail in their own reports which follow.

Independence

For several years the board has been increasing the number of independent directors and again this year a further independent non-executive has been appointed. As noted in previous years, the chief executive is a cousin of the deputy chairman. However, as announced at the time of the preliminary announcement on 27 November 2008, the deputy chairman will be stepping down from the board at the conclusion of the Annual General Meeting in February 2009. As explained in The Combined Code, the criteria of A.3.1 are only a guideline and it is the directors' view of the independence of a particular director that is ultimately important. In forming their opinion, the directors consider, amongst other things, the individual's professional characteristics, their behaviour at board meetings, their contribution to the debate and unbiased judgement.

The following analysis explains the board's duly considered view of the independence of the directors.

Director	Board's determination	Explanatory notes
Robin Broadhurst (Chairman)	Independent	• Independent under A.3.1 criteria
Stephen Dickinson (Deputy chairman)	Not independent	• Close family ties • More than nine years' service • Previously managing director • Part-time executive responsibilities • Participation in all-employee share scheme
Bill Tudor John (Senior independent director)	Independent	• Independent under A.3.1 criteria
John Barnsley	Independent	• Independent under A.3.1 criteria
Robert R S Hiscox	Independent	• Although a trustee for an Estate holding a material shareholding, the board is of the opinion that this position does not interfere with or influence his character or judgement in any way. As chairman of Hiscox Ltd, and past deputy chairman of Lloyd's, Mr Hiscox brings extensive skills and experience in his own right, which can only be beneficial to Grainger's board • The Estate has reduced its shareholding over the past four years, from 12.5 million shares to 9 million shares
Henry Pitman	Independent	• Independent under A.3.1 criteria
Baroness Margaret Ford (Appointed 3 July 2008)	Independent	• Independent under A.3.1 criteria

Full biographical details of all current directors are given on page 39.

Retirement by rotation and re-election

The board recognises that it is important to adhere to good governance principles and all board members are as such, required to stand for re-election at intervals of no more than three years. However, the board is also of the view that long-term stability in the board is an important factor, given the long-term nature of the business. Continuation of leadership throughout, for example, the period of a significant development, is considered particularly beneficial. The chairman has satisfied himself that, following evaluation, all directors offering themselves for re-election continue to show the required commitment and effective performance.

Meetings

There were six ordinary meetings of the board in the year, where the board met to review the business and to consider the items reserved specifically for it which have been documented and approved by the board. These include setting the overall strategy, approving major transactions, setting debt/gearing limits and associated hedging strategy and agreeing accounting policies. No changes were made to this schedule during the year. Decisions regarding more minor transactions are delegated to management.

Most meetings were preceded, the evening before, with an informal meeting allowing more time for debate and also a dinner, giving an opportunity for the directors to enhance their relationships with each other. All directors attended all meetings during their relevant periods of office except for Robert Hiscox, who was not present at two of the meetings, and Henry Pitman who was not present for one. This was the first year where six ordinary meetings were held, compared to four previously. The board is satisfied that six is an appropriate number and intends to continue to meet with such frequency.

CORPORATE GOVERNANCE REPORT

In order to accommodate the new timetable of meetings, the meeting which is held for an extended period in order to debate and reflect fully on strategy, was held in April rather than June. This event continues to provide an ideal opportunity for the board to spend time with the senior executives. Further, the board now receives presentations from senior executives on a rotational basis.

As well as the ordinary meetings, ad hoc meetings are arranged as necessary in order to consider major transactions or events. Due to the short notice, which is unavoidable, all directors are not always able to attend, or to join by teleconference. Wherever possible the chairman will take on views of the non-attending director prior to the meeting.

Board papers are produced and distributed in a timely manner for each meeting, being in the hands of the board five working days before the meeting. They contain sufficient financial and non-financial information to allow the board to properly monitor the group and understand the challenges facing it and opportunities open to it. The format of the papers specifically highlights items for decision and for discussion. In this way the board can be sure that it concentrates its efforts and allocates sufficient time to those items which are most important.

Each director is given an opportunity to raise an item to the agenda and any request for further information from a director is treated as a high priority. The directors also have direct access to the services of the company secretary, who reports to the chairman regarding matters of corporate governance. The appointment and removal of the company secretary is a matter for the board as a whole. Procedures also exist for directors to take independent professional advice as required, at the group's expense.

The chairman met twice during the year with the non-executives, without the executives present as planned. These meetings will continue with this frequency.

Induction, evaluation, training and development

Baroness Margaret Ford was appointed in the year and received a comprehensive, tailored induction to the company. This consisted of the provision of a 'bible' of information covering such items as the most recent risk review, recent minutes, terms of reference of the committees etc as well as sessions with each member of the senior management team. These meetings were arranged in small groups so that as well as the divisional leaders each giving a presentation of their business area, discussion and debate was encouraged.

Baroness Ford also joined a property tour, to enable her to see some of the company's properties – ranging from the core regulated portfolio through to the development activities.

Directors and Officers insurance is held by the company and details of the policy are given to new directors on appointment.

The evaluation process was again successfully completed. The process was conducted internally and consisted of a written questionnaire followed by an interview with the chairman. The questionnaire covered all of the board as a whole, the committees and the individual directors and all of these areas were picked up as relevant in the subsequent interviews. Notes of the interviews are held only by the chairman and the company secretary since it has been proved in recent years that this allows the directors to be more open in their discussions.

The chairman was pleased with the commitment shown by the directors to the process. The whole evaluation exercise and its outcomes were reviewed formally at a board meeting. As a result of the evaluation process the board identified the need for a chief operating officer to sit below board level and are in the process of defining a clear role. In response to results from last year's evaluation, there has been increased communication between executives and non-executives this year. In particular, the non-executives now receive a bi-weekly update covering items ranging from sales and the market, to management and leadership initiatives. This has been invaluable during the rapidly changing economic climate over the period under review.

The senior independent director spoke with the executives and the non-executives individually in order to evaluate the chairman. The board's written document for the separation of the roles of the chairman and the chief executive was used as a basis for the evaluation.

The board is provided with regular written updates which are relevant to a listed property company. Presentations are also received from the senior management who lead the business divisions, which inform the directors about relevant aspects of their markets. Directors are able to request specific training, through the chairman or company secretary. If any development areas are identified for the board as a whole, its committees or for directors as individuals, then they would be appropriately addressed on appointment or thereafter.

Relations with stakeholders

The primary contacts with shareholders, analysts and potential investors are the chief executive, and deputy chief executive and finance director. The usual half yearly results announcements and briefings were also attended by some of the company's most senior management and this was welcomed by shareholders. Apart from these meetings, there have again been circa. 100 meetings and presentations by the executive directors, to maintain an appropriate dialogue. They also participated in conferences, including the Credit Suisse Real Estate conference in New York. The level of meetings with private client brokers was maintained from the previous year. Feedback is always sought following such events and is presented to the board as a whole. The board is briefed on the views of major shareholders. Further, all directors, including the chairman and non-executives, are available for meetings with shareholders. There were no requests in the year from shareholders to meet Baroness Ford, the newly appointed non-executive director. Along with all other directors, she will be in attendance at the annual general meeting and available to answer questions.

The group's website includes a specific and comprehensive Investor Relations section, containing all RNS announcements, share price information, annual documents available for download etc. All shareholders have the opportunity to attend the Annual General Meeting, which continues as a route for communication with smaller/private shareholders.

The notice of meeting and annual report and accounts are sent out at least 20 working days before the meeting. Separate votes are held for each proposed resolution, including the approval of the remuneration committee report, and a proxy count is given in each case after the voting on a show of hands. Grainger includes, as standard, a 'vote withheld' category, in line with best practice. Shareholders are also able again to lodge their votes through the CREST system.

Internal control

The group has a cyclical process for identifying, assessing and managing its significant risks, which has been in place for the full year under review. The process is designed to enable the board to be confident that such risks are mitigated, or controlled as far as possible. It should be noted however that no system can eliminate the risk of failure to achieve business objectives entirely and can only provide reasonable and not absolute assurance against material misstatement or loss. The audit committee is delegated the task of reviewing all identified risks, with the ultimate key risks retained for full board review. The audit committee reports to the board at every board meeting. Risks and controls are reviewed to ensure effective management of appropriate strategic, financial, operational and compliance issues. The audit committee also reviews the half year and full year financial statements and holds discussions with the group's auditors. In addition, the group has an internal audit function which performs relevant reviews as part of a programme approved by the audit committee. The committee considers any issues or risks arising from internal audit in order that appropriate actions can be undertaken for their satisfactory resolution. The internal audit manager has a direct reporting line to the chairman of the audit committee.

An annual budget is produced, together with longer-term projections in accordance with the agreed strategy, which are presented to the board for approval. A fundamental part of the control process is the diligent monitoring of actual performance against this budget by the board. Where applicable, revisions are made to expected outturn against which further progress can be monitored.

The board also discusses in detail the projected financial impact of major proposed acquisitions and disposals, including their financing. All such proposed substantial investments are considered by all directors. Where meetings are required between board meetings and a full complement of directors cannot be achieved, a committee of directors considers the necessary formalities. The board is also responsible for the discussion and approval of the group's treasury strategy, including mitigation against changes in interest rates.

Going concern

After making diligent enquiries, including the review of future anticipated cash flows and compliance with banking covenants, the directors have a reasonable expectation that the group and company have adequate resources to continue in existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the accounts.

CORPORATE GOVERNANCE REPORT

Compliance statement

Independence of non-executive directors is explained in detail above. In the board's view it is their assessment of independence which determines compliance with the Code and therefore no non-compliance on grounds of independence has been recorded.

The board considers that it has complied in full with the Combined Code 2006, during the year ended 30 September 2008.

Nomination committee report

The nomination committee consisted throughout the year, of Robin Broadhurst as chairman, and Robert Hiscox and Bill Tudor John as independent members.

Due to the relatively small size of the board, matters which are included in the nomination committee's terms of reference are often discussed by the board as a whole. As a result, this committee met only informally and communicated by telephone or email.

The terms of reference are available on the group's website and principally relate to filling vacancies on the board. The committee is also responsible for reviewing the desirability of the continuation of service of directors required to retire by rotation.

Baroness Margaret Ford was appointed in the year. Although there was an external agency involved, having been introduced by an existing director, she was subject to a formal process involving being interviewed by all of the directors, prior to her being appointed.

Audit committee report

The audit committee meets four times each year and reports on its work at every subsequent board meeting. This is a critical part of the internal control process.

On appointment to the board on 3 July, Baroness Ford was also appointed to the audit committee. The board considers that being a member of the audit committee is an excellent way to quickly gain an understanding of the key risks in the business. After one meeting with four members present, Bill Tudor John resigned from the audit committee.

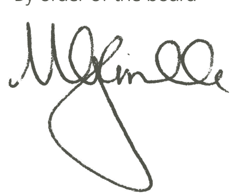
Attendance of the individual directors is shown below. Mr Barnsley has the particular recent, relevant financial experience required by The Combined Code.

	Nov 2007	Feb 2008	May 2008	Sep 2008
John Barnsley Chairman	✓	✓	✓	✓
Henry Pitman Member	✓	✓	✓	✓
Bill Tudor John Member (resigned 10 September 2007)	✓	✓	✓	✓
Baroness Margaret Ford Member (appointed 3 July 2008)	n/a	n/a	n/a	✓

The audit committee adheres to particularly strict and detailed terms of reference, which are available for inspection on the group's website. In addition to the work described within the 'Internal Control' section of the main report above, the audit committee is also responsible for reviewing the independence of the external auditor, which includes the approval of any non-audit service fees above a relatively nominal level. The audit committee is responsible for the appointment of the external auditor and for agreeing the audit fee.

The deputy chief executive/finance director and external audit partner as well as other senior management are invited to attend meetings of the committee. The audit committee requires presentations from members of staff such as the treasury director, tax director and IT director (all non-statutory directors), to ensure that they feel sufficiently close to these important individuals who have significant levels of control to maintain. Once each year the audit committee meet with management without the auditors present and also with the auditors without management present.

By order of the board



Marie Glanville ACA ACIS
Company secretary 16 December 2008

REPORT OF THE REMUNERATION COMMITTEE AND DIRECTORS' REMUNERATION REPORT

This report meets the disclosure requirements of the Companies Act and the Listing Rules and in accordance with usual practice will be put to shareholders for approval at the Annual General Meeting.

The remuneration committee

The remuneration committee consisted throughout the period of Bill Tudor John (chairman), with Robert Hiscox and John Barnsley as members.

In the opinion of the directors the committee therefore comprised three independent non-executives throughout the year. Certain shareholder pressure groups continue to raise concerns that Mr Hiscox, as trustee of an estate containing a material shareholding, should not be regarded as independent. The board maintains their view that Mr Hiscox is independent and a valued contributor to the remuneration committee.

The remuneration committee met formally four times during the year and all members attended except for Robert Hiscox, who was unable to attend one of those meetings. The committee have also communicated informally during the year, in particular with regard to the finalisation of the LTIP grant.

This year New Bridge Street Consultants LLP ('NBSC') continued to be involved in the set up and implementation of the LTIP. NBSC have no other connection with the company or its directors as individuals. Further, the remuneration committee engaged the services of the Hay Group to benchmark the salaries and packages of the executive directors.

The committee's terms of reference are available on the group's website.

Remuneration policy

Grainger's remuneration policy is designed to attract, motivate and retain high calibre individuals to enable the group to operate strategically for the continued benefit of shareholders, over the long term. In order to operate this policy, the remuneration committee receives information on remuneration packages awarded to directors in comparable organisations and aims to ensure that the rewards paid by Grainger are competitive.

The policy is also designed to align the directors' interests with those of shareholders. This is principally achieved through the use of share-based incentives and by encouraging executive directors to maintain a reasonable shareholding in the group. As a guideline, executive directors (and senior executives) are expected to hold the equivalent value of at least one year's salary in Grainger shares. Details of executive directors' shareholdings are shown on page 52. Share awards are generally satisfied by the acquisition of shares in the market, so are not dilutive to shareholders. Share options are satisfied by the issue of new share capital.

Remuneration packages balance both short and long-term rewards, as well as performance-related pay and non-performance-related. They include salary, bonus and defined contribution pension elements as well as long-term share incentive and option schemes. Usual benefits are also afforded.

No executive director is involved in the determination of his own remuneration. Fees of the non-executive directors, which include increments where a committee chairmanship or senior independent position is held, are determined by the board as a whole.

The salaries and bonuses of senior management are determined by the executive directors and reported to the remuneration committee. Senior management also participate in long-term incentive scheme arrangements described below. Usual benefits are also afforded to these individuals. In this context, senior management are those employees who are members of the 'executive team'. In addition to this, specific bonus schemes were negotiated with certain key senior management during the year, based on their specific business areas, in order to drive performance.

The remuneration committee also review the total level of salaries and bonuses paid to the group as a whole. This includes reviewing the details of any employee earning over £50,000 or earning a bonus in excess of £5,000.

REPORT OF THE REMUNERATION COMMITTEE AND DIRECTORS' REMUNERATION REPORT

Service contracts

Service contracts were updated during the year to incorporate best practice. Contract dates and unexpired terms for the directors are as follows:

	Contract date	Unexpired term*	Notice period
Rupert Dickinson	19 July 1996	No fixed term	12 months
Andrew Cunningham	26 July 2000	No fixed term	12 months
Robin Broadhurst	26 February 2004	5 months	None
Stephen Dickinson	28 February 2000	5 months	None
Bill Tudor John	24 February 2005	29 months	3 months
John Barnsley	27 February 2003	5 months	3 months
Robert Hiscox	6 March 2002	29 months	3 months
Henry Pitman	1 May 2007	17 months	3 months
Baroness Margaret Ford	3 July 2008	29 months	3 months

* calculated as at 30 September 2008 and rounded to the nearest whole month

Apart from salary and benefits in relation to the notice period described above, there are no other terms in any of the contracts which would give rise to compensation payable for early termination, or any other liability of the company.

Each non-executive director has specific terms of reference. Their contracts state an initial one-year period, with a continuation subject to review at that time. Their contracts contain no entitlement to compensation for early termination.

Other directorships

Rupert Dickinson has served as a non-executive director of Workspace Group plc throughout the period under review. Grainger's board were satisfied that the appointment would be of mutual benefit, with Rupert gaining invaluable experience of another plc. Andrew Cunningham has served as a non-executive director of The Local Shopping REIT plc. As in the previous year, both executive directors retained the fees paid to them by the respective organisations. In the year under review, Rupert Dickinson and Andrew Cunningham retained £36,000 and £30,000 respectively.

NON-PERFORMANCE-RELATED REMUNERATION

Basic salaries and benefits

Basic salaries are reviewed by the remuneration committee annually. Uplifts are by reference to cost of living, responsibilities and market rates, as for all employees and are performed at the same time of year. It was decided for the year commencing 1 October 2008 that the executive directors would receive no salary increase, in light of market conditions. Executive directors and the deputy chairman, Stephen Dickinson, who has part-time executive responsibilities, along with other senior members of staff, receive a fully expensed company car, or a car allowance. All members of staff, including the executive directors, benefit from health and life insurances.

The chairman's and non-executive directors' fees are reviewed on a biennial basis by the whole board. The non-executives agreed that due to market conditions, they would waive an increase for the period starting 1 October 2008, with the next review date set at 1 October 2009.

Pensions

The group contributes 15% of basic salary to the money purchase pension schemes of Rupert Dickinson and Andrew Cunningham. No other elements of remuneration are pensionable.

Share schemes open to all employees

Executive directors, and Stephen Dickinson, deputy chairman, are eligible to participate in two share schemes which are open to all employees with relevant service, subject to the rules of the schemes.

The first is a save as you earn ('SAYE') scheme, and the second a share incentive plan ('SIP'). Both are Inland Revenue approved and therefore subject to the limits prescribed.

Amounts relating to directors' participation in the SIP and share options under the SAYE scheme are shown on pages 49 and 50.

PERFORMANCE-RELATED REMUNERATION

As should be expected and in accordance with the Combined Code, a significant element of executive directors' and senior management's potential remuneration is performance-related. The combination of short and long-term incentives attempt to align the interests of executives and senior management with the interests of shareholders, and to reward significant outperformance of expectations.

Non-executive directors do not receive performance-related remuneration.

Annual discretionary bonus

Each year the remuneration committee considers the award of a bonus to the executive directors, which is at their ultimate discretion. The chief and deputy chief executive officers, Rupert Dickinson and Andrew Cunningham participate in an arrangement introduced in 2003 whereby the provisional bonus is calculated over a three-year period, by reference to the enhancement of the triple net asset value of Grainger, relative to a theoretical market comparator. The comparator movement is calculated with regard to the Nationwide and Halifax house price indices and also interest rates – using five-year swap rates. Bonuses remain capped at 150% of salary which would only be achieved under exceptional performance conditions. Subject always to the committee's discretion, one third of the calculated amount is approved for payment and the provisional balance is taken into account over the next two years.

It has been decided that no award will be payable for the year ended 30 September 2008, in recognition of the market conditions. In 2007, 107% of salary for that year was paid.

Long-term incentives

Grainger's policy in relation to long-term incentive schemes has evolved over time to more closely align the long-term interests of executives and senior management with those of shareholders, to reward sustained performance over a number of financial years and to encourage these employees to grow their shareholdings.

The current long-term incentive scheme ('LTIS') was approved by shareholders in February 2007.

Current long-term incentive scheme

This scheme makes conditional awards of shares to reward performance and retain key staff over rolling three-year periods. The potential award is split into two, with two thirds of the awards being dependent upon the absolute level of increase in NNNAV and one third dependent upon the increase in absolute TSR as follows:

Average annual growth in NNNAV	Percentage of the NNNAV proportion of an award which will vest
Less than or equal to average WACC	0%
Equal to average WACC + 3%	100%
Between average WACC and average WACC + 3%	Pro rata on a straight-line basis between 0% and 100%

TSR of the company over the TSR performance period	Percentage of the TSR proportion of an award which will vest
TSR being less than or equal to 8% compounded per annum (25.98% growth in total over the TSR performance period)	0%
TSR being equal to or greater than 16% compounded per annum (56.09% growth in total over the TSR performance period)	100%
Between 8% compounded per annum and 16% compounded per annum	Between 0% and 100% pro rata on a straight-line basis

REPORT OF THE REMUNERATION COMMITTEE AND DIRECTORS' REMUNERATION REPORT

There is also a matching awards element to the scheme, to encourage executives to develop and maintain a shareholding in the company. Participants may pledge or buy shares of equivalent value to 30% of their relevant salary and to the extent that performance criteria are met, these shares will be matched one for one at the end of the three-year period.

Fundamentally it was considered that absolute measures of performance were suitable because Grainger is unusual in nature and has no natural comparator group. Grainger is the only listed company of its size to invest primarily in residential property assets. All other comparably sized property companies are principally commercial or development focused.

Awards were made under this current scheme in March 2007 and January 2008 and are quantified below.

These performance criteria are believed to be stretching, but realistic and reward executives if Grainger's return to shareholders is significant in absolute terms.

Previous long-term incentive scheme

There is one prior year award outstanding which operates under the previous long-term incentive scheme so the details of that scheme are also included here. Participants were eligible to receive annual conditional awards of shares worth up to 50% of salary under the long-term incentive scheme and of share options up to a maximum of 125% of salary under the executive share option scheme. The awards under both schemes will become unconditional if challenging performance criteria are satisfied over a single three-year performance period following grant. The criteria for the awards were based on total shareholder return ('TSR') – dependent upon where Grainger's TSR lies with respect to a pre-determined comparator group as follows:

Performance condition	Vesting of option
If Grainger's TSR is equal to or greater than the upper quartile TSR of the comparator companies	100%
If Grainger's TSR is equal to the median TSR of the comparator companies	40%
If Grainger's TSR is above the median but below the upper quartile TSR of the comparator companies	Pro rata vesting
If Grainger's TSR is below the median TSR of the comparator companies	0%

As shown in the table above, no award vests unless Grainger's TSR is higher than the median TSR of the comparator group.

It should be noted that during its period of operation, it has been necessary to change the comparator group due to companies being taken over. The comparator group for the awards made in January 2006 comprised A & J Mucklow Group plc, Big Yellow Group plc, Brixton plc, Capital and Regional plc, CLS Holdings plc, Daejan Holdings plc, Derwent Valley Holdings plc, Freeport plc, Great Portland Estates plc, Helical Bar plc, London Merchant Securities plc, Mapeley Limited, Minerva plc, Quintain Estates and Development plc, Shaftesbury plc, St Mowden Properties plc, The Unite Group plc, Warner Estate Holdings plc and Workspace Group plc.

The awards under the scheme failed to vest for the second year in January 2008.

As required by legislation covering the directors' remuneration report, the graph below shows TSR (based upon share price growth with dividends reinvested) for Grainger, compared to the comparator group, the FTSE 250 and the FTSE Real Estate Index. These comparators have been chosen on the basis that they are the markets within which Grainger operates, albeit that the Real Estate Index comprises mainly commercial property companies.

Source: Datastream

The auditors have audited the following parts of the remuneration report:

Directors' remuneration

Chairman, deputy chairman and executive directors	Robin Broadhurst £'000	Stephen Dickinson £'000	Rupert Dickinson £'000	Andrew Cunningham £'000	Robert Dickinson £'000	Total £'000
Non-performance-related remuneration						
Salary and fees	120	150	490	370	–	1,130
Taxable benefits	–	18	12	24	–	54
Share incentive plan	–	6	6	6	–	18
Total non-performance-related remuneration	120	174	508	400	–	1,202
Performance-related remuneration						
Annual discretionary bonus	–	–	–	–	–	–
Total performance-related remuneration	–	–	–	–	–	–
Total remuneration for the year ended 30 September 2008	**120**	**174**	**508**	**400**	**–**	**1,202**
Total remuneration for the year ended 30 September 2007	88	174	976	750	56	2,044
Pension contributions into money purchase schemes						
Year ended 30 September 2008	**–**	**–**	**74**	**56**	**–**	**130**
Year ended 30 September 2007	–	–	69	52	–	121

Non-executive directors	John Barnsley £'000	Baroness Margaret Ford £'000	Robert Hiscox £'000	Henry Pitman £'000	Bill Tudor John £'000	Total £'000	Total all directors 2008 £'000
Non-performance-related remuneration							
Salary and fees	50	9	35	35	50	179	**1,309**
Taxable benefits	–	–	–	–	–	–	**54**
Share incentive plan	–	–	–	–	–	–	**18**
Total non-performance-related remuneration	50	9	35	35	50	179	**1,381**
Performance-related remuneration							
Annual discretionary bonus	–	–	–	–	–	–	–
Total performance-related remuneration	–	–	–	–	–	–	–
Total remuneration for the year ended 30 September 2008	**50**	**9**	**35**	**35**	**50**	**179**	**1,381**
Total remuneration for the year ended 30 September 2007	47	–	35	15	47	144	**2,188**

Baroness Margaret Ford was appointed a non-executive director on 3 July 2008. Prior to her appointment she was paid £8,750 in advisory fees.

Robert Dickinson retired from the board on 28 February 2008. Robin Broadhurst was appointed chairman on the same date. Henry Pitman was appointed a non-executive director on 1 May 2007.

REPORT OF THE REMUNERATION COMMITTEE AND DIRECTORS' REMUNERATION REPORT

Directors' share options

Ordinary shares (thousands)		Stephen Dickinson		Rupert Dickinson		Andrew Cunningham		Total	
Dates exercisable	Exercise price	30 Sep 2008	30 Sep 2007	30 Sep 2008	30 Sep 2007	30 Sep 2008	30 Sep 2007	30 Sep 2008	30 Sep 2007
Non-performance-related (available to all staff)									
SAYE scheme									
1 September 2008 to 1 March 2009	£1.865	**9**	9	**–**	–	**–**	–	**9**	9
1 September 2012 to 28 February 2013	£4.543	**–**	–	**–**	4	**–**	4	**–**	8
1 September 2013 to 28 February 2014	£1.678	**10**	–	**10**	–	**10**	–	**30**	–
Performance-related (conditional awards)									
Inland Revenue Approved Executive Share Option Scheme									
23 March 2010 to 23 March 2017	£6.409	**–**	–	**5**	5	**5**	5	**10**	10
Long-term incentive scheme									
11 January 2008 to 11 January 2015 (lapsed)	£3.818	**–**	–	**–**	138	**–**	103	**–**	241
12 January 2009 to 12 January 2016	£5.280	**–**	–	**104**	104	**78**	78	**182**	182
		19	9	**119**	251	**93**	190	**231**	450

Performance conditions for options exerciseable 11 January 2008 to 11 January 2115 at £3.818 were not met, thus the options lapsed.

The market price of the company's shares at the end of the financial year was £2.00, and the range of the closing mid-market prices during the year was £1.868 to £4.65.

Directors' share awards

Ordinary shares of 5p each (thousands)			Rupert Dickinson		Andrew Cunningham		Total	
	Award date	Earliest vesting date	30 Sep 2008	30 Sep 2007	30 Sep 2008	30 Sep 2007	30 Sep 2008	30 Sep 2007
Performance-related (conditional awards)								
Long-term incentive scheme								
2004 scheme (lapsed)	11 Jan 2005	11 Jan 2008	**–**	55	**–**	41	**–**	96
2005 scheme	12 Jan 2006	12 Jan 2009	**42**	42	**31**	31	**73**	73
2006 scheme	23 Mar 2007	23 Mar 2010	**108**	108	**81**	81	**189**	189
2007 scheme (granted in the year)	09 Jan 2008	09 Jan 2011	**217**	–	**164**	–	**381**	–
Matching awards (conditional)	23 Mar 2007	23 Mar 2010	**22**	22	**16**	16	**38**	38
	09 Jan 2008	09 Jan 2011	**43**	–	**33**	–	**76**	–
			432	227	**325**	169	**757**	396

Performance conditions for the conditional share awards set to vest on 11 January 2008 were not met.
The conditional awards therefore lapsed on those respective dates.

On behalf of the board

Bill Tudor John
Chairman of the remuneration committee

DIRECTORS' REPORT

The directors present their report and the audited financial statements for the year ended 30 September 2008.

Principal activities

During the year the group has continued its activities of property trading and development.

Review of business development and prospects

Development of the group's activities and its prospects are reviewed in the chairman's statement on pages 6 to 8 and the chief executive's review on pages 10 to 17

Results for the year

The results of the group are set out in the consolidated income statement on page 4 of the accounts section of this document which shows a loss for the financial year attributable to the equity holders of the company of £77.4m (2007: £60.9m profit).

An interim dividend of 2.27p per share (2007: 2.06p) was paid on 4 July 2008 amounting to £2.9m (2007: £2.7m) and the directors recommend the payment of a final dividend of 3.91p per share (2007: 4.12p), to be paid on 16 February 2009, amounting to £5.3m (2007: £5.2m). Any shareholder wishing to participate in the Dividend Reinvestment Plan for the 2008 final dividend will need to ensure that their application form is returned to our registrars by 18 January 2009.

Directors

The directors of the company who served during the year are listed on page 39.

Directors' and other interests

The interests of the directors in the shares of the company at 30 September 2008 and 15 December 2008, with comparative figures as at 1 October 2007 (or date of appointment, if later), are as follows:

	Ordinary Shares of 5p each (thousands)					
	Beneficial			Non-beneficial		
	1 Oct 2007*	30 Sept 2008	15 Dec 2008	1 Oct 2007	30 Sept 2008	15 Dec 2008
Robin Broadhurst	5	**9**	26	–	**–**	–
Stephen Dickinson	3,461	**3,463**	3,464	2,386	**2,386**	2,386
Rupert Dickinson	1,420	**1,448**	1,449	207	**207**	207
Andrew Cunningham	498	**507**	508	–	**–**	–
Bill Tudor John	–	**–**	–	–	**–**	–
John Barnsley	14	**28**	46	–	**–**	–
Robert Hiscox	20	**30**	50	9,000	**9,000**	9,000
Henry Pitman	25	**26**	426	–	**–**	–
Baroness Margaret Ford**	–	**–**	–	–	**–**	–
	5,443	**5,511**	5,969	11,593	**11,593**	11,593

* or date of appointment, if later

** appointed 3 July 2008

Details of directors' share options are given on page 50.

Save as disclosed above, as at 28 November 2008, the company is aware of the following interests amounting to 3% or more in the company's shares:

	Holding 000's	Holding %
Schroder Investment Management Limited*	19,234	13.86
BlackRock Investment Management Ltd	7,950	5.73
Taube Hodson & Stonex Partners Ltd*	7,159	5.16
Standard Life Investments Ltd	4,694	3.38
Aberforth Partners*	4,499	3.24
Legal & General Investment Management Ltd*	4,162	3.00

* shares held by funds managed or advised by the company indicated and/or its subsidiaries. The company is not aware of any other substantial interests amounting to 3% or more

Directors' interests in significant contracts

No directors were materially interested in any contract of significance.

Insurance of directors

The group maintains insurance for Grainger plc's directors in respect of their duties as director.

Statement of directors' responsibilities

The directors are required by UK Company law to prepare financial statements for each financial year which give a true and fair view of the affairs of the company and the group as at the end of the financial year and of the profit or loss for that period and comply with the Companies Act 1985.

The directors are responsible for ensuring that applicable accounting standards have been followed and that suitable accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, have been used in the preparation of the financial statements for the year ended 30 September 2008.

The directors must also prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company and the group will continue in business.

The directors confirm that they have complied with the above requirements in preparing the financial statements.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and the group. They are also responsible for safeguarding the assets of the company and of the group, and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Creditor payment policy

It is the group's policy to pay suppliers in accordance with their normal terms and conditions of trading. Payment in respect of the purchase of property is subject to and will comply with contractual terms. Trade creditors existing at 30 September 2008 relating to purchases of property stock generally complete 28 days after exchange of contracts. Trade creditor days relating to other trade creditors of the company and group were calculated as 19 days (2007: 18 days).

Financial risk management

Details of this are included in note 26 to the financial statements.

Charitable donations

During the year the group made charitable donations amounting to £28,495 (2007: £71,283).

Health and safety

The company seeks to achieve the highest standards in respect of health and safety of employees, and the safety of tenants. Consultants are employed to ensure that the company complies with health and safety regulations and each year the gas supply and appliances within all of the group's relevant residential properties are independently inspected under the Gas Safety (Installation and Use) Amended Regulations 1996 and certificates of compliance issued. The group employs a full time health and safety manager.

DIRECTORS' REPORT

Employment of disabled persons

The company gives full and fair consideration to applications for employment made by disabled persons, having regard to their particular aptitudes and abilities. In the event of an employee becoming disabled every effort is made to ensure that their employment within the company continues and that appropriate training is arranged where necessary. It is the policy of the company that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

Employee involvement

The group places considerable value on the involvement of its employees and has continued its practice of keeping them informed on matters affecting them as employees, for example, eligibility to join company share schemes, and on the various factors affecting the performance of the group. Communication is made using the intranet, 'The Source', and through regular meetings with, and presentations by senior management.

Independent auditors and disclosure of information to auditors

As far as each director is aware, there is no relevant audit information of which the company's auditors are unaware. Each director has taken all steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

PricewaterhouseCoopers LLP have expressed their willingness to continue in office as auditors to the company and group. A resolution to reappoint them as auditors to the company will be proposed at the next Annual General Meeting.

Shares

As disclosed in note 32 to the financial statements, the company issued 59,709 5p ordinary shares for an aggregate consideration of £116,289 in the year under various employee share option schemes. The company also bought back 300,000 5p ordinary shares for total consideration of £982,444, which are being held in treasury. A further 497,088 5p ordinary shares were transferred out of treasury into an Employee Benefit Trust. At 30 September 2008, the directors had unexpired power to repurchase up to 12,804,110 shares.

Takeover directive

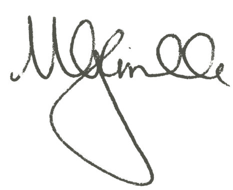
On a change of control, the club bank facilities (described in note 27 to the accounts) would become repayable had prior consent not been obtained, or the debt had not been renegotiated within 45 days. There are no other material matters relating to a change of control of the company following a takeover bid.

Post balance sheet events

Since the year end holders of £87.1m of Grainger's £112m 2014 Convertible Bond have accepted a cash payment of £35,000 per £100,000 nominal bond value to convert early. As a result 10,081,013 new shares have been issued.

On 4 December 2008, Grainger announced the completion of the sale of its Barnsbury development site for total cash consideration of £19m.

By order of the board



Marie Glanville ACA ACIS
Company secretary 16 December 2008

SHAREHOLDERS' INFORMATION

Financial calendar
Annual General Meeting 10 February 2009
Payment of 2008 final dividend 16 February 2009
Announcement of 2009 interim results May 2009
Payment of 2009 interim dividend June 2009
Announcement of 2009 final results November 2009

Share price
During the year ended 30 September 2008, the range of the closing mid-market prices of the company's ordinary shares were:

Price at 30 September 2008	200p
Lowest price during the year	187p
Highest price during the year	465p

Daily information on the company's share price can be obtained on our website or by telephoning: The Financial Times Cityline Service on 09068 432 750.

Capital gains tax
The market value of the company's shares for capital gains tax purposes at 31 March 1982 was 6.08p.

Website
Website address www.graingerplc.co.uk

Shareholders' enquiries
All administrative enquiries relating to shareholdings (for example, notification of change of address, loss of share certificates, dividend payments) should be addressed to the company's registrar at:

Capita IRG Plc
Northern House
Woodsome Park
Fenay Bridge
Huddersfield
West Yorkshire
HD8 0LA

Share dealing service
A share dealing service is available to existing shareholders to buy or sell the company's shares via Capita Share Dealing Services. Online and telephone dealing facilities provide an easy to access and simple to use service.

For further information on this service, or to buy or sell shares, please contact:
www.capitadeal.com – online dealing
0870 458 4577 – telephone dealing

Please note that the directors of the company are not seeking to encourage shareholders to either buy or sell their shares. Shareholders in any doubt as to what action to take are recommended to seek financial advice from an independent financial adviser authorised by the Financial Services and Markets Act 2000.

Secretary and registered office
Marie Glanville aca acis
Citygate
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Newcastle upon Tyne
NE1 4JE

Company registration number 125575

ADVISERS

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Financial public relations
Financial Dynamics
Holborn Gate
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London
NC2A 1PB

Corporate public relations
FD Tamesis
26 Southampton Buildings
London
WC2A 1PB

Bankers

Clearing Bank and Facility Agent
Barclays Bank PLC

Other bankers
Lloyds TSB Bank plc

The Royal Bank of Scotland plc

Allied Irish Banks plc

The Governor and Company of the Bank of Scotland

National Australia Bank Limited

Nationwide Building Society

Eurohypo AG

Hypo Real Estate Bank AG

The Governor and Company of the Bank of Ireland

GE Real Estate Finance Limited

Svenska Handelsbanken AB

SEB AG

Bayerische Hypo-und Verensbank AG

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Brewin Dolphin Securities
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NE1 4SR

Registrars and transfer office
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Tenay Bridge
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HD8 0LA

GLOSSARY OF TERMS

PROPERTY

Assured periodic tenancy ('APT')	Market-rented tenancy arising from succession from regulated. Tenant has security of tenure.
Assured shorthold tenancy ('AST')	Market-rented tenancy where landlord may obtain possession if appropriate notice served.
Assured tenancy ('AT')	Market-rented tenancy where tenant has right to renew.
Investment value ('IV') or market value	Open market value of a property subject to relevant tenancy in place.
Home reversion	Rent free tenancy where tenant has right of occupation until forfeited (usually on death). If tenant retains an equity interest in the property this is a partial home reversion.
PRS	Private rented sector.
Regulated tenancy	Tenancy regulated under 1977 Rent Act, rent (usually sub-market) set by rent officer and tenant has security of tenure.
Vacant possession ('VP') value	Open market value of a property free from any tenancies.

CORPORATE

Grainger NAV	NNNAV adjusted for the after tax value of the reversionary surplus in our regulated and equity release portfolios discounted back to present value using our risk adjusted weighted average cost of capital over the expected average period of realisation. Base case and sensitivities exist.
IFRS	International Financial Reporting Standards. Mandatory for UK-listed companies for accounting periods ending on or after 31 December 2005.

FINANCIAL

Cap	Financial instrument which, in return for a fee, guarantees an upper limit for the interest rate on a loan.
Contingent tax	The amount of tax that would be payable on the difference between the carrying value of trading properties as recorded in the balance sheet and their market value.
Dividend cover	Earnings per share divided by dividends per share.
Earnings per share ('EPS')	Profit attributable to equity shareholders divided by the weighted average number of shares in issue in the year.
Gearing	The ratio of borrowings, net of cash, to the market net asset value.
Goodwill	On acquisition of a company, the difference between the fair value of net assets acquired and the purchase price paid.
Grainger NAV	NNNAV adjusted for the taxed discounted reversionary surplus on regulated and home reversion portfolios.
Gross net asset value ('Gross NAV')	Shareholders' funds adjusted for the market value of property assets held as stock, and adding back deferred tax and before adjustments for the fair value of derivatives.
Hedging	The use of financial instruments to protect against interest rate movements.
IAS 39	Accounting standard containing complex rules for the recognition of the market value of long-term debt and financial instruments.
IFRS	International Financial Reporting Standards.
Interest cover	Profit on ordinary activities before interest and tax divided by net interest payable.
Loan to value ('LTV')	Ratio of net debt to the market value of properties.
Net net asset value (triple net or 'NNNAV')	Gross NAV adjusted for tax liabilities which would accrue if assets sold at market value and for the market value of long-term debt and derivatives.
Return on capital employed	Growth in NNNAV plus dividends paid per share as a percentage of opening NNNAV.
Return on shareholders' equity	Profit before financing costs plus all revaluation surpluses as a percentage of opening gross capital.
Swap	Financial instrument to protect against interest rate movements.
Total shareholder return ('TSR')	Return attributable to shareholders on basis of share price growth with dividends reinvested.
Weighted average cost of capital ('WACC')	The weighted average cost of funding the group's activities through a combination of shareholders' funds and debt.

CORPORATE ADDRESSES

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Grainger plc annual report and accounts for the year ended 30 September 2008

grainger figures

ACHIEVEMENTS OF THE YEAR

At Grainger, our dedicated management and staff have worked diligently in the very challenging conditions which existed during the year. As a result of these efforts, we are pleased to count the following amongst our achievements:

- ★ Operating profit up 19.1% to £106m (2007: £89m) before valuation and goodwill movements as a result of increased net rents and management fees
- ★ Sales from core and retirement solutions portfolios up 15% to £168m (2007: £146m)
- ★ New bank financing raised totalling circa. £228m
- ★ Our focus on cash conservation will continue by reducing property spend and overheads and increasing sales
- ★ Planning permission obtained for 1,550 new homes and 100,000 sq. m. of commercial space at Newlands Common, West Waterlooville
- ★ Successful tender offer for German residential company Francono Rhein-Main AG for €41.4m (£32.6m) creating critical mass in Germany

Grainger plc is the UK's largest listed residential landlord...

Financials

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF GRAINGER PLC ON THE GROUP FINANCIAL STATEMENTS

We have audited the group financial statements of Grainger plc for the year ended 30 September 2008 which comprise the consolidated income statement, the consolidated statement of recognised income and expense, the consolidated balance sheet, the statement of consolidated cash flows and the related notes. These group financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the parent company financial statements of Grainger plc for the year ended 30 September 2008 and on the information in the report of the remuneration committee and directors' remuneration report that is described as having been audited.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the group financial statements in accordance with applicable law and International Financial Reporting Standards ('IFRS') as adopted by the European Union are set out in the statement of directors' responsibilities.

Our responsibility is to audit the group financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the group financial statements give a true and fair view and whether the group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you whether in our opinion the information given in the directors' report is consistent with the group financial statements.

The information given in the directors' report includes that specific information presented in the chairman's statement and the chief executive's review that is cross-referenced from the review of business development and prospects section of the directors' report.

In addition we report to you if, in our opinion, we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We review whether the corporate governance report reflects the company's compliance with the nine provisions of the Combined Code (2006) specified for our review by the Listing Rules of the Financial Services Authority, 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 group financial statements. The other information comprises only the chairman's statement, the chief executive's review, the financial review, the corporate governance report, the directors' report, the corporate responsibility report and the unaudited part of the report of the remuneration committee and directors' remuneration report and the other items listed on both contents pages. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the group financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the group financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the group 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 group financial statements 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 group financial statements.

Opinion

In our opinion:

- the group financial statements give a true and fair view, in accordance with IFRS as adopted by the European Union, of the state of the group's affairs as at 30 September 2008 and of its loss and cash flows for the year then ended;
- the group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- the information given in the directors' report is consistent with the group financial statements.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London
16 December 2008

Note

The maintenance and integrity of the Grainger plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

CONSOLIDATED INCOME STATEMENT

For the year ended 30 September 2008	Notes	2008 £m	2007 £m
Group revenue		**246.2**	229.3
Net rental income	5	**37.7**	23.2
Profit on disposal of trading properties	6	**62.6**	62.8
Administrative expenses	8	**(6.2)**	(9.5)
Other income	9	**9.2**	6.2
Goodwill impairment	23	**(9.6)**	–
Profit on disposal of investment property	7	**0.6**	2.5
Profit on disposal of shares in subsidiary	10	**3.5**	2.0
Interest income from financial interest in property assets	21	**(0.9)**	1.8
Write down of inventories to net realisable value		**(12.3)**	–
Operating profit before net valuation (deficits)/gains on investment properties		**84.6**	89.0
Net valuation (deficits)/gains on investment properties	17	**(43.1)**	9.9
Operating profit after net valuation (deficits)/gains on investment properties		**41.5**	98.9
Change in fair value of derivatives	26	**(11.5)**	3.0
Interest expense	13	**(96.1)**	(74.4)
Interest income	13	**7.1**	9.4
Share of (loss)/profit of associates after tax	19	**(14.0)**	7.7
Share of (loss)/profit of joint ventures after tax	20	**(39.1)**	32.9
(Loss)/profit before tax	12	**(112.1)**	77.5
Taxation – current		**(5.7)**	(16.6)
Taxation – deferred		**40.4**	–
Tax credit/(charge) for the year	14	**34.7**	(16.6)
(Loss)/profit for the year		**(77.4)**	60.9
Attributable to:			
Equity holders of the company		**(77.4)**	61.0
Minority interest		**–**	(0.1)
		(77.4)	60.9
Basic (loss)/earnings per share	16	**(61.0)p**	47.3p
Diluted (loss)/earnings per share	16	**(61.0)p**	46.6p
Dividend per share	15	**6.18p**	6.18p

All of the above results relate to continuing operations.

CONSOLIDATED STATEMENT OF RECOGNISED INCOME AND EXPENSE

For the year ended 30 September 2008	Notes	2008 £m	2008 £m	2007 £m	2007 £m
(Loss)/profit for the year			**(77.4)**		60.9
Actuarial profit on BPT Limited defined benefit pension scheme net of tax	29	**0.3**		1.5	
Net exchange adjustments offset in reserves net of tax	34	**0.8**		0.3	
Changes in fair value of cash flow hedges net of tax	26	**(2.8)**		9.0	
Net (expense)/income recognised directly in equity			**(1.7)**		10.8
Total recognised income and expense for the year			**(79.1)**		71.7
Prior year adjustment – reclassification of equity release assets			**–**		(0.5)
Total recognised income and expense since last report			**(79.1)**		71.2
The total recognised income and expense in the year is attributable to:					
Equity shareholders of the parent			**(79.1)**		71.8
Minority interest			**–**		(0.1)
			(79.1)		71.7

CONSOLIDATED BALANCE SHEET

As at 30 September 2008	Notes	2008 £m	2007 £m
ASSETS			
Non-current assets			
Investment property	17	**619.3**	478.6
Property, plant and equipment	18	**2.3**	2.3
Investment in associates	19	**51.6**	68.5
Investment in joint ventures	20	**90.8**	114.8
Financial interest in property assets	21	**121.2**	131.7
Goodwill	23	**8.0**	17.4
		893.2	813.3
Current assets			
Inventories – trading properties	24	**1,142.2**	1,069.1
Trade and other receivables	25	**23.0**	16.4
Derivative financial instruments	26	**11.9**	13.1
Cash and cash equivalents	27	**43.2**	80.1
		1,220.3	1,178.7
Total assets		**2,113.5**	1,992.0
LIABILITIES			
Non-current liabilities			
Interest-bearing loans and borrowings	27	**1,635.4**	1,393.8
Trade and other payables	28	**4.0**	8.0
Retirement benefits	29	**2.1**	2.7
Provisions for other liabilities and charges	28	**1.0**	1.2
Deferred tax liabilities	14, 30	**78.4**	113.5
		1,720.9	1,519.2
Current liabilities			
Interest-bearing loans and borrowings	27	**17.9**	18.2
Trade and other payables	31	**80.1**	84.9
Current tax liabilities	14	**51.4**	45.8
Derivative financial instruments	26	**13.4**	0.8
		162.8	149.7
Total liabilities		**1,883.7**	1,668.9
Net assets		**229.8**	323.1

As at 30 September 2008	Notes	2008 £m	2007 £m
EQUITY			
Capital and reserves attributable to the company's equity holders			
Issued share capital	32, 34	**6.4**	6.4
Share premium	34	**23.1**	23.0
Merger reserve	34	**20.1**	20.1
Capital redemption reserve	34	**0.3**	0.3
Cash flow hedge reserve	34	**5.4**	8.2
Equity component of convertible bond	34	**22.4**	22.4
Retained earnings	34	**152.0**	242.6
Total shareholders' equity		**229.7**	323.0
Equity minority interests		**0.1**	0.1
Total equity	34	**229.8**	323.1

The financial statements on pages 4 to 64 were approved by the board of directors on 16 December 2008 and were signed on their behalf by:

Rupert Dickinson
Director

Andrew Cunningham
Director

STATEMENT OF CONSOLIDATED CASH FLOWS

For the year ended 30 September 2008	Notes	2008 £m	2007 £m
Cash flow from operating activities			
(Loss)/profit for the year		**(77.4)**	60.9
Depreciation	18	**0.8**	0.6
Impairment of goodwill	23	**9.6**	–
Net valuation deficits/(gains) on investment properties	17	**43.1**	(9.9)
Gain on acquisition of subsidiary		**(0.5)**	–
Net finance costs	13	**89.0**	65.0
Share of loss/(profit) of associates and joint ventures	19, 20	**53.1**	(40.6)
Profit on disposal of investment property	7	**(0.6)**	(2.5)
Profit on disposal of shares in subsidiary	10	**(3.5)**	(2.0)
Share-based payment charge	33	**0.5**	1.0
Change in fair value of derivatives	26	**11.5**	(3.0)
Interest income from financial interest in property assets	21	**0.9**	(1.8)
Taxation	14	**(34.7)**	16.6
Operating profit before changes in working capital		**91.8**	84.3
Decrease/(increase) in trade and other receivables		**2.9**	(12.1)
Decrease in trade and other payables		**(0.3)**	(1.9)
Increase in trading properties		**(79.4)**	(65.1)
Cash generated from operations		**15.0**	5.2
Interest paid		**(92.4)**	(66.1)
Taxation paid	14	**(0.2)**	(8.5)
Net cash outflow from operating activities		**(77.6)**	(69.4)
Cash flow from investing activities			
Proceeds from sale of investment property	7	**7.4**	14.8
Proceeds from financial interest in property assets		**9.5**	4.9
Disposal of subsidiary net of cash disposed of		**3.7**	251.0
Interest received		**3.8**	4.7
Dividends/distributions received	19, 20	**2.5**	8.0
Acquisition of subsidiaries, net of cash acquired	41	**(29.1)**	(146.5)
Investment in associates and joint ventures		**(11.0)**	(93.3)
Acquisition of investment property and property, plant and equipment		**(51.9)**	(100.9)
Acquisition of financial interest in property assets	21	**–**	(134.7)
Acquisition of minority interests		**(6.7)**	–
Net cash outflow from investing activities		**(71.8)**	(192.0)
Cash flows from financing activities			
Proceeds from the issue of share capital	34	**0.1**	0.5
Purchase of own shares including treasury shares	34	**(1.0)**	(14.8)
Proceeds from new borrowings		**131.4**	227.2
Issue of convertible bond net of costs		**–**	109.6
Repayment of borrowings		**(11.0)**	(12.1)
Dividends paid	15	**(8.1)**	(7.6)
Purchase of financial derivative		**–**	(0.3)
Net cash inflow from financing activities		**111.4**	302.5
Net (decrease)/increase in cash and cash equivalents		**(38.0)**	41.1
Cash and cash equivalents at beginning of year	27	**80.1**	39.0
Net exchange movements on cash and cash equivalents		**1.1**	–
Cash and cash equivalents at end of year	27	**43.2**	80.1

NOTES TO THE FINANCIAL STATEMENTS

1 Accounting policies

a) Basis of preparation

Grainger plc is a company incorporated and domiciled in the UK. It is a public limited liability company listed on the London Stock Exchange and the address of the registered office is given on page 74. The group financial statements consolidate those of the company and its subsidiaries, together referred to as the 'group', and equity account the group's interest in joint ventures and associates. The parent company financial statements present information about the company and not about its group.

The group financial statements have been prepared in accordance with EU endorsed International Financial Reporting Standards ('IFRS'), IFRIC interpretations and those parts of the Companies Act 1985 applicable to companies reporting under IFRS. The company has elected to prepare its company financial statements in accordance with UK GAAP. These are presented on pages 67 to 72.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in the group financial statements.

The group financial statements have been prepared under the historical cost convention except for the following assets and liabilities which are stated at their fair value; investment property, derivative financial instruments and financial interest in property assets.

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses. Although these estimates are based on management's best knowledge of the events and amounts involved, actual results ultimately may differ from those estimates. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in note 2.

b) Basis of consolidation

i Subsidiaries

Subsidiaries are all entities (including special purposes entities) over which the group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the group. They are de-consolidated from the date control ceases.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the group.

ii Goodwill and impairment

The purchase method of accounting is used to account for the acquisition of subsidiaries by the group. The cost of the acquisition is measured as the fair value of the assets given, equity instruments issued plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the date of acquisition. Goodwill represents the excess of the cost of an acquisition over the fair value of the group's share of net identifiable assets including intangible assets of the acquired entity at the date of acquisition. If the cost of the acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Goodwill on acquisition of subsidiaries is included in intangible assets. Goodwill on acquisition of joint ventures and associates is included in investments in joint ventures and associates.

NOTES TO THE FINANCIAL STATEMENTS

1 Accounting policies continued

Goodwill is allocated to cash-generating units for the purpose of impairment testing and is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

iii Joint ventures and associates

Joint ventures are those entities over whose activities the group has joint control, established by contractual agreement. Associates are all entities over which the group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights.

Investments in joint ventures and associates are accounted for by the equity method of accounting and are initially recognised at cost. The group's investment in joint ventures and associates includes goodwill (net of any accumulated impairment loss) identified on acquisition.

The group's share of its joint ventures' and associates' post-acquisition profits or losses is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment.

Unrealised gains on transactions between the group and its joint ventures and associates are eliminated to the extent of the group's interest in joint ventures and associates. The accounting policies of joint ventures and associates have been changed where necessary to ensure consistency with the policies adopted by the group.

iv Transactions with minority interests

The group applies a policy of treating transactions with minority interests as transactions with parties external to the group. Disposals to minority interests result in gains or losses for the group that are recorded in the income statement. On acquisition of minority interests, where the consideration paid exceeds the relevant share acquired of the carrying value of net assets of the subsidiary the difference is recorded in equity as a deduction from retained earnings.

c) Segmental reporting

The group's risks and rates of return are affected predominantly by differences between the property asset types it owns and manages. A business segment is a distinguishable group of assets and operations, reflected in the way that the group manages its business, that is subject to risks and returns that are different from those of other business segments.

The group has identified six such segments as follows:

- Core portfolio;
- Retirement solutions;
- Fund management/ residential investments;
- Development;
- European tenanted residential; and
- European Development.

All of the above segments are UK based except European tenanted residential which has its assets and tenants based in Germany and European development which has its assets based in the Czech Republic. More detail is given relating to each of the above segments, and their geographical split in the chief executive's review on pages 10 to 17 of the review section of this document and in note 4.

d) Foreign currency translation

i Functional and presentation currency

Items included in the financial statements of each of the group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in pounds sterling, which is the group's functional and presentation currency.

ii Foreign currency transactions

Foreign currency transactions are translated at the foreign exchange rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into sterling at the foreign exchange rate ruling at that date. Foreign exchange gains and losses resulting from the settlement of such transactions are recognised in the income statement.

iii Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to sterling at foreign exchange rates ruling at the balance sheet date. Revenues and expenses of foreign operations are translated at average foreign exchange rates for the relevant period.

Exchange differences arising from the translation of the net investment in foreign operations are taken to the translation reserve.

e) Investment property

Property that is held for long-term rental yields or for capital appreciation or both, and that is not occupied by the companies in the consolidated group, is classified as investment property.

Investment property is measured initially at its cost, including related transaction costs.

After initial recognition, investment property is carried at fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specified asset. If this information is not available, the group uses alternative valuation methods such as recent prices on less active markets or discounted cash flow projections.

Subsequent expenditure is included in the carrying amount of the property when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

Gains or losses arising from changes in the fair value of the group's investment properties are included in the income statement of the period in which they arise.

f) Property, plant and equipment

Property, plant and equipment is stated at historical cost less subsequent depreciation and impairment. Cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the assets' carrying amount or recognised as a separate asset, as appropriate, only when it is probable that the future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

Land is not depreciated. Depreciation on property, plant and equipment is calculated using the straight-line method to allocate their cost less residual values over their estimated useful lives, as follows:

Land	Nil
Fixtures, fittings and equipment	Five years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

g) Financial interest in property assets

Financial interest in property assets is initially recognised at fair value plus transaction costs and subsequently carried at fair value. Subsequent to initial recognition, the net change in value is recorded through the income statement as follows: i) the carrying value of the asset is increased by the effective interest rate and ii) the carrying value of the asset is revised to the net present value of the revised cash flows arising from the instrument using the effective interest rate applicable at acquisition. The change in value recorded through the income statement is shown on the line 'interest income from financial interest in property assets'.

Differences between the revised cash flows using the effective interest rate applicable at acquisition compared to revised cash flows using a year end effective interest rate, assessed as the rate available in the market for an instrument with a similar maturity and credit risk, are taken through equity. When gains or losses in the assets are realised, the accumulated fair value adjustments recognised in equity are included in the income statement as gains and losses from financial interest in property assets.

h) Inventories – trading properties

Tenanted residential properties held for sale in the normal course of business are shown in the financial statements at the lower of cost and net realisable value. Cost includes legal and surveying charges incurred during acquisition together with improvement costs. Net realisable value is the net sale proceeds which the group expects on sale of a property with vacant possession.

NOTES TO THE FINANCIAL STATEMENTS

1 Accounting policies continued

Land and property held within the development segment of the business, including house-building sites, are shown in the financial statements at the lower of cost and net realisable value. Cost represents the acquisition price including legal and other professional costs associated with the acquisition together with subsequent development costs net of amounts transferred to costs of sale. Net realisable value is the expected net sales proceeds of the developed property.

Where residential properties are sold tenanted or where land is sold without development, net realisable value is the current market value net of associated selling costs.

i) Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts.

j) Income tax

Income tax on the profits or losses for the periods presented comprises both current and deferred tax. Current tax is the expected tax payable on the taxable income for the year using rates applicable at the balance sheet date. Tax payable upon the realisation of revaluation gains recognised in prior periods is recorded as a current tax charge with a release of the associated deferred taxation.

Deferred income tax is provided using the balance sheet liability method. Provision is made for temporary differences between the carrying value of assets and liabilities in the consolidated financial statements and the values used for tax purposes. Deferred income tax is calculated after taking account of any indexation allowances and capital losses. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities and is calculated using rates enacted or substantially enacted at the balance sheet date in the tax jurisdiction in which the temporary differences arise.

Deferred income tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which the assets can be used. The deferred income tax assets and liabilities are only offset if there is a legally enforceable right of set off.

k) Employee benefits

i Defined contribution pension scheme

Obligations for contributions to defined contribution pension schemes are recognised as an expense in the income statement in the period to which they relate.

ii Defined benefit pension scheme

The group currently contributes to a defined benefit pension scheme that was closed to new members and employee contributions in 2003. The full deficit in the scheme was recognised in the balance sheet as at 1 October 2004.

An actuarial valuation of the scheme is carried out every three years. However, the valuation is updated annually by a qualified actuary for the purpose of determining the amounts to be reflected in the group's financial statements under IAS 19.

The liability recognised in the balance sheet is the present value of the defined benefit obligation at the balance sheet date less the fair value of scheme assets.

There are no current or past service costs as the scheme is closed to new members and employee contributions. Interest on pension scheme liabilities and the expected return on pension scheme assets will be reflected in the income statement each year. Actuarial gains and losses will be reflected in the consolidated statement of recognised income and expense each year.

iii Share-based compensation

The group operates a number of equity-settled, share-based compensation plans comprising awards under a long-term incentive scheme ('LTIS') and a save as you earn ('SAYE') scheme. The fair value of the employee services received in exchange for the grant of shares and options is recognised as an employee expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the shares and options granted, excluding the impact of any non-market vesting conditions. Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. At each balance sheet date, the group revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision to original estimates, if any, in the income statement with a corresponding adjustment to equity.

Awards that are subject to a market-based performance condition are valued at fair value using the Monte Carlo simulation model. Awards not subject to a market-based performance condition are valued at fair value using the Black Scholes valuation model.

When options are exercised the proceeds received net of any directly attributable transaction costs, are credited to share capital (nominal value) and share premium.

l) Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and is stated net of sales taxes and value added taxes. Revenue is recognised as follows:

i Rental and similar income

Rental income from operating leases is recognised on a straight-line basis over the lease term on an accruals basis.

ii Service charge and management fee income

Service charge and management fee income is recognised in the accounting period in which the services are rendered.

Other income is accounted for as follows:

i Income from property trading

Profits or losses arising from the sale of trading and investment property are included in the income statement where contract completion has taken place and are calculated by reference to their carrying value and are included in operating profit.

ii Income from investments

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

m) Leases

i Group as lessor

The net present value of ground rents receivable is, in the opinion of the directors, immaterial. Accordingly, ground rents receivable are taken to the income statement on a straight-line basis over the period of the lease. Properties leased out to tenants are included in the balance sheet as either investment property or as trading property under inventories.

Where the group grants a lifetime lease on an investment property and receives from the lessee an upfront payment in respect of the grant of the lease, the upfront payment is treated as deferred rent in the balance sheet. This deferred rent is released to the income statement on a straight-line basis over the projected term of the lease. At each year end the projected term of the lease is revised on an actuarial basis and the remaining deferred rent is released to the income statement on a straight-line basis over this revised lease term.

ii Group as lessee

The group occupies a number of its offices as a lessee. After a review of all of its occupational leases, the directors have concluded that all such leases are operating leases. Payments, including prepayments, made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period the lease.

The net present value of ground rents payable is, in the opinion of the directors, immaterial. Accordingly, ground rent expenses are taken to the income statement on a straight-line basis over the lease term.

n) Financial instruments

Derivatives

The group uses derivative instruments to help manage its interest rate risk. In accordance with its treasury policy, the group does not hold or issue derivatives for trading purposes.

The derivatives are recognised initially at fair value. Subsequently, the gain or loss on remeasurement to fair value is recognised immediately in the income statement, unless the derivatives qualify for cash flow hedge accounting in which case any gain or loss is taken to equity in a cash flow hedge reserve.

In order to qualify for hedge accounting, the group is required to document in advance the relationship between the item being hedged and the hedging instrument. The group is also required to demonstrate that the hedge will be highly effective on an ongoing basis. This effectiveness testing is reperformed at each period end to ensure that the hedge remains highly effective.

NOTES TO THE FINANCIAL STATEMENTS

1 Accounting policies continued

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecasted transaction is ultimately recognised in the income statement. When a forecasted transaction is no longer expected to occur, the cumulative gain or loss that was recognised in equity is immediately transferred to the income statement.

Fair value estimation

The fair value of interest rate swaps is based on a discounted cash flow model using quoted market information.

Derecognition of financial assets and liabilities

Derecognition is the point at which the group removes an asset or a liability from its balance sheet. The group's policy is to derecognise financial assets only when the contractual right to the cash flows from the financial asset expires. The group also derecognises financial assets that it transfers to another party provided the transfer of the assets also transfers the right to receive cash flows from the financial asset. When the transfer does not result in the group transferring the right to receive cash flows from the financial asset but it does result in the group assuming a corresponding obligation to pay cash flows to another recipient, the financial asset is derecognised.

The group derecognises financial liabilities only when its obligation is discharged, is cancelled or expires.

o) At fair value through profit or loss financial assets

At fair value through profit or loss financial assets are included in the balance sheet at fair value with changes in fair value taken through the income statement. At fair value through profit or loss financial assets are managed, and their performance is evaluated, on a fair value basis in accordance with the group's documented investment policy.

p) Borrowings

Borrowings are initially recognised at cost, being the fair value of consideration received, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

q) Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment in trade receivables is established when there is objective evidence that the group will not be able to collect all amounts due. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The movement in the provision is recognised in the income statement.

r) Trade payables

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

s) Provisions

Provisions are recognised when a) the group has a present obligation as a result of a past event and b) it is probable that an outflow of resources will be required to settle the obligation and c) a reliable estimate can be made of the amount of the obligation.

t) Dividends

Dividend distributions to the company's shareholders are recognised as a liability in the group financial statements in the period in which the dividends either are approved by the company's shareholders or are appropriately authorised and no longer at the discretion of the group.

u) Assets held for sale

Where a group of assets are to be disposed of by sale together or as a single group, they are classified as a disposal group. The disposal group is classified as held for sale as defined by IFRS 5 when they are available for sale in their present condition and the sale is highly probable and expected to be completed within one year from the date of classification.

v) Acquisition of and investment in own shares

The group acquires its own shares to enable it to meet its obligations under the LTIS. No gain or loss is recognised in profit or loss on the purchase, sale, issue or cancellation of the company's own shares. The acquisition cost of the shares is debited to an investment in own shares reserve within retained earnings. When shares are issued to employees under the LTIS, a transfer is made at the average cost of the shares issued between the investment in own shares reserve and the share-based payments reserve all within retained earnings (see note 34).

Where the group buys back its own shares as treasury shares it adopts the accounting as described above. Where it subsequently cancels them, issued share capital is reduced by the nominal value of the shares cancelled and this same amount is transferred to the capital redemption reserve.

w) Impact of standards and interpretations in issue but not yet effective

At the date of authorisation of these financial statements there are a number of standards, amendments and interpretations to existing standards that have been published but which are not yet effective and which have not been early adopted by the group. These are as follows:

- IFRS 8 'Operating Segments' (effective from 1 January 2009). IFRS 8 amends the current segmental reporting requirements of IAS 14 and aligns segment reporting with the requirements of the US standard SFAS 131. It requires a 'management approach' to be adopted so that segment information is presented on the same basis as that used for internal reporting purposes. This standard will apply to the group from 1 October 2009 and is expected to impact upon the group by requiring additional disclosures in the annual financial statements;
- Amendment to IAS 23 'Borrowing Costs' (effective from 1 January 2009). This amendment requires an entity to capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of the asset. A qualifying asset is one that takes a substantial period of time to get ready for use or sale. The option of immediately expensing these borrowing costs is removed. This amendment will apply to the group from 1 October 2009 and its impact is currently being assessed;
- Amendments to IFRS 3 'Business Combinations' (effective from I July 2009) and IAS 27 'Consolidated and Separate Financial Statements' (effective from 1 January 2009). The amendment to both of these standards is still subject to endorsement by the European Union. Some of the key changes are: i) the requirement to measure all consideration at fair value at acquisition date, with any subsequent changes (e.g. contingent consideration) remeasured at fair value through income; ii) the expensing of all transaction costs; and iii) stepped acquisitions to be accounted for as a disposal of existing interests and an acquisition of an enlarged interest, giving rise to potential profits or losses on disposal of the existing interest; and
- IFRIC 14 'IAS 19 – The limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction'. IFRIC 14 provides guidance on assessing the limit in IAS 19 on the amount of the surplus that can be recognised as an asset. It also explains how the pension asset or liability may be affected by a statutory or contractual minimum funding requirement. The group will apply IFRIC 14 from 1 October 2008 but it is not expected to have any impact on the group's accounts.

The following interpretations to existing standards have been published and are mandatory for the group's accounting periods beginning on or after 1 January 2008 or later periods but are not expected to have any material impact on the financial statements of the group:

- IFRIC 12 'Service Concession Arrangements'. IFRIC 12 applies to contractual arrangements whereby a private sector operator participates in the development, financing, operation and maintenance of infrastructure for public sector services. IFRIC 12 is not relevant to the group's operations as the group does not provide public sector services; and
- IFRIC 13 'Customer Loyalty Programmes'. IFRIC 13 clarifies that where goods or services are sold together with a customer loyalty incentive, the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. IFRIC 13 is not relevant to the group's operations because none of the group companies operate any loyalty programmes.

NOTES TO THE FINANCIAL STATEMENTS

2 Critical accounting estimates and assumptions

The group's significant accounting policies are stated in note 1 above. Not all of these accounting policies require management to make subjective or complex judgements or estimates. The following is intended to provide further detail relating to those accounting policies that management consider critical because of the level of complexity, judgement or estimation involved in their application and their impact on the consolidated financial statements.

Investment property valuations

The group, after review by the directors, used the valuations performed by its own in-house qualified surveying team to value its own UK-based residential investment property as at 30 September 2008. A structured sample of our in-house valuations was checked by Allsop LLP, an external independent valuer. Allsop LLP has provided the directors with the following opinion on the valuation of the group's UK investment property, "Investment property held in the core residential and retirement solutions portfolios with a value of £203.2m was valued as at 30 September 2008 by Grainger's in-house surveyors. These valuations were reviewed and approved by the directors. Allsop LLP has undertaken a comprehensive review of the director's valuation and they are satisfied with the process by which the in-house valuations were conducted. As part of the review, Allsop LLP valued approximately 50% of the core residential portfolio and approximately 33% of the retirement solutions portfolio, independently of the group. In view of the low volumes of recent market transactional evidence and the guidance to valuers under GN5 of the RICS Valuation Standards, Allsop LLP has stated to the directors that valuations of some individual dwellings may be subject to a higher than normal level of uncertainty. However, when taken in aggregate, and reported as such, Allsop LLP has concluded that the large sample size assists in the smoothing out of individual differences in value with the result that they have a high degree of confidence in the totals reported by the directors in the core and retirement solutions portfolios."

The net deficit on valuation of the core and retirement solutions portfolios as at 30 September 2008 was £34.5m and this has been taken through the income statement.

Investment property in the Germany portfolio with a value of €354.6m (£279.6m) has been valued by an external independent valuer, Cushman & Wakefield LLP as at 30 September 2008. Investment property with a value as at 30 September 2008 of £133.9m is held by FRM AG, a company acquired by the group on 4 April 2008. The last external valuation of the FRM portfolio was carried out as at 31 December 2007. However, the value of the portfolio has been reviewed by the directors as at 30 September 2008 and, in their opinion, the fair value was not materially different from the book value. Property assets with a fair value as at 30 September 2008 of £2.6m were valued by the directors.

The net deficit on valuation of investment property in the Germany portfolio as at 30 September 2008 was £8.6m and this has been taken through the income statement.

Whilst in the UK valuers rely predominantly on recent transactional evidence for similar properties to value investment property, in Germany investment property is valued using an income capitalisation approach under which net rental income is discounted to a net present value. Both methodologies are permitted under IAS 40.

The group also has investments in joint ventures and associates which include investment property. Investment property held in Grainger GenInvest LLP and Grainger GenInvest No.2 (2006) LLP, in both of which Grainger has a 50% share, were valued by an external valuer, Martin Angel FRICS, of Allsop LLP. He has provided the directors of those entities with the following opinion. "The valuations of the portfolios were made in accordance with the requirements of the RICS Valuation Standards sixth edition and International Valuation Standards. The valuation of each portfolio was on the basis of market value, subject to the assumption that the properties would be sold individually, in their existing condition, and subject to any existing leases or tenancies. In aggregate, across both entities, the valuation of the investment property was £283.2m. Allsop LLP is satisfied that, in respect of this valuation market value is the same as fair value. The valuers opinion of market value was primarily derived using comparable recent market transactions on arm's length terms.

2 Critical accounting estimates and assumptions continued

However, although there has been reasonable activity in the market for properties subject to Regulated Tenancies, there have been lower than usual volumes of recent market transactional evidence, in particular for vacant properties and properties subject to Assured Shorthold Tenancies. In line with the guidance to valuers under GN5 of the RICS Valuation Standards, Allsop LLP has stated to the directors that valuations of some individual dwellings may be subject to a lower level of confidence than is normal. However, when taken in aggregate, and reported as such, Allsop LLP has concluded that individual differences in value are likely to be smoothed out across the whole portfolio and would not materially affect our valuation".

The group has a 21.63% interest in G:res which has invested in investment property. Valuations of 100% of the G:res portfolio were carried out jointly as at 31 December 2007 and 30 June 2008 by external valuers, Allsop LLP and DTZ Debenham Tie Leung Limited. Within the valuations, blocks of flats have been valued on a block basis rather than as individual properties. As the current intention of G:res is to dispose of flats individually, valuation on an individual property basis is more in accordance with the requirements of IAS 40. Grainger has therefore estimated the uplift in value appropriate to a valuation on an individual property basis rather than a block basis for flats and has also made an assessment of the further downward movement in the market between 1 July and 30 September. It has concluded that its share of the net effect of these two adjustments is not material to the group accounts and therefore no adjustment has been made to the G:res valuation as at 30 June 2008.

The group has a 23.6% share in Schroders Residential Property Unit Trust (ResPUT). Investment property in this Fund was valued by Allsop LLP as at 30 September 2008.

Net realisable value of trading property

The group's residential trading properties are carried in the balance sheet at the lower of cost and net realisable value. In assessing net realisable value the group uses valuations carried out by its own in-house qualified surveying team. A structured sample of our in-house valuations was checked by Allsop LLP, an external independent valuer. Allsop LLP has provided the directors with the same opinion on the valuation of the group's UK trading property as they gave on the group's UK investment property (see above).

Valuing the large number of properties in our portfolio is a significant task and for this reason is undertaken on an external inspection basis only. Invariably, when our in-house valuations are compared to those of the external valuer, over 95% of the valuations are within a small acceptable tolerance. Where the difference is more significant we discuss this with the valuer to determine the reasons for the difference. Typically the reasons vary but it could be, for example, that further or better information about internal condition is available or that respective valuers have placed a different interpretation on comparable sales. Once such reasons have been identified we and the valuer agree the appropriate valuation that should be adopted.

As the group's business model is to sell trading stock on vacancy, net realisable value is the net sales proceeds which the group expects on sale of a property with vacant possession. A net realisable value provision of £2.7m has been made at 30 September 2008 to write down properties expected to be sold ultimately at vacant possession value. For properties expected to be held beyond the immediate future, this provision allows for some further decline in property prices but assumes that house prices will increase on average by 4% per annum over the 10-year period from 1 October 2007 to 30 September 2017. This is based on our review of various independent statistics which show that since 1979 the rolling 10-year average for house price inflation has not fallen below 4%. The group does sell some property as investment sales which is where the property is sold with the tenant still in situ. A net realisable value provision of £0.4m has been made at 30 September 2008 against projected investment sales.

Land and property held within the development segment of the business, including house-building sites, are shown in the financial statements at the lower of cost and net realisable value. Net realisable value is the expected net sales proceeds of the developed property and a provision is made when, and to the extent that, total projected project costs exceed total projected project revenues.

Where land is sold without development, net realisable value is the current market value net of associated selling costs.

Decisions regarding whether to develop a site or to sell a site undeveloped are made by the directors based on market conditions prevailing at the time. The assumptions adopted as at 30 September 2008 are based upon the current

NOTES TO THE FINANCIAL STATEMENTS

2 Critical accounting estimates and assumptions continued

intentions of the directors. In addition, estimates at 30 September 2008 of project profitability are based on assumptions regarding projected build costs and sales proceeds for those sites where development is expected to occur. In some cases these projections are made without the benefit of planning permission having been agreed. The assumptions made may or may not be borne out in practice. It is possible therefore that the net realisable value provision required should be more than or less than that made.

A charge of £9.2m has been made to the 2008 income statement to reduce the book value of development stock to net realisable value.

Valuation of financial interest in property assets

The valuation is based on an assessment of the future cash flows that will arise from our financial interest and on the effective interest rate used to discount those cash flows. The valuation methodology adopted is set out in note 1(g) above. The key assumptions affecting the carrying value are house price inflation and the effective interest rate.

The assumptions adopted with regard to house prices are the same as those set out under 'net realisable value of trading properties' above. A change of 1% to average house price inflation over the 10-year period from 1 October 2007 to 30 September 2017 would either increase the valuation by £5.3m or reduce the valuation by £4.9m.

We have considered the effective interest rate to adopt for valuation of our interest as at 30 September 2008. We have concluded that the effective interest rate on original recognition of the asset should also be used in the valuation as at 30 September 2008. A 1% change to the discount rate would either increase the carrying value by £9.7m or reduce the carrying value by £8.5m.

Distinction between investment and trading property

The group considers the intention at the outset when each property is acquired in order to classify the property as either an investment or a trading property. Where the intention is to either trade the property or where the property is held for immediate sale upon receiving vacant possession within the ordinary course of business, the property is classified as trading property. Where the intention is to hold the property for its long-term rental yield and/or capital appreciation, the property is classified as an investment property.

Income taxes

There are some transactions and calculations that involve a degree of estimation and judgement and whose tax treatment cannot be determined until a formal resolution has been reached with the relevant tax authorities. In such cases, the group's policy is to be prudent in its assessment of the tax benefit that may accrue in line with the contingent asset rules set out in IAS 37. Where the final outcome of these matters is different from the amounts initially recorded, such differences will impact on the income and deferred tax amounts reflected in subsequent accounting periods (see note 14).

Goodwill impairment

Goodwill can arise when a portfolio is acquired on the acquisition of a corporate entity accounted for as a business combination. The goodwill arises from the difference between how deferred tax is calculated for accounting purposes and the value ascribed to it in the acquisition negotiations. Generally, the value of goodwill is supported by the fact that the taxation cash flows will arise in future years and the discounted value of these cash flows is significantly less than the tax actually provided. The cash-generating unit for impairment testing is the portfolio acquired in the relevant entity and a goodwill impairment loss arises if the carrying amount of the portfolio exceeds the value in use which is determined as the present value of the future cash flows arising.

The goodwill impairment charge in the core business in 2008 relating to taxation as described above was £6.3m. The key sensitivities relating to the goodwill impairment testing are the discount rate used and the expected hold period for the assets concerned.

The discount rate used is the post-tax 2007 weighted average cost of capital of 6.38%, a post-tax rate as the cash flows being discounted are tax payments. A 1% increase in the discount rate would reduce the impairment charge by £0.7m whilst a 1% decrease would increase the impairment charge by £0.8m.

The hold periods used for the assets, and over which the cash flows have been discounted, are dependent upon the classification of assets between investment property and trading stock and the different property tenures. For instance, regulated properties are likely to be sold on vacancy whereas an assured shorthold property held as

2 Critical accounting estimates and assumptions continued

an investment property is more likely to be held for long-term investment gains and rental income. The hold periods used in the impairment calculations range from 10 years to 16 years with an average of 14.5 years. If the average hold period was changed by one year the impairment charge would either be reduced or increased by £0.3m

In addition to the above, goodwill of £3.3m arose in 2007 on the acquisition of the CAT portfolio in the retirement solutions business. The cash-generating unit is the CAT portfolio and a comparison has been made of the carrying value of this portfolio and the value in use based on the present value of future cash flows. The value in use does not support the carrying value of the goodwill and therefore it has been fully impaired in the 2008 income statement. The key sensitivity relating to the impairment charge is the discount rate used. A pre-tax discount rate of 9% has been adopted in the calculations. To support the full amount of goodwill would require a discount rate of 7.37% or less. To support any goodwill would require a discount rate of 8.06% or less.

Going concern

The directors are required to make an assessment of the group's ability to continue to trade as a going concern. Because of the difficult market conditions prevailing this assessment has been subject to more uncertainties than are usual. The directors have given this matter due consideration and have concluded that it is appropriate to prepare the group financial statements on a going concern basis. The two main considerations were as follows:

i Strength of the group's cash flow

The group has generated £213m of cash in 2008 from its net rents and other income, the sales of property and other working capital movements net of overhead costs. The nature of the group's property assets is that the majority are unmodernised and of relatively low average value. They are therefore generally affordable and provide the opportunity for a purchaser to maintain or increase value through refurbishment. These factors help the group to sustain demand when properties become vacant. In addition, properties can be sold without waiting for vacancy and these 'investment' sales assist the group in generating cash flows. The group has demonstrated, through the 15% increase in sales proceeds achieved in 2008 from its core and retirement solution portfolios, that it can sell assets even in more difficult market conditions.

ii Continued support of the group's banks

We maintain a regular and constructive dialogue with our banking syndicate and keep them informed of how the company is performing. Two important issues to consider in relation to our banks are the renewal of facilities and covenant compliance.

Facilities – At 30 September 2008 the group had headroom of £370m on its bank facilities, £303m of which was on the UK core facility. The first significant debt maturity is a facility of £400m due in June 2010 which is more than 12 months after the date of these financial statements. The headroom at 30 September 2008 represents 76% of this first debt maturity.

Covenant compliance – Our core facility has two covenants covering loan to value ('LTV') ratio and interest cover. Under the first, it is possible that a LTV of 80% could lead to default of the facility agreement. At 70% LTV purchasing restrictions apply although to a large extent the business is currently operating under the restrictions by reducing its expenditure on new acquisitions. LTV on the core facility was 66% at 30 September 2008 although this was reduced to 64% shortly after the year end by the early conversion of 78% of our convertible bond. We are able to take action to help keep the LTV ratio down, the main action being asset sales. We have estimated that if we are able to maintain sales proceeds in 2009 at the same level as achieved in 2008, then UK asset values as used for covenant purposes will have to fall by approximately 24% in the year ended 30 September 2009 for the 80% LTV level to be reached. This is before any other actions that management could take to improve the LTV position.

Under the second covenant test, our interest cost must be covered 1.25 times by net cash flow before interest. As at 30 September 2008 the ratio stood at 2.2 times. This covenant is calculated by reference to the previous 12 months results and, given the cash inflows that have already been achieved to date and our expectations in relation to sales to 30 September 2009 the directors are confident that, in the absence of unforseen circumstances, this covenant will be met at the next two testing points, 31 March 2009 and 30 September 2009.

NOTES TO THE FINANCIAL STATEMENTS

3 Analysis of (loss)/profit before tax

The results for the year have been significantly affected by valuation movements. The table below provides further analysis of the income statement showing the results of trading activities separately from valuation movements.

	2008			2007		
	Trading £m	Valuation £m	Total £m	Trading £m	Valuation £m	Total £m
Group revenue	**246.2**	**–**	**246.2**	229.3	–	229.3
Net rental income	**37.7**	**–**	**37.7**	23.2	–	23.2
Profit on disposal of trading properties	**62.6**	**–**	**62.6**	62.8	–	62.8
Administrative expenses	**(6.2)**	**–**	**(6.2)**	(9.5)	–	(9.5)
Other income	**8.7**	**0.5**	**9.2**	6.2	–	6.2
Goodwill impairment	**–**	**(9.6)**	**(9.6)**	–	–	–
Profit on disposal of investment properties	**0.6**	**–**	**0.6**	2.5	–	2.5
Profit on disposal of shares in subsidiary	**3.5**	**–**	**3.5**	2.0	–	2.0
Interest income from financial interest in property assets	**(0.9)**	**–**	**(0.9)**	1.8	–	1.8
Write down of inventories to net realisable value	**–**	**(12.3)**	**(12.3)**	–	–	–
Operating profit/(loss) before net valuation (deficits)/gains on investment properties	**106.0**	**(21.4)**	**84.6**	89.0	–	89.0
Net valuation (deficits)/gains on investment properties	**–**	**(43.1)**	**(43.1)**	–	9.9	9.9
Operating profit/(loss) after net valuation (deficits)/gains on investment properties	**106.0**	**(64.5)**	**41.5**	89.0	9.9	98.9
Change in fair value of derivatives	**–**	**(11.5)**	**(11.5)**	–	3.0	3.0
Interest expense	**(96.1)**	**–**	**(96.1)**	(74.4)	–	(74.4)
Interest income	**7.1**	**–**	**7.1**	9.4	–	9.4
Share of (loss)/profit of associates after tax	**0.2**	**(14.2)**	**(14.0)**	3.2	4.5	7.7
Share of (loss)/profit of joint ventures after tax	**(5.0)**	**(34.1)**	**(39.1)**	(2.0)	34.9	32.9
(Loss)/profit before tax	**12.2**	**(124.3)**	**(112.1)**	25.2	52.3	77.5

4 Segmental information

As at 30 September 2008 the group is organised into the six segments as set out in the tables below. All of the segments have their assets and undertake their business in the UK except European tenanted residential which has its assets and tenants in Germany and European development which has its assets and undertakes its business in the Czech Republic.

The group monitors its operations in the segments as shown in the tables following. There is no primary or secondary split and the above is a complete analysis by business and geographic segment.

4 Segmental information continued

2008 Income statement (£m)	Core portfolio	Retirement solutions	Fund management/ residential investments	Development	European tenanted residential	European development	Unallocated	Group total 30 September 2008
Group revenue	181.0	25.7	6.3	11.3	21.9	–	–	246.2
Net rental income	21.3	4.6	–	1.0	10.8	–	–	37.7
Profit on disposal of trading properties	58.4	7.3	–	(3.1)	–	–	–	62.6
Administrative expenses	3.6	–	(3.6)	–	–	–	(6.2)	(6.2)
Other income	2.4	–	6.3	–	0.5	–	–	9.2
Goodwill impairment	(6.3)	(3.3)	–	–	–	–	–	(9.6)
Profit on disposal of investment property	0.5	–	–	–	0.1	–	–	0.6
Profit on disposal of shares in subsidiary	–	–	–	–	–	3.5	–	3.5
Interest income from financial interest in property assets	–	(0.9)	–	–	–	–	–	(0.9)
Write down of inventories to net realisable value	(3.1)	–	–	(9.2)	–	–	–	(12.3)
Operating profit/(loss) before net valuation deficits on investment properties	76.8	7.7	2.7	(11.3)	11.4	3.5	(6.2)	84.6
Net valuation deficits on investment properties	(20.7)	(13.8)	–	–	(8.6)	–	–	(43.1)
Operating profit/(loss) – segment result	56.1	(6.1)	2.7	(11.3)	2.8	3.5	(6.2)	41.5
Change in fair value of derivatives								(11.5)
Interest expense								(96.1)
Interest income								7.1
Share of loss of associates after tax								(14.0)
Share of loss of joint ventures after tax								(39.1)
Loss before tax								(112.1)
Included in the above analysis are the following non-cash expenses:								
Depreciation	(0.6)	(0.1)	–	(0.1)	–	–	–	(0.8)
Share-based payments	(0.1)	(0.1)	–	(0.1)	–	–	(0.2)	(0.5)

Of the share of loss of associates after tax of £14.0m, a loss of £14.2m is attributable to fund management/residential investment and a profit of £0.2m is attributable to European development.

Of the share of loss of joint ventures after tax of £39.1m, £38.1m is attributable to fund management/residential investment, £0.8m is attributable to development and £0.2m is attributable to European development.

NOTES TO THE FINANCIAL STATEMENTS

4 Segmental information continued

2007 Income statement (£m)	Core portfolio	Retirement solutions	Fund management/ residential investments	Development	European tenanted residential	European development	Unallocated	Group total 30 September 2007
Group revenue	160.3	16.7	1.1	41.3	9.9	–	–	229.3
Net rental income	15.0	1.2	1.1	1.3	4.6	–	–	23.2
Profit on disposal of trading properties	59.2	4.8	–	(1.2)	–	–	–	62.8
Administrative expenses	4.6	–	(4.6)	–	–	–	(9.5)	(9.5)
Other income	0.6	–	5.3	0.2	0.1	–	–	6.2
Profit on disposal of investment property	1.6	–	0.1	0.4	0.4	–	–	2.5
Profit on disposal of shares in subsidiary	–	–	2.0	–	–	–	–	2.0
Interest income from financial interest in property assets	–	1.8	–	–	–	–	–	1.8
Operating profit/(loss) before net valuation gains on investment properties	81.0	7.8	3.9	0.7	5.1	–	(9.5)	89.0
Net valuation gains/(deficits) on investment properties	2.5	(1.5)	–	–	8.9	–	–	9.9
Operating profit/(loss) – segment result	83.5	6.3	3.9	0.7	14.0	–	(9.5)	98.9
Change in fair value of derivatives								3.0
Interest expense								(74.4)
Interest income								9.4
Share of profit of associates after tax								7.7
Share of profit of joint ventures after tax								32.9
Profit before tax								77.5
Included in the above analysis are the following non-cash expenses:								
Depreciation	(0.4)	(0.1)	–	(0.1)	–	–	–	(0.6)
Share-based payments	(0.2)	(0.1)	(0.2)	(0.1)	(0.1)	–	(0.3)	(1.0)

Of the share of profit of associates after tax of £7.7m, £6.5m is attributable to fund management/residential investment and £1.2m is attributable to European development.

Of the share of profit of joint ventures after tax of £32.9m, £29.6m is attributable to fund management/residential investment and £3.3m is attributable to development.

4 Segmental information continued

2008 Segment assets (£m)	Core portfolio	Retirement solutions	Fund management/ residential investments	Development	European tenanted residential	European development	Total 30 September 2008
Assets							
Investment property	104.2	99.0	–	–	416.1	–	619.3
Investment in associates	–	–	51.6	–	–	–	51.6
Investment in joint ventures	–	–	77.7	7.2	–	5.9	90.8
Financial interest in property assets	–	121.2	–	–	–	–	121.2
Goodwill	8.0	–	–	–	–	–	8.0
Inventories – trading properties	768.1	239.5	–	133.2	1.4	–	1,142.2
Trade and other receivables	2.8	0.7	9.4	1.4	1.9	2.8	19.0
Cash and cash equivalents	0.6	1.8	–	0.3	19.8	0.9	23.4
Total segment assets	883.7	462.2	138.7	142.1	439.2	9.6	2,075.5
Unallocated assets							
Property, plant and equipment							2.3
Derivative financial instruments							11.9
Trade and other receivables							4.0
Cash and cash equivalents							19.8
Total assets							2,113.5
Liabilities							
Interest-bearing loans and borrowings	–	38.0	–	–	301.4	–	339.4
Trade and other payables	4.3	32.4	–	18.7	13.3	0.9	69.6
Total segment liabilities	4.3	70.4	–	18.7	314.7	0.9	409.0
Unallocated liabilities							
Interest-bearing loans and borrowings							1,313.9
Trade and other payables							14.5
Retirement benefits							2.1
Current tax liabilities							51.4
Provisions for other liabilities and charges							1.0
Deferred tax liabilities							78.4
Derivative financial instruments							13.4
Total liabilities							1,883.7
Net assets							229.8
Other unallocated items							
Capital expenditure on property, plant and equipment	–	–	–	–	–	–	0.7

NOTES TO THE FINANCIAL STATEMENTS

4 Segmental information continued

2007 Segment assets (£m)	Core portfolio	Retirement solutions	Fund management/ residential investments	Development	European tenanted residential	European development	Total 30 September 2007
Assets							
Investment property	127.8	109.1	–	–	241.7	–	478.6
Investment in associates	–	–	67.5	–	–	1.0	68.5
Investment in joint ventures	–	–	108.0	6.8	–	–	114.8
Financial interest in property assets	–	131.7	–	–	–	–	131.7
Goodwill	14.1	3.3	–	–	–	–	17.4
Inventories – trading properties	753.7	210.8	–	98.2	–	6.4	1,069.1
Trade and other receivables	1.5	0.7	8.1	1.3	1.0	2.3	14.9
Cash and cash equivalents	1.6	7.3	–	0.1	4.9	0.7	14.6
Total segment assets	898.7	462.9	183.6	106.4	247.6	10.4	1,909.6
Unallocated assets							
Property, plant and equipment							2.3
Derivative financial instruments							13.1
Trade and other receivables							1.5
Cash and cash equivalents							65.5
Total assets							1,992.0
Liabilities							
Interest-bearing loans and borrowings	–	41.0	–	–	133.2	3.6	177.8
Trade and other payables	9.0	34.6	–	12.2	23.2	0.5	79.5
Total segment liabilities	9.0	75.6	–	12.2	156.4	4.1	257.3
Unallocated liabilities							
Interest-bearing loans and borrowings							1,234.2
Trade and other payables							13.4
Retirement benefits							2.7
Current tax liabilities							45.8
Provisions for other liabilities and charges							1.2
Deferred tax liabilities							113.5
Derivative financial instruments							0.8
Total liabilities							1,668.9
Net assets							323.1
Other unallocated items							
Capital expenditure on property, plant and equipment	–	–	–	–	–	–	0.8

5 Net rental income

	2008 £m	2007 £m
Gross rental income	**70.7**	52.7
Property repair and maintenance costs	**(19.9)**	(15.8)
Property operating expenses (see note 8)	**(13.1)**	(13.7)
	37.7	23.2

6 Profit on disposal of trading properties

	2008 £m	2007 £m
Proceeds from sale of trading properties	**162.2**	166.0
Carrying value of trading properties sold	**(88.8)**	(92.8)
Other sales costs (see note 8)	**(10.8)**	(10.4)
	62.6	62.8

7 Profit on disposal of investment property

	2008 £m	2007 £m
Proceeds from sale of investment property	**7.4**	14.8
Carrying value of investment property sold (see note 17)	**(6.8)**	(12.3)
	0.6	2.5

8 Administrative expenses

	2008 £m	2007 £m
Total group expenses	**30.1**	33.6

Many of the group's expenses relate directly to either property management activities or to staff involved directly with the sale and acquisition of property. Accordingly, total group expenses shown above have been allocated as follows:

	2008 £m	2007 £m
Property operating expenses (see note 5)	**13.1**	13.7
Costs attributable to the disposal of trading properties (see note 6)	**10.8**	10.4
Administrative expenses	**6.2**	9.5
	30.1	33.6

NOTES TO THE FINANCIAL STATEMENTS

9 Other income

	2008 £m	2007 £m
Property and asset management fee income	**7.0**	5.8
Crop store and agricultural income	**0.6**	0.4
Other sundry income	**1.1**	–
Gain on acquisition of subsidiary (note 41)	**0.5**	–
	9.2	6.2

The gain on acquisition of subsidiary represents the excess of the group's interest in the net fair value of Francono Rhein-Main AG's (FRM) identifiable assets, liabilities and contingent liabilities over the cost to the group. Further details relating to the acquisition of FRM are provided in note 41.

10 Profit on disposal of shares in subsidiary

	2008 £m	2007 £m
Sale of shares in CCZ a.s and Prazsky Project a.s.	**3.5**	–
Sale of shares in G:res1 Limited	**–**	2.0
	3.5	2.0

During the year, the group acquired an additional 3.4% of the equity of two companies incorporated in the Czech Republic, CCZ a.s. and Prazsky Project a.s. bringing the aggregate group holding to 85% in each company. The group then sold 35% of its equity holding in each company reducing its holding to 50% and making a profit on sale of equity of £3.5m. In 2007, the group disposed of 78.4% of its equity interest in G:res1 Limited and made a profit on sale of equity of £2.0m.

11 Employees

	2008 £m	2007 £m
Wages and salaries including termination benefits	**13.3**	14.6
Social security costs	**1.4**	1.5
Other pension costs – defined contribution scheme (see note 29)	**0.9**	0.8
Share-based payments	**0.5**	1.0
	16.1	17.9

The average monthly number of group employees during the year (including executive directors) was:

	2008 £m	2007 £m
UK tenanted residential	**273**	226
UK development	**15**	14
European tenanted residential	**12**	7
	300	247

Details of directors' remuneration, including pension costs, share options and interests in the LTIS are provided in the audited section of the remuneration committee report on pages 49 to 51 of the review section of this document which form part of these financial statements.

11 Employees continued

	2008 £m	2007 £m
Key management compensation		
Salaries and short-term employee benefits	**3.1**	4.5
Post-employment benefits	**0.3**	0.3
Share-based payments	**0.4**	0.8
	3.8	5.6

Key management figures shown above include the executive and the non-executive directors.

12 (Loss)/profit before tax

	2008 £m	2007 £m
(Loss)/profit before tax is stated after charging/(crediting):		
Depreciation on fixtures, fittings and equipment	**0.8**	0.6
Impairment of goodwill	**9.6**	–
Gain on acquisition of subsidiary	**(0.5)**	–
Bad debt expense	**0.9**	0.1
Foreign exchange gains	**(1.5)**	(0.4)
Operating lease payments	**1.5**	1.1
Auditors' remuneration – audit	**0.1**	0.1
Auditors' remuneration – non-audit	**0.4**	0.5

The remuneration paid to PricewaterhouseCoopers LLP, the group's principal auditors, is disclosed below:

Auditors' remuneration

	2008 £'000	2007 £'000
Audit fees		
Fees payable to the company's auditors for the audit of the parent company and consolidated financial statements	**136**	136
Non-audit fees		
The audit of the company's subsidiaries pursuant to legislation	**58**	45
Other service pursuant to legislation:		
Tax services	**145**	172
Other services	**166**	241
Total fees	**505**	594

Other services include transaction services of £163,000 (2007: £210,849).

Operating lease payments represent the lease payments made in the year relating to renting of office space used by the group, car leases under contract hire arrangements and operating lease payments relating to office equipment such as photocopiers. Leases relating to office space used by the group have initial terms of varying lengths, between five to 14 years.

Rent reviews generally take place every five years. Contract hire car leases generally have a three-year term. There are no other significant operating lease arrangements requiring disclosure under IAS 17. The group's operating lease commitments are shown in note 38.

NOTES TO THE FINANCIAL STATEMENTS

13 Interest

	2008 £m	2007 £m
Interest expense		
Bank loans and mortgages	**87.9**	69.5
Convertible bond	**6.9**	2.5
Loan notes	**0.8**	0.8
Other interest payable	**–**	0.5
Foreign exchange gains on financing activities	**(1.5)**	(0.4)
Amortisation of issue costs	**2.0**	1.3
Interest on net pension scheme liabilities	**–**	0.2
	96.1	74.4
Interest income		
Interest receivable from associates and joint ventures (see note 36)	**4.1**	6.3
Other interest receivable	**3.0**	3.1
	7.1	9.4
Net finance costs	**89.0**	65.0

14 Taxation

	2008 £m	2007 £m
Current tax		
UK corporation tax on profits	**11.6**	15.9
Adjustments relating to prior years	**(5.9)**	0.7
	5.7	16.6
Deferred tax		
Origination and reversal of timing differences	**(38.6)**	1.9
Adjustments relating to prior years	**(1.8)**	(1.9)
	(40.4)	–
Income tax (credit)/expense for the year	**(34.7)**	16.6

14 Taxation continued

Movements in taxation during the year are set out below:

	Opening balance £m	Payments in the year £m	Acquired in the year £m	Movements recognised in income £m	Exchange adjustments £m	Movements recognised in equity £m	Closing balance £m
Current tax	45.8	(0.2)	0.1	5.7	–	–	**51.4**
Deferred tax							
Trading property uplift to fair value on acquisition	67.5	–	–	(7.2)	–	–	**60.3**
Investment property revaluation	40.6	–	3.8	(24.5)	0.2	–	**20.1**
Accelerated capital allowances	2.1	–	–	0.1	–	–	**2.2**
Short-term timing differences	(0.2)	–	–	(8.6)	0.1	–	**(8.7)**
Actuarial surplus on BPT Limited pension scheme	0.8	–	–	(0.2)	–	0.1	**0.7**
Fair value movement in cash flow hedges and exchange adjustments	2.7	–	–	–	–	1.1	**3.8**
	113.5	–	3.8	(40.4)	0.3	1.2	**78.4**
Total tax – 2008 movement	159.3	(0.2)	3.9	(34.7)	0.3	1.2	**129.8**
Total tax – 2007 movement	128.3	(8.5)	19.4	16.6	–	3.5	**159.3**

The tax (credit)/charge for the year comprises:

	2008 £m	2007 £m
UK taxation	**(41.4)**	9.2
Overseas taxation	**6.7**	7.4
	(34.7)	16.6

The tax (credit)/charge for the year is lower than the standard rate of corporation tax in the UK of 29% (2007: 30%). The differences are explained below:

	2008 £m	2007 £m
(Loss)/profit before tax	**(112.1)**	77.5
(Loss)/profit before tax at a rate of 29% (2007: 30%)	**(32.5)**	23.3
Expenses not deductible for tax purposes	**2.1**	0.7
Goodwill impairment	**2.6**	–
Impact of tax rate change	**1.7**	(6.0)
Corporation tax on capital gains	**–**	7.4
Utilisation of current and prior period capital losses	**(10.6)**	(3.0)
Deferred tax released relating to capital gains	**–**	(6.3)
Other losses and non-taxable items	**–**	1.7
Adjustment in respect of prior periods	**2.0**	(1.2)
Total income tax (credit)/expense in the income statement (see above)	**(34.7)**	16.6

NOTES TO THE FINANCIAL STATEMENTS

14 Taxation continued

As detailed in note 30, deferred tax has been taken direct to equity in relation to the actuarial surplus on the BPT Limited pension scheme and the fair value movement in cash flow hedges and exchange adjustments.

Factors that may affect future tax charges

The group has not taken all of the benefit in relation to capital losses brought forward and available for offset against subsequent capital gains arising as this has yet to be formally agreed with the relevant tax authorities. If it is found that all the capital losses are available for offset against capital gains, then provisions of up to £16m would be released over the coming years.

15 Dividends

Under IAS 10, final dividends are excluded from the balance sheet either until they are approved by the company in general meeting or when they have been appropriately authorised and are no longer at the discretion of the group. Dividends paid in the year are shown below:

	2008 £m	2007 £m
Ordinary dividends on equity shares:		
Final dividend for the year ended 30 September 2007 – 4.12p per share	**5.2**	–
Final dividend for the year ended 30 September 2006 – 3.75p per share	**–**	4.9
Interim dividend for the year ended 30 September 2008 – 2.27p per share	**2.9**	–
Interim dividend for the year ended 30 September 2007 – 2.06p per share	**–**	2.7
	8.1	7.6

In addition to the above, a provision has been made in the accounts to 30 September 2008 of £0.2m for the payment of a dividend to the minority interest in FRM at a rate of €0.13 per share before tax. The payment of this dividend has been authorised by the management board of FRM and was approved by the Local Court of Frankfurt on 30 September 2008. The total dividend taken to equity in the year is therefore £8.3m (2007: £7.6m).

A final dividend relating to 2008 of 3.91p per share has been proposed by the board. If approved, this will result in a further distribution of £5.3m and it will be paid on 16 February 2009 to shareholders on the register on 9 January 2009. The 2008 interim dividend of 2.27p per share was paid in July 2008.

This gives a total dividend for 2008 of 6.18p per share, the same level as in 2007.

16 (Loss)/earnings per share

Basic

Basic (loss)/earnings per share is calculated by dividing the profit or loss attributable to equity holders of the company by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares purchased by the group and held both in trust and as treasury shares to meet its obligations under the long-term incentive scheme ('LTIS').

Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of shares outstanding by the dilutive effect of ordinary shares that the company may potentially issue relating to its convertible bond and its share option schemes and contingent share awards under the LTIS, based upon the number of shares that would be issued if 30 September 2008 was the end of the contingency period. The (loss)/profit for the year is adjusted to add back the after tax interest cost on the liability component of the convertible bond. Where the effect of the above adjustments is antidilutive, as is the case in 2008, they are excluded from the calculation of diluted (loss)/earnings per share.

16 Earnings per share continued

	30 September 2008			30 September 2007		
	Loss for the year £m	Weighted average number of shares (thousands)	Loss per share pence	Profit for the year £m	Weighted average number of shares (thousands)	Earnings per share pence
Basic (loss)/earnings per share						
(Loss)/profit attributable to equity holders	**(77.4)**	**126,720**	**(61.0)**	61.0	128,849	47.3
Effect of potentially dilutive securities						
Options and shares	**–**	**–**	**–**	–	752	(0.3)
Convertible bond	**–**	**–**	**–**	1.8	4,866	(0.4)
Diluted (loss)/earnings per share						
(Loss)/profit attributable to equity holders	**(77.4)**	**126,720**	**(61.0)**	62.8	134,467	46.6

17 Investment property

	2008 £m	2007 £m
Opening balance	**478.6**	219.4
Additions:		
Acquisitions	**23.9**	122.5
Subsequent expenditure	**4.4**	–
Business combinations	**131.9**	173.3
Disposals	**(6.8)**	(12.3)
Disposal as part of disposal of subsidiary	**–**	(209.8)
Net valuation (deficits)/gains	**(43.1)**	9.9
Exchange adjustments	**30.3**	7.3
Transfer from owner occupied property	**0.1**	–
Transfer from a disposal group	**–**	168.3
Closing balance	**619.3**	478.6

The group has valued all of its investment property as at 30 September 2008 at fair value.

Information relating to the basis of valuation of investment property, the use of external, independent, valuers and the judgements and assumptions adopted by management is set out in note 2 ‘Critical accounting estimates and assumptions’.

A revaluation deficit of £43.1m has arisen on valuation of investment property to fair value as at 30 September 2008 (2007: gain of £9.9m) and this has been taken to the income statement.

The historical cost of the group’s investment property as at 30 September 2008 is £605.7m (2007: £420.6m).

Rental income from investment property during the year was £31.9m (2007: £16.1m).

Direct property repair and maintenance costs arising from investment property that generated rental income during the year was £7.8m (2007: £4.2m).

Direct operating expenses arising from investment property that did not generate rental income during the year amounted to £0.1m (2007: £0.4m).

NOTES TO THE FINANCIAL STATEMENTS

18 Property, plant and equipment

	Fixtures fittings and equipment £m	Owner-occupied property £m	Total £m
Cost			
At 1 October 2007	4.7	0.1	4.8
Additions	0.7	–	0.7
Acquisition of subsidiary	0.2	–	0.2
Transfer to investment property	–	(0.1)	(0.1)
Disposals	(0.9)	–	(0.9)
At 30 September 2008	4.7	–	4.7
Depreciation			
At 1 October 2007	2.5	–	2.5
Charge for the year	0.8	–	0.8
Disposals	(0.9)	–	(0.9)
At 30 September 2008	2.4	–	2.4
Net book value			
At 30 September 2008	**2.3**	**–**	**2.3**
At 30 September 2007	2.2	0.1	2.3
Cost			
At 1 October 2006	3.9	0.1	4.0
Additions	0.8	–	0.8
At 30 September 2007	4.7	0.1	4.8
Depreciation			
At 1 October 2006	1.9	–	1.9
Charge for the year	0.6	–	0.6
At 30 September 2007	2.5	–	2.5
Net book value			
At 30 September 2007	**2.2**	**0.1**	**2.3**
At 30 September 2006	2.0	0.1	2.1

19 Investment in associates

	2008 £m	2007 £m
Opening balance	**68.5**	2.0
Loans repaid	**–**	(2.1)
Share of (losses)/profits	**(14.0)**	7.7
Distributions received	**(2.1)**	(0.6)
Share of change in fair value of cash flow hedges taken through equity	**(0.8)**	0.4
At fair value through profit or loss financial assets transferred to investment in associates (see note 22)	**–**	19.0
Net assets of G:res1 Limited transferred to investment in associates	**–**	88.3
Additional equity invested in G:res1 Limited	**–**	84.4
Sale of equity in G:res1 Limited	**–**	(130.6)
Closing balance	**51.6**	68.5

19 Investment in associates continued

As at 30 September 2008, the group's interest in associates was as follows:

	% of share capital/units held	Country of incorporation
G:res1 Limited	21.6	Jersey
Schroders Residential Property Unit Trust (ResPUT)	23.6	Jersey

In relation to the group's investment in associates, the group's share of the aggregated assets, liabilities, revenues and profit or loss are shown below:

	G:res1 Limited £m	ResPUT £m	OU Robbins £m	2008 £m	2007 £m
Non-current assets	81.7	16.9	–	**98.6**	114.3
Current assets	5.0	0.2	–	**5.2**	5.8
Non-current liabilities	(50.6)	–	–	**(50.6)**	(49.7)
Current liabilities	(1.6)	–	–	**(1.6)**	(1.9)
Net assets	34.5	17.1	–	**51.6**	68.5
Revenues	4.5	1.0	0.2	**5.7**	12.3
(Loss)/profit	(11.6)	(2.6)	0.2	**(14.0)**	7.7

20 Investment in joint ventures

	Net assets £m	Loans £m	Goodwill £m	Total £m
At 1 October 2006	12.2	57.7	1.6	71.5
Loans advanced	–	17.1	–	17.1
Share of profits	34.3	–	(1.4)	32.9
Share of change in fair value of cash flow hedges taken through equity	0.7	–	–	0.7
Distributions received	(7.4)	–	–	(7.4)
At 30 September 2007	39.8	74.8	0.2	114.8
Additions	2.3	–	–	2.3
Loans advanced	–	13.8	–	13.8
Share of losses	(39.1)	–	–	(39.1)
Goodwill impairment charge taken to income statement	–	–	(0.2)	(0.2)
Share of change in fair value of cash flow hedges taken through equity	(1.0)	–	–	(1.0)
Net assets of subsidiaries transferred to investment in joint ventures	0.6	–	–	0.6
Distributions received	(0.4)	–	–	(0.4)
At 30 September 2008	**2.2**	**88.6**	**–**	**90.8**

NOTES TO THE FINANCIAL STATEMENTS

20 Investment in joint ventures continued

At 30 September 2008, the group's interest in joint ventures was as follows:

	% of share capital held	Country of incorporation
Grainger GenInvest LLP	50	United Kingdom
Grainger GenInvest No 2 (2006) LLP	50	United Kingdom
Curzon Park Limited	50	United Kingdom
King Street Developments (Hammersmith) Limited	50	Czech Republic
CCZ a.s.	50	Czech Republic
CCY a.s.	50	Czech Republic
Prazsky Project a.s.	50	Czech Republic

In relation to the group's investment in joint ventures, the group's share of the aggregated assets, liabilities, revenues and profit or loss are shown below:

2008 Summarised income statement

	Grainger GenInvest LLP £m	Grainger GenInvest No.2 (2006) LLP £m	Czech Republic combined £m	Curzon Park Limited £m	2008 £m
Net rental income	**0.8**	**2.2**	**–**	**–**	**3.0**
Profit on disposal of investment property	**(0.1)**	**0.1**	**–**	**–**	**–**
Operating profit before valuation gains	**0.7**	**2.3**	**–**	**–**	**3.0**
Net valuation deficits on investment properties	**(9.8)**	**(24.3)**	**–**	**–**	**(34.1)**
Operating loss	**(9.1)**	**(22.0)**	**–**	**–**	**(31.1)**
Interest payable	**(2.4)**	**(4.6)**	**(0.2)**	**(0.8)**	**(8.0)**
Loss before tax	**(11.5)**	**(26.6)**	**(0.2)**	**(0.8)**	**(39.1)**
Taxation	**–**	**–**	**–**	**–**	**–**
Loss after tax	**(11.5)**	**(26.6)**	**(0.2)**	**(0.8)**	**(39.1)**

2008 Summarised balance sheet

	Grainger GenInvest LLP £m	Grainger GenInvest No.2 (2006) LLP £m	Czech Republic combined £m	Curzon Park Limited £m	2008 £m
Investment property	**39.0**	**102.6**	**–**	**–**	**141.6**
Current assets	**0.4**	**4.7**	**11.4**	**18.4**	**34.9**
Total assets	**39.4**	**107.3**	**11.4**	**18.4**	**176.5**
Non-current liabilities	**(34.7)**	**(105.3)**	**(4.7)**	**(12.0)**	**(156.7)**
Current liabilities	**(2.3)**	**(3.7)**	**(4.0)**	**(7.6)**	**(17.6)**
Net assets/(liabilities)	**2.4**	**(1.7)**	**2.7**	**(1.2)**	**2.2**

The results and financial position of the three Czech Republic companies have been aggregated in the above tables as individually they are not material and the development being undertaken in Prague is being managed as a single development with each company owning part of the combined site.

20 Investment in joint ventures continued

2007 Summarised income statement

	Grainger GenInvest LLP £m	Grainger GenInvest No.2 (2006) LLP £m	Regen (NT) LLP £m	Curzon Park Limited £m	2007 £m
Net rental income	1.3	3.8	–	–	5.1
Profit on disposal of trading property	–	–	5.1	–	5.1
Profit on disposal of investment property	1.5	1.1	–	–	2.6
Goodwill impairment	–	–	(1.4)	–	(1.4)
Operating profit before valuation gains	2.8	4.9	3.7	–	11.4
Net valuation gains on investment properties	9.1	22.3	–	–	31.4
Operating profit	11.9	27.2	3.7	–	42.8
Interest payable	(2.4)	(7.1)	–	(0.4)	(9.9)
Profit/(loss) before tax	9.5	20.1	3.7	(0.4)	32.9
Taxation	–	–	–	–	–
Profit/(loss) after tax	9.5	20.1	3.7	(0.4)	32.9

2007 Summarised balance sheet

	Grainger GenInvest LLP £m	Grainger GenInvest No.2 (2006) LLP £m	Regen (NT) LLP £m	Curzon Park Limited £m	2007 £m
Investment property	49.3	127.4	–	–	176.7
Current assets	0.3	4.7	0.4	20.9	26.3
Total assets	49.6	132.1	0.4	20.9	203.0
Non-current liabilities	(33.1)	(102.9)	–	(11.2)	(147.2)
Current liabilities	(2.4)	(3.5)	–	(10.1)	(16.0)
Net assets/(liabilities)	14.1	25.7	0.4	(0.4)	39.8

There is no tax charge on any profits made in the LLP companies as they are ‘transparent’ for tax. Any tax payable on Grainger’s share of the profits is included within the group tax charge.

21 Financial interest in property assets

	2008 £m	2007 £m
Opening balance	**131.7**	–
Additions	**–**	134.7
Cash received from the instrument	**(9.6)**	(4.8)
Amounts taken to income statement	**(0.9)**	1.8
Closing balance	**121.2**	131.7

Financial interest in property assets relates to the CHARM portfolio, which is a financial interest in equity mortgages. It is accounted for under IAS 39 in accordance with the designation available-for-sale financial assets.

Credit risk arises from the credit exposure relating to cash receipts from the financial instrument. All of the cash receipts are guaranteed by the Church Commissioners, a counterparty considered to be low risk as they have no history of past due or impaired amounts and there are no past due amounts outstanding at the year end.

NOTES TO THE FINANCIAL STATEMENTS

22 At fair value through profit or loss financial assets

	2008 £m	2007 £m
Opening balance	**–**	19.0
Transfer to investment in associates (see note 19)	**–**	(19.0)
Closing balance	**–**	–

In 2007, due to an increase in the group's percentage holding in the Schroder Residential Property Unit Trust, combined with an increased level of influence for the group arising from its engagement as property adviser to the Unit Trust, the group's investment, which had been classified as an at fair value through profit or loss financial asset, was transferred to investment in associates (see the 2007 comparative in note 19).

23 Goodwill

	2008 £m	2007 £m
Opening balance	**17.4**	–
Arising on acquisitions during the year	**–**	17.4
Impairment charge taken to income statement	**(9.4)**	–
Closing balance	**8.0**	17.4

Of the £8.0m (2007: £17.4m) of goodwill carried in the group's balance sheet, £8.0m (2007: £14.1m) relates to the UK core portfolio and £nil (2007: £3.3m) to the retirement solutions division.

The total goodwill impairment charge in the income statement comprises:

	2008 £m
Impairment charge as shown above	**(9.4)**
Impairment charge on goodwill shown within investment in joint ventures (see note 20)	**(0.2)**
	(9.6)

The gross carrying amount of goodwill and accumulated goodwill impairment losses as at 30 September 2008 were £24.0m and £16.0m respectively (2007: £24.0m and £6.4m respectively). Details of the impairment tests and charge are given in note 2.

24 Inventories – trading properties

	2008 £m	2007 £m
Residential trading properties	**1,009.0**	964.5
Development trading properties	**133.2**	104.6
	1,142.2	1,069.1

The market value of inventories as at 30 September 2008 was £1,519.1m (2007: £1,711.9m).

Write-downs to net realisable value and amounts written off book values in the year amounted to £12.3m (2007: £1.9m).

The cost of inventories recognised as an expense is shown in note 6 'Profit on disposal of trading properties' and amounted to £88.8m (2007: £92.8m).

25 Trade and other receivables

	2008 £m	2007 £m
Trade receivables	**11.1**	6.4
Less: Provision for impairment of trade receivables	**(1.2)**	(0.7)
Trade receivables – net	**9.9**	5.7
Other receivables	**11.2**	9.0
Prepayments	**1.9**	1.7
	23.0	16.4

The fair values of trade and other receivables are considered to be equal to their carrying amounts.

Other receivables includes a loan of £9.4m (2007: £7.0m) made to the Mornington Capital Special Situations Co-investment Fund 1 Limited Partnership. The loan has been used by the fund to invest in real estate joint venture partnerships. The loan bears interest at between 5% and 8% per annum above EURIBOR and is repayable within one year. The loan is secured by fixed and floating charges over the assets of the fund.

As at 30 September 2008, trade receivables of £1.2m were impaired and fully provided for (2007: £0.7m). The individually impaired receivables are based on a review of outstanding arrears and an assessment of collectability. The ageing of these receivables is:

	2008 £m	2007 £m
Up to two months	**0.1**	0.1
Three months or more	**1.1**	0.6
	1.2	0.7

Rental debtors are due on demand and hence all balances outstanding at the year end are past due. The balances within trade debtors which are past due but are not considered to be impaired, because we have either collected the debt since the balance sheet date or there is a history of regular payment, are as follows:

	2008 £m	2007 £m
Up to two months	**1.7**	1.0

The carrying amounts of the group's trade and other receivables are denominated in the following currencies:

	2008 £m	2007 £m
Pounds	**9.3**	8.4
Czech Koruna	**2.4**	0.2
Euros	**11.3**	7.8
	23.0	16.4

NOTES TO THE FINANCIAL STATEMENTS

25 Trade and other receivables continued

Movements on the group provision for impairment of trade receivables are as follows:

	2008 £m	2007 £m
Opening balance	**0.7**	1.0
Provision for receivables impairment during the year	**1.0**	0.2
Receivables written off during the period as uncollectible	**(0.4)**	(0.4)
Unused amounts reversed	**(0.1)**	(0.1)
Closing balance	**1.2**	0.7

The creation and release of provisions for impaired receivables have been included in property repair and maintenance costs in the consolidated income statement (note 5). Amounts provided for are written off when there is no expectation of recovering additional cash.

The other classes within trade and other receivables do not contain impaired assets.

The maximum exposure to credit risk at the reporting date is the carrying value of each class of receivables mentioned above. Tenant deposits of £0.7m (2007: £0.6m) are held which provide some security against rental arrears and property dilapidations caused by the tenant. In addition, the loan to Mornington is secured as described above. The group does not hold any other collateral as security.

26 Financial risk management and derivative financial instruments

Financial risk management

The group's objectives for managing financial risk are to minimise the risk of adverse effects on performance and to ensure the ability of the group to continue as a going concern while securing access to cost effective finance and maintaining flexibility to respond quickly to opportunities which arise.

The group's policies on financial risk management are approved by the board of directors and implemented by group treasury. Written policies and procedures cover interest rate risk, credit risk, the use of derivative and non-derivative financial instruments and investment of excess liquidity. Compliance is monitored by internal auditors. Group treasury reports to the risk committee.

The group uses derivative financial instruments to hedge its exposure to financial risk but does not take positions for speculative purposes.

The sources of financial risk and the policies and activities used to mitigate each are discussed below and include credit risk, liquidity risk and market risk which includes interest rate risk, foreign exchange risk, house price risk in relation to the CHARM portfolio, our financial interest in property assets, and capital risk.

26 Financial risk management and derivative financial instruments continued

Categories of financial instruments

A summary of the classifications of the financial assets and liabilities held by the group is set out in the following table:

	2008 Book value £m	2008 Fair value £m	2008 Fair value adjustment £m	2007 Book value £m	2007 Fair value £m	2007 Fair value adjustment £m
Financial interest in property assets	**121.2**	**121.2**	**–**	131.7	131.7	–
Trade and other receivables	**21.1**	**21.1**	**–**	14.7	14.7	–
Derivative financial instruments	**11.9**	**11.9**	**–**	13.1	13.1	–
Cash and cash equivalents	**43.2**	**43.2**	**–**	80.1	80.1	–
Total financial assets	**197.4**	**197.4**	**–**	239.6	239.6	–
Non-current liabilities						
Interest-bearing loans and borrowings	**1,635.4**	**1,644.8**	**9.4**	1,393.8	1,396.6	2.8
Trade and other payables	**4.0**	**4.0**	**–**	8.0	8.0	–
Provisions for other liabilities and charges	**1.0**	**1.0**	**–**	1.2	1.2	–
Current liabilities						
Interest-bearing loans and borrowings	**17.9**	**17.9**	**–**	18.2	18.2	–
Trade and other payables	**17.0**	**17.0**	**–**	30.6	30.6	–
Derivative financial instruments	**13.4**	**13.4**	**–**	0.8	0.8	–
Total financial liabilities	**1,688.7**	**1,698.1**	**9.4**	1,452.6	1,455.4	2.8
Total net financial liabilities	**1,491.3**	**1,500.7**	**9.4**	1,213.0	1,215.8	2.8

The fair value adjustment relates to the group's fixed rate loan with Lloyds TSB Bank plc and the liability component of the convertible bond, both of which are stated at amortised cost in the consolidated balance sheet. There is no requirement under IAS 39 to revalue these loans to fair value in the statutory balance sheet.

Credit risk

Credit risk is the risk of financial loss due to a counterparty's failure to honour its obligations. The group's principal financial assets include its financial interest in property assets, bank balances and cash, trade and other receivables and financial derivatives. The carrying amount of financial assets recorded in the financial statements represents the group's maximum exposure to credit risk without taking account of the value of any collateral obtained.

The group's financial interest in property assets relates to a financial interest in equity mortgages held by the Church Commissioners, a counterparty considered to be low risk as they have no history of past due or impaired amounts and there are no past due amounts outstanding at the year end.

The group's principal credit risk relates to trade receivables. Where it is identified that recovery is doubtful a provision for impairment is made. For all Assured Shorthold Tenancies credit checks are performed prior to acceptance of the tenant. Regulated tenants are incentivised through the benefit of their tenancy agreement to avoid default on their rent. Lifetime tenancies are generally at low or zero rent and hence suffer minimal credit risk. Rent deposits and personal guarantees are held in respect of some leases. Taking these factors into account the risk to the group of individual tenant default and the credit risk of trade receivables is considered low, as is borne out by the low level of trade receivables written off both in this year and in prior years.

NOTES TO THE FINANCIAL STATEMENTS

26 Financial risk management and derivative financial instruments continued

The credit risk on liquid funds and derivative financial instruments is managed through the group's policies of monitoring counterparty exposure, concentration of credit risk through the use of multiple counterparties and the use of counterparties of good financial standing. Cash and short-term deposits at 30 September 2008 amounted to £43.2m (2007: £80.1m). Deposits were placed with financial institutions with A- or better credit ratings.

At 30 September 2008, the fair value of all interest rate derivatives which had a positive value was £11.9m (2007: £13.1m). All the counterparties have investment grade credit ratings.

At 30 September 2008, the largest combined credit exposure to a single counterparty arising from money market deposits and interest rate swaps was £306.3m (2007: £280.5m) which represents 14.5% (2007: 14.1%) of total assets.

Liquidity risk

The group ensures that it maintains continuity and flexibility through a spread of maturities.

Although the group's core funding is supported by covenants requiring certain levels of loan to value with respect to the entities in the group of obligors and to maintaining a certain level of interest cover at the group level the loan is not secured directly against any property allowing operational flexibility. The group has comfortably complied with its covenants during 2008 and as at 30 September 2008 (see note 2 on page 19).

The group ensures that it maintains sufficient cash for operational requirements at all times. The group uses short-term money market deposits to manage its liquidity. The group also ensures that it has sufficient undrawn committed borrowing facilities from a diverse range of banks to allow for operational flexibility and to meet committed expenditure on its developments.

The core business in particular is very cash generative from its gross rents and sales of trading properties. In adverse trading conditions, new acquisitions can be stopped and, consequently, the group is able to reduce gearing levels and improve liquidity quickly.

The following table analyses the group's financial liabilities and net-settled derivative financial liabilities at the balance sheet date into relevant maturity groupings based on the remaining period to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. As the amounts included in the table are the contractual undiscounted cash flows, these amounts will not equal the amounts disclosed on the balance sheet for borrowings, derivative financial instruments, trade and other payables and provisions for liabilities and charges. A reconciliation to the balance sheet amounts is given on page 41. Trade and other payables due within 12 months equal their carrying balances as the impact of discounting is not significant.

The cash flows are calculated using yield curves for floating rate interest-bearing liabilities. Foreign currency related cash flows are calculated by means of the forward rates relevant to each maturity date.

	Less than 1 year £m	Between 1 and 2 years £m	Between 2 and 5 years £m	Over 5 years £m	Total £m
At 30 September 2008					
Interest-bearing loans and borrowings	**124.1**	**488.4**	**958.1**	**562.2**	**2,132.8**
Cash flow hedges	**(5.8)**	**(1.2)**	**(3.8)**	**8.8**	**(2.0)**
Trade and other payables	**51.0**	**–**	**4.0**	**–**	**55.0**
Provisions for liabilities and charges	**0.1**	**0.1**	**0.4**	**0.8**	**1.4**

	Less than 1 year £m	Between 1 and 2 years £m	Between 2 and 5 years £m	Over 5 years £m	Total £m
At 30 September 2007					
Interest-bearing loans and borrowings	111.5	94.4	988.9	736.8	1,931.6
Cash flow hedges	(4.7)	(2.3)	(4.4)	(2.2)	(13.6)
Trade and other payables	53.7	4.0	–	4.0	61.7
Provisions for liabilities and charges	0.1	0.1	0.4	1.0	1.6

26 Financial risk management and derivative financial instruments continued

Reconciliation of maturity analysis

	Less than 1 year £m	Between 1 and 2 years £m	Between 2 and 5 years £m	Over 5 years £m	Total £m
At 30 September 2008					
Interest-bearing loans and borrowings (see note 27)	**17.9**	**393.1**	**787.5**	**454.8**	**1,653.3**
Foreign exchange impact of forward rates	**0.7**	**0.4**	**2.2**	**36.3**	**39.6**
Interest	**105.5**	**91.5**	**164.9**	**67.2**	**429.1**
Unamortised borrowing costs	**–**	**3.4**	**3.5**	**3.9**	**10.8**
Financial liability cash flows shown above	**124.1**	**488.4**	**958.1**	**562.2**	**2,132.8**

	Less than 1 year £m	Between 1 and 2 years £m	Between 2 and 5 years £m	Over 5 years £m	Total £m
At 30 September 2007					
Interest-bearing loans and borrowings (see note 27)	18.2	5.0	783.6	605.2	1,412.0
Foreign exchange impact of forward rates	0.3	1.4	1.2	41.6	44.5
Interest	93.0	88.0	197.4	86.2	464.6
Unamortised borrowing costs	–	–	6.7	3.8	10.5
Financial liability cash flows shown above	111.5	94.4	988.9	736.8	1,931.6

The group's undrawn committed borrowing facilities are monitored against projected cash flows.

Maturity of committed undrawn borrowing facilities

	2008 £m	2007 £m
Expiring:		
Within one year	**46.8**	10.0
Between one and two years	**–**	41.4
Between two and five years	**296.0**	174.6
Total	**342.8**	226.0

The above facilities are those freely available to be drawn for group purposes.

Market risk

The group is exposed to market risk through interest rates, foreign exchange fluctuations, the availability of credit and house price movements relating to the CHARM portfolio. The approach the group takes to each of these risks is set out below. The group is not exposed to equity price risk nor to commodity price risk.

Fair values

The fair value of swaps and other financial instruments is derived from the present value of future cash flows discounted at rates obtained by means of the current yield curve appropriate for those instruments.

NOTES TO THE FINANCIAL STATEMENTS

26 Financial risk management and derivative financial instruments continued

The following financial instruments were in existence as at 30 September 2008:

	2008		2007	
	Assets	Liabilities	Assets	Liabilities
Interest rate swaps – cash flow hedges in hedge accounting relationships	**8.4**	**1.2**	9.5	0.1
Interest rate swaps – cash flow hedges not in hedge accounting relationships	**3.5**	**12.2**	3.6	0.7
	11.9	**13.4**	13.1	0.8

Interest rate swaps are all classified as either current assets or current liabilities.

The notional principal amount of the outstanding interest rate swap contracts as at 30 September 2008 was £1,228.3m (2007: £847.3m). As at 30 September 2008 the fixed interest rates vary from 3.43% to 6.0% (2007: 3.43% to 6.0%). The fair value movement relating to cash flow hedges not in hedge accounting relationships amounted to a charge of £11.5m (2007: credit of £3.0m).

All of the financial derivatives included in the above table were valued by external consultants, using a discounted cash flow model and quoted market information. They were checked internally using a bespoke software package.

In accordance with IAS 39, the group has reviewed its interest rate hedges. In the absence of hedge accounting, movements in fair value would have been taken directly to the income statement. However, where cash flow hedges have been viewed as being effective any gains or losses have been taken to equity through the cash flow hedge reserve.

A valuation was carried out at 30 September 2008 by external consultants, to calculate the market value of the group's fixed rate debt on a replacement basis, taking into account the difference between the fixed interest rates for the group's borrowings and the market value and prevailing interest rate of appropriate debt instruments as a fair value adjustment. The fair value compared to the carrying amounts of the group's fixed rate financial liabilities at 30 September 2008 is analysed below.

	Book value at 30 September 2008	Fair value at 30 September 2008
Fixed rate loan facilities	**153.6**	**163.0**

	Book value at 30 September 2007	Fair value at 30 September 2007
Fixed rate loan facilities	152.5	155.3

Interest rate risk

The group's interest rate risk arises from the risk of fluctuations in interest charges on floating rate borrowings. The group mitigates this risk through the use of variable to fixed interest rate swaps, caps and collars. This subjects the group to fair value risk as the value of the financial derivatives fluctuates in line with variations in interest rates. However, the group seeks to cash flow hedge account where applicable. The group is, however, driven by commercial considerations when hedging its interest rate risk and is not driven by the strict requirements of the hedge accounting rules under IAS 39 if this is to the detriment of achieving the best commercial arrangement.

Hedging activities are carried out under the terms of the group's hedging policies and are regularly reviewed by the board to ensure compliance with this policy. The board reviews its policy on interest rate exposure regularly with a view to establishing that it is still relevant in the prevailing and forecast economic environment. The current group treasury policy is to maintain floating rate exposure of no greater than 35% of expected borrowing. As at 30 September 2008, 85% (2007: 74%) of the group's net borrowings were economically hedged to fixed or capped rates.

26 Financial risk management and derivative financial instruments continued

As at 30 September 2008, the market value of derivatives designated as cash flow hedges under IAS 39, is a net asset of £7.2m (2007: £9.4m). The movement in fair value measured in the income statement on cash flow hedges in the year ended 30 September 2008 was a charge of £11.5m (2007: credit of £3.0m). At 30 September 2008, the market value of derivatives not designated as cash flow hedges under IAS 39, is a net liability of £8.7m (2007: asset of £2.9m). The cash flows occur and enter in the determination of profit and loss until the maturity of the hedged debt. The table below summarises debt hedged at 30 September 2008.

Cash flow hedged debt

	2008 £m	2007 £m
Cash flow hedges maturing:		
Within one year	**214.2**	0.1
Between one and two years	**227.4**	216.9
Between two and five years	**565.9**	407.0
Over five years	**220.8**	223.3
	1,228.3	847.3

Interest rate profile – including the effect of derivatives

	2008 Sterling £m	2008 Euro £m	2008 Total £m	2007 Sterling £m	2007 Euro £m	2007 Total £m
Fixed rate	**133.3**	**20.3**	**153.6**	134.3	18.2	152.5
Capped rate	**862.1**	**366.2**	**1,228.3**	712.1	135.1	847.2
Variable rate	**235.6**	**46.6**	**282.2**	354.2	68.6	422.8
	1,231.0	**433.1**	**1,664.1**	1,200.6	221.9	1,422.5

At 30 September 2008, the weighted average interest rate of the sterling fixed rate debt is 7.13% (2007: 7.09%). The weighted average period for which the rate is fixed is nine years (2007: 10 years). The weighted average interest rate of the euro fixed rate debt is 0.5% (2007: 0.5%). The weighted average period for which the rate is fixed is 42 years (2007: 43 years).

Based on the group's interest rate profile at the balance sheet date a 1% increase in interest rates would decrease annual profits by £3.3m (2007: £4.1m). Similarly a 1% decrease would increase annual profits by £5.3m (2007: £6.9m). This has been calculated to include the effect of hedge accounting.

Upward movements in medium and long-term interest rates, associated with higher interest rate expectation, increase the value of the group's interest rate swaps that provide protection against such moves. The converse is true for downward movements in the yield curve. Where the group's swaps qualify as effective hedges under IAS 39, these movements in fair value are recognised directly in equity rather than the income statement.

Foreign exchange risk

The group's foreign exchange risk arises from the exposure due to translating overseas trading performance and overseas net assets into sterling and it does not have foreign currency trading with cross border currency flows. The group hedges foreign currency assets naturally by funding them through borrowings in the applicable foreign currency and aims to ensure that it has no material unhedged net assets or liabilities denominated in a foreign currency. Profit translation is not hedged.

NOTES TO THE FINANCIAL STATEMENTS

26 Financial risk management and derivative financial instruments continued

The group's balance sheet translation exposure is summarised below:

	2008 Euro £m	2007 Euro £m	2008 Czech Koruna £m	2007 Czech Koruna £m
Gross foreign currency assets	**454.4**	257.5	**9.2**	8.8
Gross foreign currency liabilities	**(449.9)**	(245.2)	**–**	(3.9)
Net exposure	**4.5**	12.3	**9.2**	4.9

As at 30 September 2008 it is estimated that a general increase/decrease of 10 percentage points in the value of Sterling against the Euro would increase/decrease the group's profit before tax by approximately £1.2m (2007: £1.2m) and equity by £0.5m (2007: £1.2m).

As at 30 September 2008 it is estimated that a general increase/decrease of 10 percentage points in the value of Sterling against the Czech Koruna would increase/decrease the group's profit before tax by approximately £0.3m (2007: £0.1m) and equity by £0.9m (2007: £0.5m).

In 2007 the group also had an investment of £1m in Tallin. The sensitivities against movements in the Estonian Kroon are not considered material.

Credit availability risk

Credit availability risk relates to the group's ability to refinance its borrowings at the end of their terms or to secure additional financing where necessary. The group maintains relationships with a range of lenders and maintains sufficient headroom through committed borrowings.

House price risk

The cash flows arising from the group's financial interest in property assets (CHARM) are related to the movement in value of the underlying property assets and, therefore, are subject to movements in house prices. However, consistent with the group's approach to house price risk across its portfolio of trading and investment properties the group does not seek to eliminate this risk as it is a fundamental part of the group's business model.

At 30 September 2008 it is estimated that, with respect to the group's financial interest in property assets a general increase/(decrease) of one percentage point in house prices would increase/(decrease) the group's profit before tax by approximately £1m (2007: £1m).

Capital risk management

The board manages the group's capital through the regular review of: cash flow projections, the ability of the group to meet contractual commitments, covenant tests, dividend cover and gearing. The group manages the level of its equity shareholders funds by means of dividends, share purchases and share issues.

Loans within the group have associated covenant requirements with respect to loan to value and interest cover ratios. The board regularly reviews all covenants and projected future levels to monitor anticipated compliance and available headroom against key thresholds. For the group as a whole the board does not have a specific loan to value target but it is reviewed in the context of the board's view of markets, the prospects of and risks relating to the portfolio and the recurring cash flows of the business.

The group monitors its cost of debt and weighted average cost of capital ('WACC') on a regular basis. At 30 September 2008, the weighted average cost of debt was 6.17% (2007: 6.14%) and the WACC was 5.43% (2007: 6.38%). Investment and development opportunities are evaluated using the WACC in order to ensure long-term shareholder value is created.

Certain group subsidiaries are regulated by the Financial Services Authority and therefore have externally applied capital adequacy requirements, however, these do no have any material impact on the group as a whole.

27 Financial assets and liabilities

i Interest-bearing loans and borrowings

	2008 £m	2007 £m
Current liabilities		
Mortgages	**0.2**	0.2
Bank loans	**4.9**	1.8
Loan notes	**12.8**	16.2
	17.9	18.2
Non-current liabilities		
Mortgages	**20.1**	18.0
Bank loans	**1,524.2**	1,287.3
Convertible bond	**91.1**	88.5
	1,635.4	1,393.8
Total interest-bearing loans and borrowings	**1,653.3**	1,412.0

Costs relating to the raising of the loan finance set off against the balances shown in the above table amount to £10.8m (2007: £10.5m).

Analysis of bank loans

a) £1.3bn Multi Option Facility Agreement (the 'MOF')

	2008 £m	2007 £m
Term Facility A	**225.0**	225.0
Term Facility B	**200.0**	200.0
Revolving Facility A	**407.0**	475.0
Revolving Facility B	**245.0**	141.0
Revolving Facility B Euro	**148.2**	84.5
Total	**1,225.2**	1,125.5

Headroom on the MOF facility at 30 September 2008 was £302.8m (2007: £174.6m).

Interest is payable at the agreed margin over LIBOR plus mandatory costs. The agreed margin and final repayment date of the options are as follows:

	Margin %	Final repayment date
Facility		
Term Facility A	0.90	June 2013
Term Facility B	0.85	June 2014
Revolving Facility A	0.70	June 2011
Revolving Facility B	0.65	June 2010
Revolving Facility C	1.00	June 2013

The MOF is secured by floating charges over the assets of the group.

NOTES TO THE FINANCIAL STATEMENTS

27 Financial assets and liabilities continued

b) Other UK bank loans

	2008 £m	2007 £m
Fixed rate – Pounds Sterling	**40.0**	43.2
Variable rate – Pounds Sterling	**8.5**	10.0
	48.5	53.2

The fixed rate loan is secured by fixed charges over specific retirement solutions home reversion assets in the group's subsidiary company Hamsard 2517 Limited and bears interest at a fixed rate of 6.32%.

The variable rate loan is secured by fixed charges over specific investment property assets in The Tilt Estate Company Limited and bears interest at 0.9% above base rate.

c) European bank loans

	2008 £m	2007 £m
Bank loans – Euro	**264.6**	115.6
Bank loan – Czech Koruna	**–**	3.6
	264.6	119.2

Headroom on these facilities at 30 September 2008 amounted to £30.0m (2007: £41.4m).

The Euro bank loans are secured by floating and fixed charges over the investment property in the group's Germany portfolio. The loans bear interest at between 0.6% and 2.1% over EURIBOR.

d) Analysis of loan notes

	2008 £m	2007 £m
Fixed rate – Pounds Sterling	**0.6**	0.9
Floating rate – Pounds Sterling	**12.2**	15.3
	12.8	16.2

The fixed rate loan notes are secured by a bank guarantee and bear interest at a fixed rate of 3.25%.

The floating rate loan notes are secured by bank guarantees and cash collateral and bear interest at between 0.75% and 1% under LIBOR.

e) Mortgages

	2008 £m	2007 £m
Mortgages – Euro	**20.3**	18.2

The mortgages are secured by floating and fixed charges over the investment property in the group's Germany portfolio and bear interest at a fixed rate of 0.5%.

27 Financial assets and liabilities continued

f) Convertible bond

	2008 £m	2007 £m
Opening balance	**90.2**	–
Total fair value on initial recognition	**–**	112.0
Equity component of new issue	**–**	(22.4)
Amortised during the year	**2.5**	0.6
	92.7	90.2

A £112m 3.625% convertible bond due 2014 was issued in May 2007. Interest is payable semi-annually. Unless previously redeemed, converted, purchased or cancelled the bond is convertible at any time up to 12 May 2014 into fully paid up ordinary shares at a conversion price of £8.64. The convertible bond is a compound financial instrument and the carrying amount has been allocated to its equity and liability components in the group balance sheet. The liability component has been determined by measuring the fair value of a similar liability that does not have an associated equity component. The discount rate used for this was based on a rate of 7.5% compounded semi-annually. The liability component has been deducted from the fair value of the compound financial instrument as a whole and the residual element has been assigned to the equity component. The liability element is subsequently measured at amortised cost using the effective interest rate method.

Since the year end, holders of £87.1m of the £112m 3.625% 2014 convertible bond have accepted a cash payment of £35,000 per £100,000 nominal bond value to convert early (see note 40).

The analysis of the loans and borrowings in the above tables is before deducting unamortised issue costs relating to the raising of the loan finance.

Other loans and borrowings information

The MOF, variable rate UK bank loans and the European bank loans are generally rolled over every three months. At roll over, LIBOR, EURIBOR and PRIBOR are reset for the following interest period.

The fixed rate UK bank loan and the mortgages are at a fixed rate of interest which do not reprice. The fixed rate loan is repayable after more than five years. The mortgage has repayments of £0.3m within one year, £1.1m within two to five years and £18.9m after more than five years. The effective interest rate on borrowings was 6.2% (2007: 6.1%).

The maturity profile of the group's debt, net of finance costs, is as follows:

	2008 £m	2007 £m
Within one year	**17.9**	18.2
Between one and two years	**393.1**	5.0
Between two and five years	**787.5**	783.6
Over five years	**454.8**	605.2
	1,653.3	1,412.0

NOTES TO THE FINANCIAL STATEMENTS

27 Financial assets and liabilities continued

The interest rate risk profile of the group's debt after taking into account the various financial derivatives used by the group to manage its interest rate risk is as follows:

	2008			
	Fixed rate liabilities £m	Capped rate liabilities £m	Floating rate liabilities £m	Total £m
Loan notes	**0.6**	**–**	**12.2**	**12.8**
Mortgages – Euro	**20.3**	**–**	**–**	**20.3**
Convertible bond	**92.7**	**–**	**–**	**92.7**
Bank loans				
Pounds Sterling	**40.0**	**862.1**	**223.4**	**1,125.5**
Euro	**–**	**366.2**	**46.6**	**412.8**
	153.6	**1,228.3**	**282.2**	**1,664.1**
Unamortised issue costs				**(10.8)**
				1,653.3

	2007			
	Fixed rate liabilities £m	Capped rate liabilities £m	Floating rate liabilities £m	Total £m
Loan notes	0.9	–	15.3	16.2
Mortgages – Euro	18.2	–	–	18.2
Convertible bond	90.2	–	–	90.2
Bank loans				
Pounds Sterling	43.2	712.1	338.9	1,094.2
Euro	–	135.1	65.0	200.1
Czech Koruna	–	–	3.6	3.6
	152.5	847.2	422.8	1,422.5
Unamortised issue costs				(10.5)
				1,412.0

The group's borrowings subject to fixed interest rates and to swaps, caps and collars (capped rates) have the following weighted average interest rates and weighted average maturity dates. The weighted average interest rates shown are inclusive of loan margins.

27 Financial assets and liabilities continued

	2008			
	Fixed rate weighted average rate %	Weighted average period years	Capped rate weighted average rate %	Weighted average period years
Loan notes	**3.25**	**1**	**–**	**–**
Mortgages	**0.50**	**42**	**–**	**–**
Convertible bond	**3.63**	**6**	**–**	**–**
Bank loans – Pounds Sterling	**6.32**	**16**	**6.02**	**3**
Bank loans – Euro	**–**	**–**	**4.94**	**6**

	2007			
	Fixed rate weighted average rate %	Weighted average period years	Capped rate weighted average rate %	Weighted average period years
Loan notes	3.25	1	–	–
Mortgages	0.50	43	–	–
Convertible bond	3.63	7	–	–
Bank loans – Pounds Sterling	6.32	17	6.30	3
Bank loans – Euro	–	–	4.76	7

ii Financial assets

The group has the following cash and cash equivalents at 30 September 2008:

	2008 £m	2007 £m
Pounds Sterling	**33.4**	73.4
Euro	**8.9**	6.0
Czech Koruna	**0.9**	0.7
	43.2	80.1

Short-term deposits totalling £12.1m (2007: £14.7m) with an average maturity of three months are held as cash collateral. These have an effective interest rate of 5.51% (2007: 4.86%). Included within 2008 year end cash balances is £4m held in third-party client accounts where Grainger acts as Trustee or agent. The corresponding liability is included within trade creditors.

At the year end £4.7m (2007: £47.2m) was placed on the overnight money market at a rate of 4.35% (2007: £46.0m at a rate of 5.49% and £1.2m at a rate of 3.01%). Remaining cash and cash equivalents are held as cash at bank or in hand.

The group has an overdraft facility of £10m as at 30 September 2008 (2007: £10m).

NOTES TO THE FINANCIAL STATEMENTS

28 Non-current liabilities

	2008 £m	2007 £m
i Trade and other payables		
Trade and other payables	**4.0**	8.0

Trade and other payables is deferred consideration for the purchase of land at West Waterlooville and is payable in April 2013.

	2008 £m	2007 £m
ii Provisions for other liabilities and charges		
Other	**1.0**	1.2

29 Pension costs

Defined contribution scheme

The group operates a defined contribution pension scheme for its employees. The assets of the scheme are held separately from those of the group in independently administered funds. Pension arrangements for directors are disclosed in the report of the remuneration committee and the directors' remuneration report on page 49 of the review section of this document. The pension cost charge in these financial statements represents contributions payable by the group. This is shown in note 11.

Defined benefit scheme

In addition to the above, the group also operates a defined benefit pension scheme, the BPT Limited Retirement Benefits Scheme. The assets of the scheme are held separately in funds administered by trustees and are invested with an independent investment manager. Costs and funding are assessed with the advice of an independent qualified actuary using the projected unit credit method. Actuarial valuations are carried out every three years and the last full actuarial valuation was undertaken as at 1 July 2007. This scheme was operated by BPT Limited which became a subsidiary of Grainger plc in 2003.

The actuarial valuation as at 1 July 2007 was based on the main actuarial assumptions of an investment return of 6.8% per annum, salary increases of 4.9% per annum and inflation-linked increases to pensions in deferment of 3.4% per annum. The scheme assets were valued at £17.9m and scheme liabilities at £21.1m, a funding level of 85%. The funding level for the scheme at the previous valuation as at 1 July 2004 was 79%.The trustees and the employer have agreed a recovery plan to eliminate the deficit. This plan will run for seven years with company contributions to the scheme of £48,350 per month, £580,200 per annum. The actuary also undertook a Section 179 valuation as at 1 July 2007 as required by the Pension Protection Fund. The funding level on a Section 179 valuation basis was 142%.

The scheme was closed to new members and to employee contributions in 2003. Accordingly, there is no current service cost for the scheme.

The IAS 19 calculations for disclosure purposes have been based upon the 1 July 2007 actuarial valuation but have been updated to 30 September 2008 by a qualified independent actuary.

29 Pension costs continued

Pension cost recognised in the income statement

	2008 £m	2007 £m
Interest on pension scheme liabilities	**0.9**	0.9
Expected return on pension scheme assets	**(0.9)**	(0.7)
	–	0.2

The net pension cost shown above has been included within interest expense (see note 13).

The change in the present value of defined benefit obligation over the year was as follows:

	2008 £m	2007 £m
Present value of projected defined benefit obligation at start of the year	**16.7**	18.1
Interest on pension scheme liabilities	**0.9**	0.9
Actuarial gain	**(3.0)**	(2.0)
Benefits paid	**(0.7)**	(0.3)
Insurance policies	**3.4**	–
Present value of projected defined benefit obligation at end of the year	**17.3**	16.7

The change in the present value of the scheme assets over the year was as follows:

	2008 £m	2007 £m
Opening fair value of scheme assets	**14.0**	13.5
Expected return on scheme assets	**0.9**	0.7
Employer contributions	**0.2**	0.1
Actuarial loss	**(2.6)**	–
Benefits paid	**(0.7)**	(0.3)
Insurance policies	**3.4**	–
Closing fair value of scheme assets	**15.2**	14.0

The net actuarial gain shown in the above tables of £0.4m (2007: £2.0m) net of tax has been included in the consolidated statement of recognised income and expense (see page 5).

Defined benefit obligations, scheme assets and scheme deficit

	2008 £m	2007 £m	2006 £m	2005 £m	2004 £m
Total market value of assets	**15.2**	14.0	13.5	12.1	10.7
Present value of scheme liabilities	**(17.3)**	(16.7)	(18.1)	(17.4)	(15.3)
Scheme deficit at 30 September	**(2.1)**	(2.7)	(4.6)	(5.3)	(4.6)

The scheme deficit of £4.6m, net of deferred tax, was taken into the opening IFRS balance sheet as at 1 October 2004.

NOTES TO THE FINANCIAL STATEMENTS

29 Pension costs continued

Actuarial gain recognised in the consolidated statement of recognised income and expense

	2008 £m	2007 £m
Actual return less expected return on assets	**(2.6)**	–
Experience gain on liabilities	**1.3**	–
Gain on change of assumptions	**1.7**	2.0
Total actuarial gain before tax	**0.4**	2.0

Market value of scheme assets and expected rates of return

	30 September 2008		30 September 2007	
	Market value £m	Long-term expected rate of return %	Market value £m	Long-term expected rate of return %
Equities	**5.0**	**7.3%**	6.3	7.6%
Bonds	**6.5**	**5.5%**	6.8	5.3%
Properties	**0.3**	**7.3%**	0.4	7.6%
Other	**–**	**5.0%**	0.5	5.8%
Insurance policies	**3.4**	**7.0%**	–	–
Total value of assets	**15.2**		14.0	

The assets of the scheme are held with AXA Sun Life in a managed fund. As the above table shows, the assets of the scheme are primarily held within equities and bonds. The equity return of 7.3% in 2008 and 7.6% in 2007 is based on an equity risk premium of 2.6% above the 15-year fixed rate on gilts. The directors consider this to be at the mid point of the acceptable range. The return on bonds has been determined by reference to actual yields.

Principal actuarial assumptions under IAS 19

	2008	2007
Discount rate	**7.00% p.a.**	5.90% p.a.
Inflation	**3.60% p.a.**	3.40% p.a.
Rate of increase in salaries	**5.10% p.a.**	4.90% p.a.
Rate of increase in pensions in payment	**5.00% p.a.**	5.00% p.a.
Mortality tables for pensioners	**107% of PCMA00 year of birth tables allowing for long cohort improvements with 1.25% minimum improvements for males and 0.75% minimum improvements for females each year**	PXA92c2025*
Mortality tables for non-pensioners	**As for pensioners**	As for pensioners

* after allowing for short cohort effect

The mortality assumption has been updated to be the same as that used in the actuarial valuation as at 1 July 2007. The resulting life expectancy for a future male pensioner currently aged 55 is 89.5 years (2007: 86.2 years), and for a future female pensioner aged 55 is 91.1 years (2007: 89.1 years). The life expectancy for a current male pensioner is 88.7 years (2007: 85.9 years), and for a current female pensioner is 90.7 years (2007: 88.7 years).

29 Pension costs continued

History of experience gains and losses

	2008	2007	2006	2005	2004
Difference between the expected and the actual return on scheme assets:					
Amount	**£(2.6)m**	–	£0.6m	£0.8m	(£0.9)m
Percentage of scheme assets	**(17.1)%**	–	4.2%	6.6%	(8.4)%
Experience gains and losses on scheme liabilities:					
Amount	**£1.3m**	–	–	£0.9m	(£0.5)m
Percentage of present value of liabilities	**7.5%**	–	–	5.2%	(3.3)%

Set out below is an analysis of how the scheme deficit would vary with changes to the key actuarial assumptions:

Discount rate increased by 0.1%	decrease in deficit of £0.2m
Inflation increased by 0.1%	increase in deficit of £0.1m
Life expectancies increased by one year	increase in deficit of £0.4m

The actual returns on scheme assets in 2008 was a loss of £1.7m (2007: a gain of £0.7m). The cumulative amount of actuarial gains recognised in the consolidated statement of recognised income and expense before taxation is £2.3m (2007: £1.9m).

Payments to the scheme in 2008

The group expects to make payments to the scheme in 2008 based on the recovery plan agreed with the scheme trustees. Contributions in the next 12 months are estimated at £580,200.

30 Deferred tax liabilities

The movement in the provision for deferred taxation is as follows:

	2008 £m	2007 £m
Opening balance	**113.5**	91.1
Acquisition of subsidiaries in the year	**3.8**	18.9
Recognised in the income statement	**(40.4)**	–
Recognised in equity:		
Actuarial surplus on BPT pension scheme	**0.1**	0.6
Fair value movement in cash flow hedges and exchange adjustments	**1.1**	2.9
Exchange adjustments	**0.3**	–
Closing balance	**78.4**	113.5

In addition to the above, the group has a contingent tax liability representing the difference between the carrying value of trading properties in the balance sheet and their market value. This contingent tax, which is not provided in the accounts, amounts to £104.5m (2007: £176.7m).

NOTES TO THE FINANCIAL STATEMENTS

31 Trade and other payables

	2008 £m	2007 £m
Deposits received	**0.7**	0.6
Trade payables	**15.8**	29.7
Other taxation and social security	**0.5**	0.3
Accruals and deferred income	**63.1**	54.3
	80.1	84.9

Trade payables includes £0.6m (2007: £23.6m) relating to acquisitions of property where contracts have either been unconditionally exchanged or notarised.

Accruals and deferred income includes £29.1m (2007: £31.2m) of rent received in advance relating to lifetime leases.

32 Share capital

	2008 £m	2007 £m
Authorised		
160,000,000 (2007: 160,000,000) ordinary shares of 5p each	**8.0**	8.0
Allotted, called-up and fully paid		
128,716,094 (2007: 128,656,385) ordinary shares of 5p each	**6.4**	6.4

Grainger plc acquired 300,000 of its own shares on 10 January 2008. The total amount paid to acquire the shares was £1.0m and has been deducted from retained earnings within shareholders' equity (see note 34). These shares are held as treasury shares.

As at 30 September 2008, share capital included 584,673 (2007: 584,673) shares held by The Grainger Trust Employee Trustee Company Limited, 1,017,088 (2007: 520,000) shares held by The Grainger Employee Benefit Trusts and 452,912 (2007: 650,000) shares held by Grainger plc as treasury shares. The total of these shares is 2,054,673 (2007: 1,754,673) with a nominal value of £102,734 (2007: £87,734).

Movements in issued share capital during the year and the previous year were as follows:

	Number	Nominal value £'000
At 1 October 2006	129,925,482	6,496
Options exercised under the executive share option scheme	63,645	3
Options exercised under the LTIS scheme	74,586	4
Options exercised under SAYE schemes	117,672	6
Treasury shares bought back and cancelled	(1,525,000)	(76)
At 30 September 2007	128,656,385	6,433
Options exercised under the LTIS scheme	11,307	1
Options exercised under SAYE schemes	48,402	2
At 30 September 2008	**128,716,094**	**6,436**

32 Share capital continued

Share options

Certain senior executives hold options to subscribe for shares in the company under long-term incentive schemes. In addition, the company operates a SAYE share option scheme available to employees. The number of shares subject to options as at 30 September 2008, the periods in which they were granted and the periods in which they may be exercised are given below:

Year of grant	Exercise price (pence)	Exercise period	2008 number	2007 number
Long-term incentive scheme ('LTIS')				
2003	191.8	2006-13	**52,586**	63,893
2005	381.8	2008-15	**–**	370,525
2006	528.0	2009-16	**313,445**	313,445
2007	640.9	2010-17	**14,040**	14,040
			380,071	761,903
SAYE share options				
2002	163.6	2005-08	**–**	10,115
2003	186.5	2006-09	**25,615**	58,060
2004	271.8	2007-10	**6,250**	29,655
2005	334.0	2008-11	**18,796**	39,702
2006	413.0	2009-12	**3,527**	65,798
2007	454.3	2010-13	**1,745**	65,592
2008	167.8	2011-14	**612,351**	–
			668,284	268,922
Total share options			**1,048,355**	1,030,825

NOTES TO THE FINANCIAL STATEMENTS

32 Share capital continued

The movement on the share options schemes during the year is as follows:

	Opening position	Exercised	Granted	Lapsed	Closing position
LTIS schemes					
2003	63,893	(11,307)	–	–	52,586
2005	370,525	–	–	(370,525)	–
2006	313,445	–	–	–	313,445
2007	14,040	–	–	–	14,040
	761,903	(11,307)	–	(370,525)	380,071
Weighted average exercise price (pence per share)	430.8p	191.8p	–	381.8p	485.7p
SAYE scheme					
2002	10,115	(10,115)	–	–	–
2003	58,060	(31,173)	–	(1,272)	25,615
2004	29,655	(6,160)	–	(17,245)	6,250
2005	39,702	(954)	–	(19,952)	18,796
2006	65,798	–	–	(62,271)	3,527
2007	65,592	–	–	(63,847)	1,745
2008	–	–	612,351	–	612,351
	268,922	(48,402)	612,351	(164,587)	668,284
Weighted average exercise price (pence per share)	337.6p	195.5p	167.8p	402.9p	176.2p

For those share options exercised during the year, the weighted average share price at the date of exercise was 350.9p (2007: 610p).

For share options outstanding at the end of the year, the weighted average remaining contractual life is 2.60 years (2007: 1.17 years).

There were 96,404 share options exercisable at the year end with a weighted average exercise price of 217.2p.

Further details of the above option schemes is provided in the report of the remuneration committee and directors' remuneration report on pages 45 to 51 of the review section of this document which forms part of these financial statements.

33 Share-based payments

The group operates an equity-settled, share-based compensation plan comprising awards under a long-term incentive scheme ('LTIS') and a save as you earn ('SAYE') scheme.

Awards under the LTIS for 2006 and prior are subject to market performance conditions under which the total shareholder return ('TSR') of the company is measured against a peer group. There is no vesting below median performance. If the company TSR equals the median of the peer group 40% will vest. If the group's TSR is equal to or greater than the upper quartile TSR of the peer group, 100% will vest. At points between the median and upper quartile of the peer group there is pro rata vesting between 40% and 100%. Awards under the LTIS for 2006 and prior have been valued at fair value using a Monte Carlo simulation model.

For awards under the 2008 and 2007 LTIS, one third are subject to an absolute total shareholder return performance condition measured over three years from the date of grant and two thirds are subject to annual growth in Net Net Net Asset Value ('NNNAV') measured over three years from the date of grant. One third of the awards, therefore, are subject to a market-based performance condition and these have been valued at fair value using a Monte Carlo simulation model. The remaining two thirds of the awards are subject to a non-market-based performance condition and have been valued at fair value using a Black-Scholes valuation model.

33 Share-based payments continued

Awards under the SAYE scheme have been valued at fair value using a Black Scholes model.

Shares were awarded, subject to the vesting conditions set out above, to executive directors and selected employees during the year under the LTIS but there were no options granted in the year under this scheme.

Share options were granted to employees of the group during the year under the SAYE scheme. The main assumptions used to value the shares and options granted during the year are as follows:

LTIS

Share awards:

Award date	9 January 2008 Market-based	9 January 2008 Non-market-based
Number of shares on grant	**350,096**	**700,193**
Exercise price (£)	**–**	**–**
Vesting period from date of grant (years)	**3**	**3**
Exercise period after vesting (years)	**7**	**7**
Share price at grant (£)	**3.170**	**3.170**
Expected risk free rate (%)	**5.310**	**5.310**
Expected dividend yield (%)	**0.900**	**0.900**
Expected volatility (%)	**26.000**	**26.000**
Fair value (£)	**1.210**	**3.081**

SAYE

Award date	11 July 2008 3-year scheme	11 July 2008 5-year scheme
Number of shares on grant	**229,837**	**382,514**
Exercise price (£)	**1.678**	**1.678**
Vesting period from date of grant (years)	**3**	**5**
Expected exercise date	**1 Dec 11**	**1 Dec 13**
Share price at grant (£)	**2.020**	**2.020**
Expected risk free rate (%)	**4.698**	**4.698**
Expected dividend yield (%)	**1.100**	**1.100**
Expected volatility (%)	**21.000**	**21.000**
Fair value (£)	**0.640**	**0.730**

The expected volatility figures used in the valuation were calculated based on the historic volatility over a period equal to the expected term from the date of grant.

The share-based payments charge recognised in the income statement is £0.5m (2007: £1.0m).

Movements in options and options exercisable as at 30 September 2008 are shown in note 32.

NOTES TO THE FINANCIAL STATEMENTS

34 Consolidated statement of changes in equity

	Issued share capital £m	Share premium £m	Merger reserve £m	Equity component of convertible bond £m	Capital redemption reserve £m	Cash flow hedge reserve £m	Retained earnings £m	Total £m
Balance as at 1 October 2006	6.5	22.6	20.1	–	0.2	(0.8)	201.3	249.9
Retained profit for the year	–	–	–	–	–	–	60.9	60.9
Actuarial gain on BPT pension scheme net of tax	–	–	–	–	–	–	1.5	1.5
Changes in fair value of cash flow hedges net of tax	–	–	–	–	–	9.0	–	9.0
Net exchange adjustment offset in reserves	–	–	–	–	–	–	0.3	0.3
Purchase of own shares	–	–	–	–	–	–	(7.0)	(7.0)
Issue of shares to satisfy employee share options	–	0.4	–	–	–	–	–	0.4
Treasury shares bought back and cancelled	(0.1)	–	–	–	0.1	–	(7.8)	(7.8)
Share-based payments charge	–	–	–	–	–	–	1.0	1.0
Dividends paid	–	–	–	–	–	–	(7.6)	(7.6)
Issue of convertible bond	–	–	–	22.4	–	–	–	22.4
Balance as at 30 September 2007	6.4	23.0	20.1	22.4	0.3	8.2	242.6	323.0
Loss for the year	–	–	–	–	–	–	(77.4)	(77.4)
Actuarial gain on BPT pension scheme net of tax	–	–	–	–	–	–	0.3	0.3
Changes in fair value of cash flow hedges net of tax	–	–	–	–	–	(2.8)	–	(2.8)
Net exchange adjustment offset in reserves	–	–	–	–	–	–	0.8	0.8
Purchase of own shares	–	–	–	–	–	–	(1.0)	(1.0)
Issue of shares to satisfy employee share options	–	0.1	–	–	–	–	–	0.1
Share-based payments charge	–	–	–	–	–	–	0.5	0.5
Dividends	–	–	–	–	–	–	(8.3)	(8.3)
Acquisition of minority interests	–	–	–	–	–	–	(5.5)	(5.5)
Balance as at 30 September 2008	**6.4**	**23.1**	**20.1**	**22.4**	**0.3**	**5.4**	**152.0**	**229.7**

Merger reserve

The merger reserve arose when the company issued shares in partial consideration for the acquisition of City North Group plc. The issue satisfied the provisions of Section 131 of the Companies Act 1985 and the premium relating to the shares issued was credited to a merger reserve.

Cash flow hedge reserve

The fair value movements on those derivative financial instruments qualifying for hedge accounting under IAS 39 are taken to this reserve.

34 Consolidated statement of changes in equity continued

The retained earnings reserve comprises various elements. Those elements and the movements in each are set out below:

	Share-based payment reserve £m	Treasury shares bought back and cancelled £m	Investment in own shares £m	Translation reserve £m	Retained earnings £m	Total retained earnings reserve £m
Balance as at 1 October 2006	0.5	–	(1.4)	0.1	202.1	201.3
Retained profit for the year	–	–	–	–	60.9	60.9
Actuarial gain on BPT pension scheme net of tax	–	–	–	–	1.5	1.5
Net exchange adjustment offset in reserves	–	–	–	0.3	–	0.3
Purchase of own shares	–	–	(7.0)	–	–	(7.0)
Treasury shares bought back and cancelled	–	(7.8)	–	–	–	(7.8)
Share-based payments charge	1.0	–	–	–	–	1.0
Dividends paid	–	–	–	–	(7.6)	(7.6)
Balance as at 30 September 2007	1.5	(7.8)	(8.4)	0.4	256.9	242.6
Loss for the year	–	–	–	–	(77.4)	(77.4)
Actuarial gain on BPT pension scheme net of tax	–	–	–	–	0.3	0.3
Net exchange adjustment offset in reserves	–	–	–	0.8	–	0.8
Purchase of own shares	–	–	(1.0)	–	–	(1.0)
Share-based payments charge	0.5	–	–	–	–	0.5
Dividends	–	–	–	–	(8.3)	(8.3)
Acquisition of minority interests	–	–	–	–	(5.5)	(5.5)
Balance as at 30 September 2008	**2.0**	**(7.8)**	**(9.4)**	**1.2**	**166.0**	**152.0**

Share-based payments reserve

This reserve comprises the cumulative credit entries relating to the share-based payments charge made in the income statement less the average cost of shares issued to employees as part of the LTIS scheme.

Shares bought back and cancelled

During the year, Grainger plc did not buy back and cancel any shares (2007: 1,525,000 shares at a cost of £7,846,020).

Investment in own shares reserve

As at 30 September 2008, the group owned its own shares as follows: 584,673 (2007: 584,673) shares held by The Grainger Trust Employee Trustee Company Limited, 1,017,088 (2007: 520,000) shares held by The Grainger Employee Benefit Trusts and 452,912 (2007: 650,000) shares held by Grainger plc as treasury shares. The total of shares held is 2,054,673 (2007: 1,754,673) with a cost of £9,459,400 (2007: £8,455,374).

NOTES TO THE FINANCIAL STATEMENTS

35 List of principal subsidiaries

The directors consider that providing details of all subsidiaries, joint ventures and associates as at 30 September 2008 would result in disclosure of excessive length. The following information relates to those subsidiary undertakings whose results or financial position, in the opinion of the directors, principally affected the group. A full list will be appended to the next annual return.

	Proportion of nominal value ordinary issued shares held by			
Name of undertaking	Group %	Company %	Incorporated	Activity
Northumberland & Durham Property Trust Limited	100		England & Wales	Property Trading
Grainger Residential Management Limited	100	100	England & Wales	Property Management
Grainger Asset Management Limited	100	100	England & Wales	Asset Management
Warren Court Limited	100		England & Wales	Property Trading
Grainger Hornsey Limited	100		England & Wales	Land Development
West Waterlooville Developments Limited	100		England & Wales	Land Development
BPT (Bradford Property Trust) Limited	100		England & Wales	Property Trading
BPT (Residential Investments) Limited	100		England & Wales	Property Investment
Grainger Finance Company Limited	100	100	England & Wales	Finance Company
Bromley Property Investments Limited	100		England & Wales	Finance Company
Home Properties Limited	100		England & Wales	Property Trading
Bridgewater Tenancies Limited	100		England & Wales	Property Trading
Bridgewater Equity Release Limited	100		England & Wales	Property Investment
Homesafe Equity Release LP	100		England & Wales	Property Investment
Hamsard 2517 Limited	100		England & Wales	Property Trading
Grainger Recklinghausen Portfolio 1 Sarl & Co KG	100		Germany	Property Investment
Grainger Recklinghausen Portfolio 2 Sarl & Co KG	100		Germany	Property Investment
Grainger Berlin Portfolio 1 Sarl & Co KG	100		Germany	Property Investment
Grainger Stuttgart Portfolio 1 Sarl & Co KG	100		Germany	Property Investment
Grainger Stuttgart Portfolio 2 Sarl & Co KG	100		Germany	Property Investment
Francono Rhein-Main AG	100		Germany	Property Investment
Grainger Luxembourg Financing (No. 1) Sarl	100		Luxembourg	Finance Company
Grainger Luxembourg Financing (No. 2) Sarl	100		Luxembourg	Finance Company
Grainger Luxembourg Financing (No. 3) Sarl	100		Luxembourg	Finance Company
Grainger Luxembourg Germany Holdings Sarl	100		Luxembourg	Holding Company
Grainger Treasury Properties (2006) LLP	100		England & Wales	Property Investment
The Tilt Estate Company Limited	100		England & Wales	Property Investment
Grainger Retirement Housing No.1 (2007) Limited	100		England & Wales	Property Investment
BPT Limited	100		England & Wales	Investment Company
Grainger Malta Finance Limited	100		Malta	Finance Company

All subsidiaries are consolidated in the group accounts.

36 Related party transactions

During the year and at the year end, the group held a 50% interest in Grainger GenInvest LLP and Grainger GenInvest No 2 (2006) LLP. The group provides a number of services to both partnerships and receives an asset adviser fee, a sales fee, a commercial management fee and a treasury services fee. Amounts recognised in the income statement and outstanding balances at the year end are as follows:

	2008 Fees recognised £'000	2008 Year-end balance £'000	2007 Fees recognised £'000	2007 Year-end balance £'000
Asset adviser fee	**878**	**256**	688	200
Sales fee	**36**	**8**	83	–
Commercial management fee	**30**	**8**	7	5
Treasury fee	**30**	**9**	10	9
	974	**281**	788	214

In addition, the group has provided loans to both partnerships as follows:

	Balance as at 30 September 2008 £m	Balance as at 30 September 2007 £m	2008 Interest receivable £m	2007 Interest receivable £m
Grainger GenInvest LLP – 8.5% fixed interest loan note	**7.1**	7.9	**0.7**	0.7
Grainger GenInvest No 2 (2006) LLP – 11.0% fixed interest loan note	**4.8**	4.5	**0.3**	0.3
Grainger GenInvest No 2 (2006) LLP – mezzanine loan at LIBOR plus 4%	**68.3**	55.6	**6.6**	5.1
	80.2	68.0	**7.6**	6.1

Interest receivable is included within interest receivable from associates and joint ventures shown in note 13. The difference of £3.5m between the figure shown above of £7.6m and the amount shown in note 13 of £4.1m is a consolidation adjustment to eliminate interest receivable by the group from the Grainger GenInvest entities against interest payable in those entities to the group.

The loan notes have no fixed repayment date and are subordinated to external financing with each LLP. If not demanded before, the Grainger GenInvest LLP loan notes are repayable by 23 June 2015 and the Grainger GenInvest No 2 (2006) LLP loan notes by 31 December 2016. The mezzanine loan is repayable on demand but has a final repayment date of 20 March 2011.

The group held a 50% interest in Curzon Park Limited as at 30 September 2008. The group has provided a loan to Curzon Park Limited as at 30 September 2008 of £7.4m (2007: £6.8m). The loan is repayable on demand and bears interest at 4% per annum.

The group held a 21.6% interest in G:res1 Limited as at 30 September 2008. The group provides a number of services to the fund and receives a property management fee, a lettings and renewal fee, and an asset management fee. Amounts recognised in the income statement and the outstanding balance at the year end are as follows:

	2008 Fees recognised £'000	2008 Year-end balance £'000	2007 Fees recognised £'000	2007 Year-end balance £'000
Property management fees	**1,437**	**364**	1,081	352
Lettings and renewal fees	**187**	**49**	130	49
Asset management fees	**2,739**	**616**	2,078	707
Insurance intermediary fee	**–**	**–**	38	–
	4,363	**1,029**	3,327	1,108

NOTES TO THE FINANCIAL STATEMENTS

36 Related party transactions continued

The group held a 23.6% interest in the Schroder Residential Property Unit Trust as at 30 September 2008. The group provides a number of services to the Trust and receives a property management fee, a lettings and renewal fee and an asset management fee. Amounts recognised in the income statement and the outstanding balance at the year end are as follows:

	2008 Fees recognised £'000	2008 Year-end balance £'000	2007 Fees recognised £'000	2007 Year-end balance £'000
Property management fees	**320**	**90**	345	87
Lettings and renewal fees	**13**	**4**	26	–
Asset management fees	**530**	**140**	587	168
	863	**234**	958	255

Details of key management compensation are provided in note 11.

37 Capital commitments

As at 30 September 2008, the group and its joint ventures and associates had capital commitments of £nil (2007: £nil).

38 Operating lease commitments

The future aggregate minimum lease payments payable by the group under non-cancellable operating leases are as follows:

	2008 £m	2007 £m
Operating leases which expire:		
Not later than one year	**0.5**	0.5
Later than one year and not later than five years	**0.9**	0.8
Later than five years	**5.9**	6.6
	7.3	7.9

The group does not expect to receive any payments under non-cancellable sub-leases (2007: £nil).

39 Contingent liabilities

The properties in certain subsidiary companies forming a 'guarantee group' provide the security for the group's MOF facility (see note 27). The properties in certain of the group's German subsidiaries provide security for the non-recourse finance raised in those subsidiary undertakings.

The group has provided guarantees under performance bonds relating to its UK development division and as guarantees against certain loan notes issued by the group. As at 30 September 2008, this amounted to £14.3m (2006: £11.4m). Subsequent to the year end a guarantee for £8.5m relating to a development project was released.

In addition, the group has an obligation, under the sale and purchase agreement for the land at West Waterlooville, to pay further consideration should the site value exceed certain pre-agreed amounts. It is not possible to determine the amount or timing of any such future payments due to the long-term nature of the site's development and the associated uncertainties with respect to planning applications. However, any future payments will not fall due until at least 2015 and will be spread over a number of years.

40 Post-balance sheet events

i Since the year end, holders of £87.1m of the £112m 3.625% 2014 convertible bond have accepted a cash payment of £35,000 per £100,000 nominal bond value to convert early. The effects of this early conversion have been to: i) issue 10.08m ordinary shares; ii) eliminate £57m nominal of debt; iii) increase net assets by £42.0m; and iv) to reduce the LTV on our core facility to 64.1% from 66.4% at the year end.

In the year to 30 September 2009 there will be a one-off charge to the income statement of £30.5m representing the cash amount paid to bondholders. Annual interest costs will be reduced by approximately £3.6m per annum as a result of the overall reduction in debt. In addition, by converting prior to the interest payment date of 14 November the group will be able to write back to the 2009 income statement approximately £1.6m of interest accrued at 30 September 2008 that will not be paid.

ii We completed the sale of our development site at Barnsbury in North London on 4 December 2008 realising proceeds of £19m.

41 Business combinations

On 4 April 2008, the group acquired 85.1% of Francono Rhein-Main AG a property investment company owning residential property in the Frankfurt area of Germany. The acquired business contributed revenue of £4.8m and net profit before tax of £0.6m to the group for the period from 4 April 2008 to 30 September 2008. If the acquisition had occurred on 1 October 2007, group revenue would have been £250.3m and group loss before tax would have been £109.6m.

Details of the net assets acquired and the gain on acquisition are as follows:

	£m
Purchase consideration:	
Cash paid	**30.3**
Direct costs relating to the acquisition	**2.3**
Total purchase consideration	**32.6**
Fair value of net assets acquired	**(33.1)**
Gain on acquisition of subsidiary (note 9)	**(0.5)**

The gain on acquisition of subsidiary is attributable to the fact that the group has been able to negotiate a 'bargain purchase'.

NOTES TO THE FINANCIAL STATEMENTS

41 Business combinations continued

The assets and liabilities as at 4 April 2008 arising from the acquisition are as follows:

	Fair value and acquiree's carrying value £m
Investment property	**131.9**
Property, plant and equipment	**0.2**
Trade and other receivables	**2.9**
Inventories	**1.3**
Cash and cash equivalents	**3.2**
Borrowings	**(90.7)**
Trade and other payables	**(6.0)**
Deferred tax liabilities (see note 14)	**(3.8)**
Net assets	**39.0**
Minority interests (14.9%)	**(5.9)**
Net assets acquired	**33.1**
Purchase consideration settled in cash	**(32.6)**
Cash and cash equivalents in subsidiary acquired	**3.2**
Cash outflow on acquisition	**(29.4)**

There were no adjustments required to adjust the book values of FRM's assets and liabilities to fair value.

On 18 October 2007 the group acquired 81.6% of Prazsky Project a.s. a company registered in the Czech Republic and which owns land on the same development site as the land owned by the group's existing subsidiary CCZ a.s. The acquisition has had no material impact on the group's results for the period to 30 September 2008. The assets and liabilities as at 18 October arising from the acquisition are as follows:

	Fair value £m
Inventories – development land	**5.3**
Cash and cash equivalents	**0.3**
Borrowings	**(3.3)**
Trade and other payables	**(1.5)**
Net assets	**0.8**
Minority interests (18.4%)	**(0.1)**
Net assets acquired	**0.7**
Purchase consideration settled in cash	**–**
Cash and cash equivalents in subsidiary acquired	**0.3**
Cash inflow on acquisition	**0.3**

Inventories – development land was valued at a fair value of £5.3m on acquisition. This was £0.9m higher than the value in Prazsky Project a.s.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF GRAINGER PLC ON THE PARENT COMPANY FINANCIAL STATEMENTS

We have audited the parent company financial statements of Grainger plc for the year ended 30 September 2008 which comprise the company balance sheet and the related notes. These parent company financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the report of the remuneration committee and directors' remuneration report that is described as having been audited.

We have reported separately on the group financial statements of Grainger plc for the year ended 30 September 2008.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report, the report of the remuneration committee and the parent company financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the statement of directors' responsibilities.

Our responsibility is to audit the parent company financial statements and the part of the report of the remuneration committee and directors' remuneration report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the parent company financial statements give a true and fair view and whether the parent company financial statements and the part of the report of the remuneration committee and directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the directors' report is consistent with the parent company financial statements.

The information given in the directors' report includes that specific information presented in the chairman's statement and the chief executive's review that is cross-referenced from the review of business development and prospects section of the directors' report.

In addition we report to you if, in our opinion, 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 regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the annual report and consider whether it is consistent with the audited parent company financial statements. The other information comprises only the chairman's statement, the chief executive's review, the financial review, the corporate governance report, the directors' report, the corporate responsibility report and the unaudited part of the report of the remuneration committee and directors' remuneration report and the other items listed in both contents pages. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the parent company financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the parent company financial statements and the part of the report of the remuneration committee and directors' remuneration report to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the parent company financial statements, and of whether the accounting policies are appropriate to the company'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 parent company financial statements and the part of the report of the remuneration committee and directors' remuneration report 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 parent company financial statements and the part of the report of the remuneration committee and directors' remuneration report to be audited.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF GRAINGER PLC ON THE PARENT COMPANY FINANCIAL STATEMENTS

Opinion

In our opinion:

- the parent company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 30 September 2008;
- the parent company financial statements and the part of the report of the remuneration committee and directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the directors' report is consistent with the parent company financial statements.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London
16 December 2008

Note

The maintenance and integrity of the Grainger plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

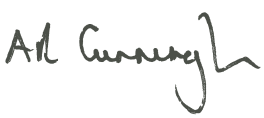
Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

PARENT COMPANY BALANCE SHEET

As at 30 September 2008	Notes	2008 £m	2007 £m
Fixed assets			
Tangible assets	2	**0.2**	0.3
Investments	3	**109.4**	149.1
		109.6	149.4
Current assets			
Debtors	4	**325.8**	261.4
Cash at bank and in hand		**0.6**	3.0
		326.4	264.4
Creditors: amounts falling due within one year	5	**127.9**	135.3
Net current assets		**198.5**	129.1
Total assets less current liabilities		**308.1**	278.5
Creditors: amounts falling due after more than one year			
Convertible bond	6	**91.1**	88.5
Provisions for liabilities and charges	7	**0.4**	1.2
Net assets		**216.6**	188.8
Capital and reserves			
Called-up equity share capital	8	**6.4**	6.4
Share premium	9	**23.1**	23.0
Capital redemption reserve	9	**0.3**	0.3
Equity component of convertible bond	9	**22.4**	22.4
Profit and loss account	9	**164.4**	136.7
Total shareholders' funds		**216.6**	188.8

The financial statements on pages 67 to 72 were approved by the board of directors on 16 December 2008 and were signed on their behalf by:

Rupert Dickinson
Director



Andrew Cunningham
Director

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

1 Accounting policies

a) Basis of preparation

The financial statements have been prepared on a going concern basis in accordance with the historical cost convention as modified by the revaluation of certain investments, in accordance with the Companies Act 1985 and applicable UK accounting standards.

The company has taken the exemption allowed under Section 230(4) of the Companies Act 1985 from the requirement to present its own profit and loss account. The profit for the year was £36.3m (2007: £2.1m). On an historical cost basis the profit for the year would have been £38.5m (2007: £1.2m). These financial statements present information about the company as an individual undertaking and not about its group.

In accordance with the exemption in FRS1 'Cash Flow Statements' (revised 1996), the company has not prepared a cash flow statement on the grounds that it has presented its own consolidated financial statements.

The company has taken advantage of the exemption in FRS 8 'Related Party Transactions', from the requirement to disclose such transactions on the grounds that it has presented its own consolidated financial statements.

b) Accounting policies

The company financial statements have been prepared under UK GAAP rather than under IFRS which has been adopted for group reporting. The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the company's financial statements.

c) Tangible fixed assets

These comprise office fixtures, fittings and equipment and are carried at historical cost less accumulated depreciation and impairment. Subsequent costs are included in the assets carrying amount or recognised as a separate asset, as appropriate, only when it is probable that the future economic benefits associated with the item will flow to the company and the cost of the item can be measured reliably. Depreciation is provided on a straight-line basis over the estimated useful life of the assets which is assessed as five years.

d) Investments

Investments in equity instruments that have a quoted market price in an active market or whose fair value can be reliably measured are valued at fair value under FRS 26 'Financial Instruments: Recognition and Measurement'. Fair value is measured as the net asset value per unit held.

e) Investment in subsidiaries

Investments in subsidiaries are carried at historical cost less provision for impairment.

f) Taxation

Corporation tax is provided on taxable profits or losses at the current rate.

Deferred tax assets and liabilities arise from timing differences between the recognition of gains and losses in the accounts and their recognition in a tax computation.

In accordance with FRS 19 'Deferred Tax', deferred tax is provided in respect of all timing differences that have originated, but not reversed, at the balance sheet date that may give rise to an obligation to pay more or less tax in future. Deferred tax is measured on a non-discounted basis.

g) Own shares including treasury shares

Transactions of the Grainger Trust Employee Trust Company Limited and The Grainger Employee Benefit Trusts are included in the company's financial statements. The purchase of shares in the company by each trust and any treasury shares bought back by the company are debited directly to equity.

2 Tangible fixed assets

	Fixtures, fittings and equipment £m
Cost	
At 1 October 2007 and 30 September 2008	0.9
Depreciation	
At 1 October 2007	0.6
Charge for the year	0.1
At 30 September 2008	0.7
Net book value	
At 30 September 2008	**0.2**
At 1 October 2007	0.3

3 Fixed asset investments

	Investment in subsidiaries £m	Investment in Schroder Residential Property Unit Trust £m	Total £m
Cost			
At 1 October 2007	129.0	20.1	149.1
Additions	0.5	–	0.5
Provision for impairment	(37.2)	–	(37.2)
Reduction to fair value	–	(3.0)	(3.0)
At 30 September 2008	**92.3**	**17.1**	**109.4**

The provision for impairment of £37.2m has been made against the company's investment in City North Limited. The provision is required after the reduction in capital in that company (see note 10).

Investments in equity instruments that do not have a quoted market price in an active market or whose fair value cannot be reliably measured cannot be valued at fair value under FRS 26. The investment in the Schroder Residential Property Unit Trust can be reliably measured and, therefore, has been valued at fair value under FRS 26.

A list of the principal subsidiaries of the company is given in note 35 on page 60.

4 Debtors

	2008 £m	2007 £m
Amounts owed by group undertakings	**325.1**	260.7
Other debtors	**0.7**	0.7
	325.8	261.4

Debtors in both 2007 and 2008 are all due within one year.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

5 Creditors: amounts falling due within one year

	2008 £m	2007 £m
Loan notes	**0.4**	0.6
Amounts owed to group undertakings	**125.3**	132.6
Corporation tax payable	**0.3**	–
Other taxation and social security	**0.1**	–
Accruals and deferred income	**1.8**	2.1
	127.9	135.3

The loan notes are secured by bank guarantees and cash collateral and bear interest at between 0.75% and 1% under LIBOR. The loan notes are repayable within one year.

6 Convertible bond

	2008 £m	2007 £m
Opening balance	**90.2**	–
Total fair value on initial recognition	**–**	112.0
Equity component of new issue	**–**	(22.4)
Amortised during the year	**2.5**	0.6
	92.7	90.2
Unamortised issue costs	**(1.6)**	(1.7)
Liability component at 30 September 2008	**91.1**	88.5

The £112m 3.625% convertible bond due 2014 was issued in May 2007. Interest is payable semi-annually. Unless previously redeemed, converted, purchased or cancelled the bond is convertible at any time up to 12 May 2014 into fully paid up ordinary shares at a conversion price of £8.64. The convertible bond is a compound financial instrument and the carrying amount has been allocated to its equity and liability components in the group balance sheet. The liability component has been determined by measuring the fair value of a similar liability that does not have an associated equity component. The discount rate used for this was based on a rate of 7.5% compounded semi-annually. The liability component has been deducted from the fair value of the compound financial instrument as a whole and the residual element has been assigned to the equity component. The liability element is subsequently measured at amortised cost using the effective interest rate method.

Since the year end, holders of £87.1m of the £112m 3.625% 2014 convertible bond have accepted a cash payment of £35,000 per £100,000 nominal bond value to convert early (see note 11).

7 Provisions for liabilities and charges

	2008 £m	2007 £m
Deferred tax liability:		
Opening balance	**1.2**	1.0
Deferred tax on revaluation deficits/gains	**(0.8)**	0.3
Impact of change in tax rate	**–**	(0.1)
Closing balance	**0.4**	1.2

The deferred tax balance relates to the tax on the unrealised gain on the revaluation of the investment in units in the Schroder Residential Property Unit Trust. Deferred tax is provided at a rate of 28% (2007: 28%).

8 Share capital

	2008 £m	2007 £m
Authorised		
160,000,000 (2007: 160,000,000) ordinary shares of 5p each	**8.0**	8.0
Allotted, called-up and fully paid		
128,716,094 (2007: 128,656,385) ordinary shares of 5p each	**6.4**	6.4

Grainger plc acquired 300,000 of its own shares on 10 January 2008. The total amount paid to acquire the shares was £1.0m and has been deducted from retained earnings within shareholders' equity (see note 9). These shares are held as treasury shares. As at 30 September 2008, share capital included 584,673 (2007: 584,673) shares held by The Grainger Trust Employee Trustee Company Limited, 1,017,088 (2007: 520,000) shares held by The Grainger Employee Benefit Trusts and 452,912 (2007: 650,000) shares held by Grainger plc as treasury shares. The total number of shares held at 30 September 2008 was 2,054,673 (2007: 1,754,673) with a nominal value of £102,734 (2007: £87,734).

Movements in issued share capital during the year and the previous year were as follows:

	Number	Nominal value £'000
At 1 October 2006	129,925,482	6,496
Options exercised under the executive share option scheme	63,645	3
Options exercised under the LTIS scheme	74,586	4
Options exercised under SAYE schemes	117,672	6
Treasury shares bought back and cancelled	(1,525,000)	(76)
At 30 September 2007	128,656,385	6,433
Options exercised under the LTIS scheme	11,307	1
Options exercised under SAYE schemes	48,402	2
At 30 September 2008	**128,716,094**	**6,436**

Details of share options granted by the company are provided in note 32 on pages 55 and 56.

NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

9 Reserves

	Share premium £m	Capital redemption reserve £m	Equity component of convertible bond £m	Profit and loss account £m
At 1 October 2007	23.0	0.3	22.4	136.7
Retained profit for the year	–	–	–	36.3
Share-based payment charge	–	–	–	0.5
Issue of shares to satisfy employee share options	0.1	–	–	–
Purchase of own shares	–	–	–	(1.0)
Dividends paid	–	–	–	(8.1)
At 30 September 2008	**23.1**	**0.3**	**22.4**	**164.4**

10 Reduction of share capital in subsidiary

Following a written resolution dated 18 July 2008, the High Court sanctioned on 13 August 2008 the reduction of the share capital of City North Limited a wholly owned subsidiary of the company. Details of the reduction can be found in the accounts of the subsidiary. Grainger plc received amounts totalling £74,083,479 following the reduction of the share capital and this has been credited to the profit and loss account.

11 Other information

Post balance sheet event

Since the year end, holders of £87.1m of the £112m 3.625% 2014 convertible bond have accepted a cash payment of £35,000 per £100,000 nominal bond value to convert early. The effects of this early conversion have been to: i) issue 10.08m ordinary shares; ii) eliminate £57m nominal of debt; iii) increase net assets by £42.0m; and iv) to reduce the LTV on our core facility to 64.1% from 66.4% at the year end.

In the year to 30 September 2009 there will be a one-off charge to the income statement of £30.5m representing the cash amount paid to bondholders. Annual interest costs will be reduced by approximately £3.6m per annum as a result of the overall reduction in debt. In addition, by converting prior to the interest payment date of 14 November, the company will be able to write back to the 2009 income statement approximately £1.6m of interest accrued at 30 September 2008 that will not be paid.

Dividends

Information on dividends paid and declared is given in note 15 on page 30.

Share options

Details of share options outstanding and the movements during the year are given in note 32 on pages 55 and 56 respectively.

Employees

The company had no employees in 2008 (2007: none) other than the directors. Details of their remuneration are given on page 49 of the review section of this document.

Audit fees

The audit fee for the year was £8,000 (2007: £8,000).

FIVE-YEAR RECORD FOR THE YEAR ENDED 30 SEPTEMBER 2008

	UK GAAP	IFRS			
	2004 £m	2005 £m	Restated 2006 £m	2007 £m	2008 £m
Turnover	217.4	227.6	206.3	229.3	**246.2**
Gross rental income	41.0	45.5	52.6	52.7	**70.7**
Sales of investment properties	41.1	13.3	40.6	14.8	**7.4**
Trading profits	72.6	67.2	56.2	62.8	**62.6**
Profit/(loss) before taxation**	59.6	41.0	47.7	77.5	**(112.1)**
Profit/(loss) after taxation and minority interests**	36.8	31.1	33.5	60.9	**(77.4)**
Dividends	5.7	6.9	6.9	7.6	**8.3**

	Pence per share	Pence per share	Pence per share	Pence per share	Pence per share
(Loss)/earnings**	29.94	24.88	25.99	47.26	**(61.05)**
Dividends per share	4.65	5.11	5.62	6.18	**6.18**

	£m	£m	£m	£m	£m
Fixed assets and stocks on a financial statements basis	950.8	1,225.4	1,467.8	1,865.0	**2,027.4**
Fixed assets and stocks at market value	1,454.5	1,639.3	2,009.9	2,514.7	**2,404.6**
Share capital and reserves	177.9	211.1	250.1	323.1	**229.8**

	Pence per share	Pence per share	Pence per share	Pence per share	Pence per share
Net asset value on a financial statements basis	143.4	159.1	192.5	251.1	**178.4**
Net asset value including fixed assets and stocks at market value*	546.8	475.4	606.3	751.7	**471.5**
Dividend cover**	6.5x	4.7x	4.6x	7.7x	**–**
Share price at 30 September	367.0p	456.0p	628.0p	447.5p	**200.0p**

Share price and per share figures have been restated for 2004 to take account of the five for one share split that took place in February 2005.

Information relating to 2004 is presented under UK GAAP as directed by IFRS 1. The main adjustments that would be required to comply with IFRS are those set out in note 38 to the 2006 consolidated financial statements.

In addition:

* corporation tax has not been provided on valuation surpluses relating to stocks

** excluding exceptional items and including share of joint ventures and associates

SHAREHOLDERS' INFORMATION

Financial calendar
Annual General Meeting 10 February 2009
Payment of 2008 final dividend 16 February 2009
Announcement of 2009 interim results May 2009
Payment of 2009 interim dividend June 2009
Announcement of 2009 final results November 2009

Share price
During the year ended 30 September 2008, the range of the closing mid-market prices of the company's ordinary shares were:

Price at 30 September 2008	200p
Lowest price during the year	187p
Highest price during the year	465p

Daily information on the company's share price can be obtained on our website or by telephoning: The Financial Times Cityline Service on 09068 432 750.

Capital gains tax
The market value of the company's shares for capital gains tax purposes at 31 March 1982 was 6.08p.

Website
Website address www.graingerplc.co.uk

Shareholders' enquiries
All administrative enquiries relating to shareholdings (for example, notification of change of address, loss of share certificates, dividend payments) should be addressed to the company's registrar at:

Capita IRG Plc
Northern House
Woodsome Park
Fenay Bridge
Huddersfield
West Yorkshire
HD8 0LA

Share dealing service
A share dealing service is available to existing shareholders to buy or sell the company's shares via Capita Share Dealing Services. Online and telephone dealing facilities provide an easy to access and simple to use service.

For further information on this service, or to buy or sell shares, please contact:
www.capitadeal.com – online dealing
0870 458 4577 – telephone dealing

Please note that the directors of the company are not seeking to encourage shareholders to either buy or sell their shares. Shareholders in any doubt as to what action to take are recommended to seek financial advice from an independent financial adviser authorised by the Financial Services and Markets Act 2000.

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Company registration number 125575

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Bankers

Clearing Bank and Facility Agent
Barclays Bank PLC

Other bankers
Lloyds TSB Bank plc

The Royal Bank of Scotland plc

Allied Irish Banks plc

The Governor and Company of the Bank of Scotland

National Australia Bank Limited

Nationwide Building Society

Eurohypo AG

Hypo Real Estate Bank AG

The Governor and Company of the Bank of Ireland

GE Real Estate Finance Limited

Svenska Handelsbanken AB

SEB AG

Bayerische Hypo-und Verensbank AG

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GLOSSARY OF TERMS

PROPERTY

Assured periodic tenancy ('APT')	Market-rented tenancy arising from succession from regulated. Tenant has security of tenure.
Assured shorthold tenancy ('AST')	Market-rented tenancy where landlord may obtain possession if appropriate notice served.
Assured tenancy ('AT')	Market-rented tenancy where tenant has right to renew.
Investment value ('IV') or market value	Open market value of a property subject to relevant tenancy in place.
Home reversion	Rent free tenancy where tenant has right of occupation until forfeited (usually on death). If tenant retains an equity interest in the property this is a partial home reversion.
PRS	Private rented sector.
Regulated tenancy	Tenancy regulated under 1977 Rent Act, rent (usually sub-market) set by rent officer and tenant has security of tenure.
Vacant possession ('VP') value	Open market value of a property free from any tenancies.

CORPORATE

Grainger NAV	NNNAV adjusted for the after tax value of the reversionary surplus in our regulated and equity release portfolios discounted back to present value using our risk adjusted weighted average cost of capital over the expected average period of realisation. Base case and sensitivities exist.
IFRS	International Financial Reporting Standards. Mandatory for UK-listed companies for accounting periods ending on or after 31 December 2005.

FINANCIAL

Cap	Financial instrument which, in return for a fee, guarantees an upper limit for the interest rate on a loan.
Contingent tax	The amount of tax that would be payable on the difference between the carrying value of trading properties as recorded in the balance sheet and their market value.
Dividend cover	Earnings per share divided by dividends per share.
Earnings per share ('EPS')	Profit attributable to equity shareholders divided by the weighted average number of shares in issue in the year.
Gearing	The ratio of borrowings, net of cash, to the market net asset value.
Goodwill	On acquisition of a company, the difference between the fair value of net assets acquired and the purchase price paid.
Grainger NAV	NNNAV adjusted for the taxed discounted reversionary surplus on regulated and home reversion portfolios.
Gross net asset value ('Gross NAV')	Shareholders' funds adjusted for the market value of property assets held as stock, and adding back deferred tax and before adjustments for the fair value of derivatives.
Hedging	The use of financial instruments to protect against interest rate movements.
IAS 39	Accounting standard containing complex rules for the recognition of the market value of long-term debt and financial instruments.
IFRS	International Financial Reporting Standards.
Interest cover	Profit on ordinary activities before interest and tax divided by net interest payable.
Loan to value ('LTV')	Ratio of net debt to the market value of properties.
Net net asset value (triple net or 'NNNAV')	Gross NAV adjusted for tax liabilities which would accrue if assets sold at market value and for the market value of long-term debt and derivatives.
Return on capital employed	Growth in NNNAV plus dividends paid per share as a percentage of opening NNNAV.
Return on shareholders' equity	Profit before financing costs plus all revaluation surpluses as a percentage of opening gross capital.
Swap	Financial instrument to protect against interest rate movements.
Total shareholder return ('TSR')	Return attributable to shareholders on basis of share price growth with dividends reinvested.
Weighted average cost of capital ('WACC')	The weighted average cost of funding the group's activities through a combination of shareholders' funds and debt.

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