

Who we are

Derwent London is the largest central London focused real estate investment trust, owning a portfolio of 5.1 million sq ft (475,600m²) valued at £1.9 billion.

Strength of purpose is what defines us. Our business model has been developed to combine flair, innovation and management focus to add value to our extensive portfolio of properties and maintain a stable long-term financial position. Throughout the tough economic environment of the past two years we have continued to regenerate, refurbish and let our properties. This has proved that our business model is successful in various market conditions and is testament to our discipline and consistency. We are active and well capitalised, reinforcing our respected position in the property market. We nurture and improve our expanding portfolio, underpinned by the strength and depth of our team and our rigorous approach to portfolio management.

We have developed a reputation for anticipating the locations of tomorrow and contributing to London's regeneration. Both our commitment to the highest quality of sustainable building design and our focus on the communities in which we operate enable us to provide highly attractive space for our tenants.

Overview



Our principal objective

Our principal objective is to add value to our properties to deliver above average long-term returns to shareholders.

We accomplish this by focusing on four strategic aims:

- sourcing interesting buildings where we can identify and create value;
- devising tailor-made planning solutions for each property and working closely with architects and designers to optimise innovative design;
- focusing on enterprising portfolio management; and
- maintaining financial stability through flexible funding and timely recycling of capital.

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At a glance

2009 key achievements

Mar Sale of Dorset Square **£16.8m**

EDF letting at Qube **£1.5m pa**

Jupiter letting at 1 Grosvenor Place **£0.4m pa**

Apr **£125.0m** bank facility refinanced

Jul Sale of Arup Phase I **£59.4m**

Aug 45 Whitfield Street pre-let to Target Media Group **£0.3m pa**

Oct Charlotte Building completed (4,400 m²) **£0.6m pa** pre-let
Qube **100%** let

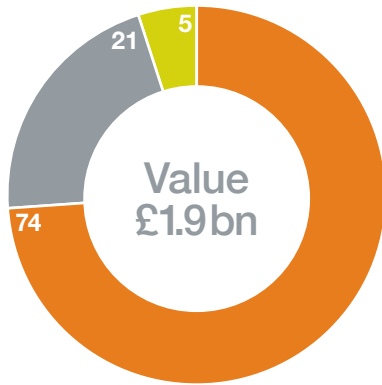
Nov Sale of The Rotunda **£41.4m**

Dec Completion of third and final Arup phase (7,900 m²)

Icon Entertainment letting at Charlotte Building **£0.3m pa**

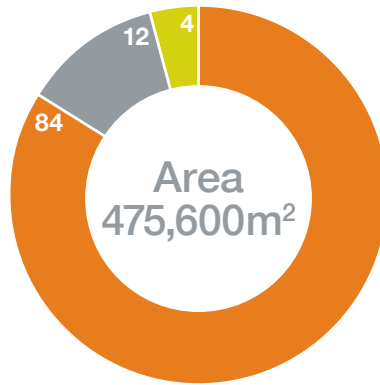
100th letting of the year to Innocent Drinks at Portobello Dock **£0.4m pa**

Profile of property ownership %



West End
City
Provincial

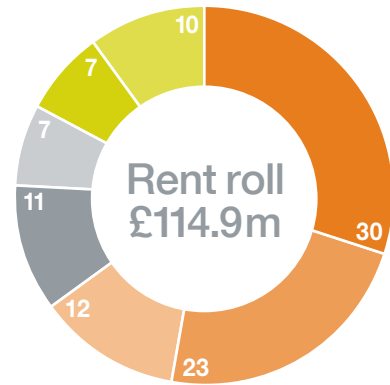
Profile of use types %



Office
Retail*
Other

*including ancillary retail in office buildings

Profile of tenants' business sectors %



Professional and business services
Media, TV, marketing and advertising
Retail sales
Retail head offices, showrooms
Financial
Government and public administration
Other

Lettings achieved

2009

31,500m²
£9.3m pa

2008

45,300m²
£16.3m pa

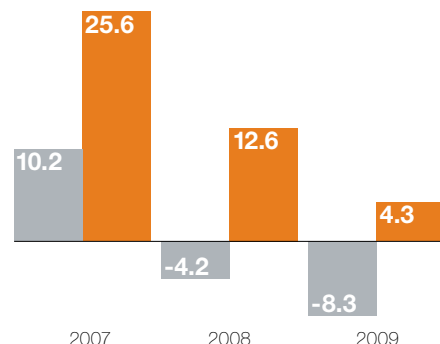
Consistently low vacancy rates %



Derwent London (by ERV)
Derwent London (by floor area)

Outperformance of IPD

Three year rolling property return (%)



IPD All UK Property Index
Derwent London

Financial highlights

Adjusted net asset value

2009

1,168p ↓ 5%

2008

1,226p

Recurring profit before tax

2009

£60.2m ↑ 158%

2008

£23.3m

Recurring net property income

2009

£114.8m ↑ 21%

2008

£95.0m

Recurring earnings per share

2009

55.55p ↑ 143%

2008

22.83p

Gearing

Profit and loss (ICR)

2009

330%

2008

247%

Balance sheet

2009

62.2%

2008

71.2%

Property (LTV)

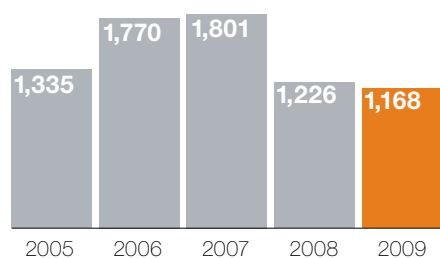
2009

36.4%

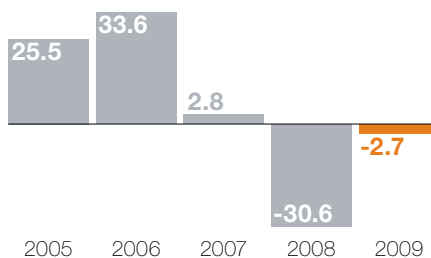
2008

39.7%

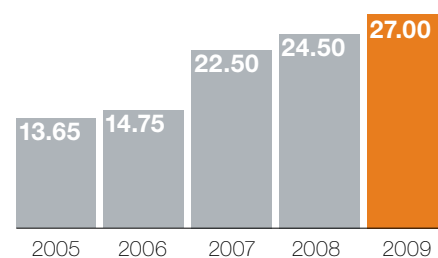
Adjusted net asset value per share p



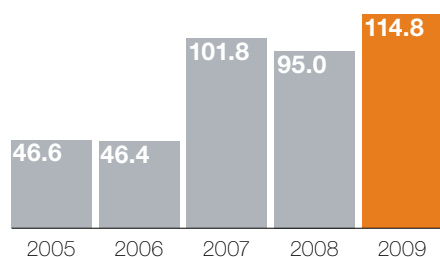
Total return %



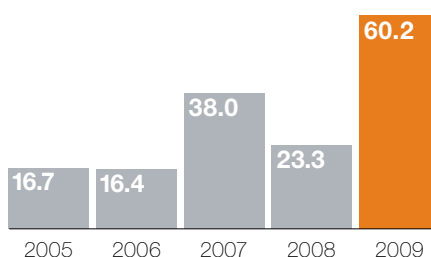
Dividend per share* p



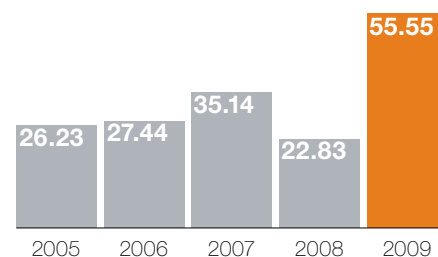
Recurring net property income £m



Recurring profit before tax £m



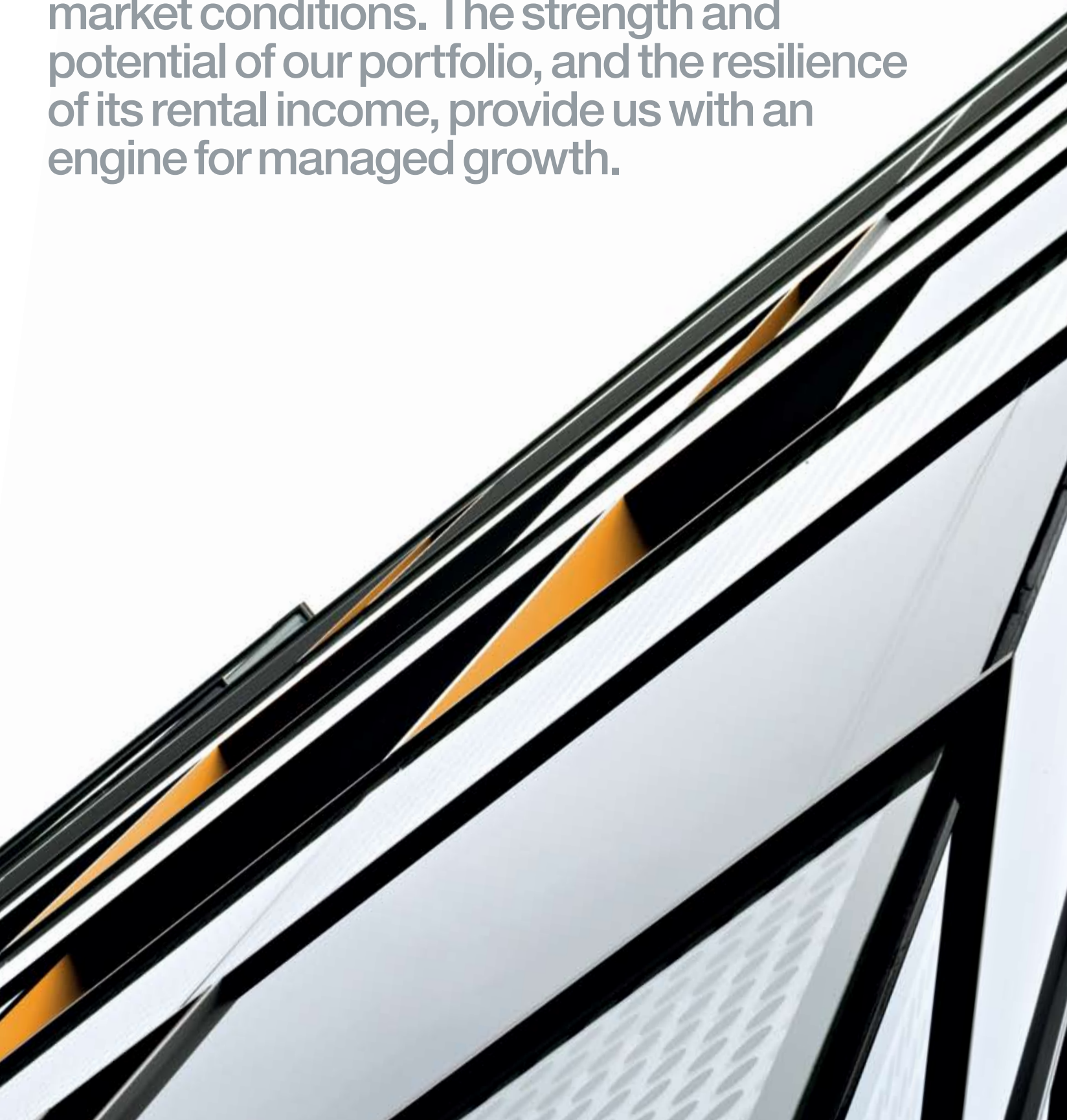
Recurring earnings per share p



*Based on the distribution of year's earnings
A list of definitions is provided on page 108

Chairman's statement

Derwent London's strong performance demonstrates the robustness of the group's business model even in extreme market conditions. The strength and potential of our portfolio, and the resilience of its rental income, provide us with an engine for managed growth.



Overview

Derwent London's strong performance during the year demonstrates the robustness of the group's business model even in extreme market conditions. This, together with the flexibility of the group's financing arrangements and management's ability to operate successfully in challenging circumstances, meant that Derwent is the only REIT in the FTSE 350 not to have raised equity during 2009.

The group excels in creating a unique brand of well-designed offices in favoured central London locations that provide tenants with contemporary space at mid-market rents. This attention to value and design contributed to the completion of over 100 lettings during 2009. Taken with the strong performance in 2008 when we completed 82 lettings, this is testament to the success of our product in a tough economic environment.

The focus of our portfolio was sharpened and our balance sheet strengthened after £208.3m of sales of non-core properties. Overall, these sales showed a discount of 7.4% from the December 2008 valuations.

The momentum of the group's regeneration programme was maintained during the year with capital expenditure of £91.5m being invested on various projects throughout the portfolio.

These achievements were reflected in the company's share price performance which resulted in a total shareholder return of 87%, making Derwent the top performing REIT in the FTSE 350 in 2009.

No major acquisitions were made in the year as we did not identify any opportunities that were sufficiently attractive to us. However, the group has many potential schemes within its portfolio of income-producing assets that can be developed to commence a new phase of innovative regeneration projects. Capital expenditure for 2010 is anticipated to be approximately £63m with a further £200m which could be incurred from 2011 onwards on identified schemes.

Results

Following a first half in which property values declined sharply, the second half of the year saw a strong rebound in our operational area of central London, with an upward revaluation of our portfolio from the half year of 9.8%. The net result was that, after a fall of 22.1% in 2008, the value of properties held throughout the year contracted by only 3.3% during 2009. This compares to a fall of 5.4% in the IPD Central London Offices Capital Growth Index.

Adjusted net asset value per share at 31st December 2009 was 1,168p against 1,226p a year earlier, a decrease of 4.7%.

Recurring profit before tax for the year, which excludes a number of items described in the finance review, was £60.2m against £23.3m in 2008. Consequently, recurring earnings per share rose to 55.55p from 22.83p. The board is proposing an increase in the final dividend of 15% to 18.85p which,

as a REIT, will all be paid as a Property Income Distribution on 17th June 2010 to shareholders on the register on 21st May 2010. Together with the interim dividend, which was maintained at 8.15p per share, this makes a total dividend for the year of 27.00p per share, an increase of 10% on 2008. This reflects the board's commitment to a progressive dividend policy balanced by prudent cash management.

The group continues to be in excellent financial health. Balance sheet gearing has been reduced to 62.2% from 71.2% a year earlier and unutilised, committed bank facilities increased to £425m as at 31st December 2009 from £291m last year. All financial covenants were exceeded comfortably throughout the year, a reflection of the attention given to our financing arrangements to ensure that we have a stable financial structure. This approach continues to be a key feature of the group's business model.

The board

As announced in September 2009, Chris Odom, our Finance Director for almost 22 years, has decided to retire and he will be leaving the company after the annual general meeting in May 2010. Chris has been a key member of both the board and the executive management team, overseeing the successful financing of the business through recession and expansion. We wish him well in his retirement. Chris's successor, Damian Wisniewski, joined the board on 1st February 2010 when Chris stepped down as a director. Damian has had considerable experience within the property sector and is a welcome addition to our well regarded management team.

Outlook

Economic indicators have yet to demonstrate a sustained recovery but rents within our central London villages have virtually stabilised and, for the first time since early 2008, an anticipation of rental growth is emerging. We have seen a significant recovery in property values in our operational area with yields reduced through a strong demand for investment property, albeit with bank finance to the real estate sector remaining in limited supply.

The strength and potential of our existing portfolio, and the resilience of its rental income, provide us with an engine for managed growth that can respond to the prevailing economic conditions. As the recovery of the central London economy appears to be gathering momentum, we continue to seek buildings where we can implement Derwent's distinctive brand of regeneration and are preparing to advance the timing of some of our schemes. I am confident that with their skills, flair and experience, your management team will continue to position the group successfully through the next phase of the central London property cycle.

R.A. Rayne
17th March 2010

Our market

Investor confidence returned during the second half of 2009

The UK economy officially left recession during the fourth quarter of 2009, supported by a combination of low interest rates, high government intervention and resilient consumer spending. Official figures from the Office for National Statistics, however, revealed that GDP growth in the fourth quarter was only 0.3%, indicating that the recovery is still fragile. This followed six quarters of economic decline and one of the deepest downturns on record. Overall, the UK economy contracted 5.0% in 2009 compared to growth of 0.5% in 2008 and 2.6% in 2007.

Now that economic recovery is tentatively under way, the health of London's economy is crucial for driving the UK's future growth. The capital city generates more than one fifth of the UK's economic output, is Europe's premier financial centre and is home to one of the most diverse, highly skilled and versatile labour pools in the world. London's cosmopolitan culture and vibrant lifestyle add to the city's long-term attractiveness to national and international occupiers.

This global city is our marketplace, in which we own and manage a diverse portfolio of innovative, intelligently designed yet affordable properties in a range of strategic central locations, with a particular focus on the West End.

Central London office occupier market

The central London office market comprises more than 20 million m² (216 million sq ft). Within this, 49% of stock is located in the City, 42% in the West End and 9% in Docklands. In general, the West End – the geographical focus of our business – has the broadest tenant base. The area is home to a vibrant mix of media companies, professional and business services firms and specialist fund management houses. In contrast, the City and Docklands have a narrower focus on banking, insurance and legal services.

Recent office space statistics from leading surveyors CB Richard Ellis (CBRE) highlight the positive impact of the economic turnaround on our market. While take-up of central London office space hit a 20-year low of 258,000m² during the first half of 2009, it rebounded to an above-average level of 581,000m² during the second half of the year.

CBRE's statistics also show trends in central London office vacancy rates that offer further reasons to be positive. Vacancies for the overall central London office market began 2009 at 5.3% and peaked at 7.7% in June, before falling to 7.2% by the end of the year. Looking at the second half of 2009 by sub-area, vacancy rates in the West End fell from 7.4% to 6.8%, while those in the City fell from 10.0% to 8.5%. This trend supports our strategy of delivering new office space to the market over the next few years. This strategy is reinforced by the fact that there has been little property development since the market slowdown and this is not expected to pick up in the near future with central London office completions estimated to total

382,000m² in 2010 and 100,000m² in 2011. Such levels are considerably lower than the long-term annual average of 504,000m².

Improved operating conditions are starting to translate into signs of rental stabilisation. Again, with our mid-market, West End focus, Derwent London is particularly well placed to benefit from this trend. At the year end, prime rents stood at £860 per m² (£80 per sq ft) in the West End and £475 per m² (£44 per sq ft) in the City. This compares to our competitive mid-market rental focus of £325-£540 per m² (£30-£50 per sq ft), which has proven more resilient to the effects of the downturn. We are now seeing a decrease in tenant incentives and believe that selective rental growth will return to our markets during 2010. The West End, where the supply-demand imbalance is most acute, and where the majority of our activities are focused, should experience the strongest market recovery. A new rating valuation takes effect from 1st April 2010 to be phased in over the next two to three years. This will increase tenants' total occupation costs. However, it is anticipated that the effect at Derwent London properties will be lower than at buildings in higher rental areas.

Central London office investment market

Investor confidence returned during the second half of 2009, with the lending market easing slightly, transaction levels improving, yields compressing and values rising. As a result, central London office investment transactions in the second half of 2009 totalled £4.7bn – substantially higher than the £2.3bn worth of transactions during the first half of the year and in line with the long-term average.

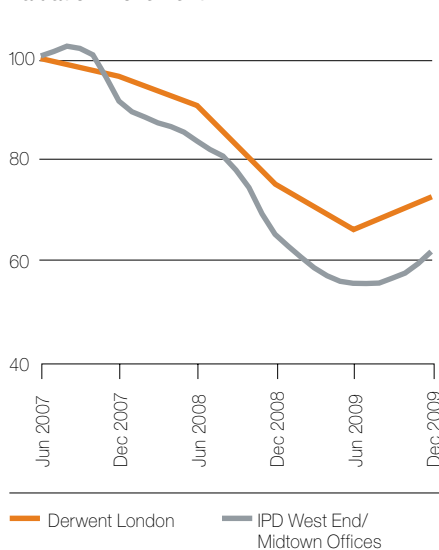
Early in 2009, the investment focus in London centred on properties secured on long-term income. However, with a limited supply of such assets, demand spread to a wider range of properties as the year progressed.

Attracted by the weakness of sterling, overseas buyers accounted for 73% of central London transactions in 2009 compared to the 10-year average of 49%. UK property companies comprised 11% of total activity, while domestic institutions accounted for 6%.

The IPD Monthly Property Index for West End/Midtown offices provides a clear illustration of the severity of capital value movements over the recent downturn. From peak to trough, over a 23-month period between August 2007 and July 2009, the index declined by approximately 45%. This adjustment was considerably quicker than that seen during the early 1990s recession, when the peak to trough period was 40 months and values declined by a similar amount.

The subsequent pick-up in values in the current cycle has been equally pronounced, with yield compression driving the above index up by more than 10% during the last five months of 2009.

Valuation movement¹



¹ June 2007 = 100

Our portfolio

Our property portfolio comprises 475,600m² (5.1 million sq ft) and is focused on designed, innovative central London offices, predominantly in the West End. This concentration plays to our core strengths: extensive experience, knowledge and expertise built up over time operating in these locations.

In total, the West End comprises 74% of our portfolio, with key ownerships in Fitzrovia, Victoria, Soho, Covent Garden, Noho and Belgravia. The City borders, including Clerkenwell and Holborn, account for 21% of our properties.

Our portfolio is let to nearly 600 tenants, which collectively generate an annualised net contracted rental income of £114.9m. Our two largest business sectors are representative of the tenant profile across the West End: professional and business services (30%) and media, television, marketing and advertising (23%). This dynamic tenant base has been particularly robust during the downturn, with rental default rates remaining at a low level throughout the year.

Other characteristics of our portfolio are a low void rate and affordable mid-market rents that have remained reversionary. It is a portfolio that holds substantial value-creating opportunities, the full potential of which will be realised through asset management and the delivery of quality space, through redevelopment, regeneration or refurbishment.

